

# The Audit Findings for Nottingham City Council

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Year ended 31 March 2019

29 July 2019



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The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed for the purpose of expressing our opinion on the financial statements. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose all defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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## Headlines

This table summarises the key findings and other matters arising from the statutory audit of Nottingham City Council ('the Council') and the preparation of the group and Council's financial statements for the year ended 31 March 2019 for those charged with governance.

<p><b>Financial Statements</b></p>	<p>Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the group and Council's financial statements:</p> <ul style="list-style-type: none"> <li>• give a true and fair view of the financial position of the group and Council and the group and Council's income and expenditure for the year; and</li> <li>• have been properly prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014.</li> </ul> <p>We are also required to report whether other information published together with the audited financial statements (including the Annual Governance Statement (AGS), Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</p>	<p>Our audit field work is substantially complete, however at the time of writing there remains a level of uncertainty in relation to the group accounts. This is because the auditor of Robin Hood Energy has not been able to conclude their audit of this subsidiary company. We are working with both officers and the other auditors to conclude this matter as soon as possible, but we are unable to give our opinion until this work is complete.</p> <p>Our audit work was completed on site during June and July. Our findings are summarised on pages 4 to 16.</p> <p>We have requested one material change to date in the draft accounts, in relation to the net pension liability. This primarily arose from the national McCloud pension issue, but also corrected for a material difference between estimated return on assets figures used by the actuary in the original report and the actual return reported at 31 March. The impact is to increase total expenditure in the Council and Group Comprehensive Income and Expenditure Statement by £15.3m and the net pension liability in the Balance Sheet by £30.3m.</p> <p>The draft financial statements and working papers were presented for audit in accordance with the agreed timetable of the end of May 2019 and were of a good standard..</p> <p>We have raised recommendations for management as a result of our audit work in Appendix A. The position against prior year recommendations made by the previous auditors (KPMG) is detailed in Appendix B. Audit adjustments are detailed in Appendix C.</p> <p>We have concluded that the other information to be published with the financial statements is consistent with our knowledge of your organisation and the financial statements we have audited.</p>
<p><b>Value for Money arrangements</b></p>	<p>Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report if, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('the value for money (VFM) conclusion').</p>	<p>We have not completed our risk based review of the Council's value for money arrangements, with work still outstanding in relation to the risk on the governance and monitoring of the Council's subsidiary companies – in part relating to the ongoing work on the position of RHE.</p> <p>We do not anticipate issuing the value for money conclusion prior to the 31 July. Our findings in relation to the two other significant risks are summarised on pages 17 to 22.</p>
<p><b>Statutory duties</b></p>	<p>The Local Audit and Accountability Act 2014 ('the Act') also requires us to:</p> <ul style="list-style-type: none"> <li>• report to you if we have applied any of the additional powers and duties ascribed to us under the Act; and</li> <li>• To certify the closure of the audit.</li> </ul>	<p>We have not exercised any of our additional statutory powers or duties to date, however this will remain under review until the work on the VFM conclusion has been completed and the audit has been certified as closed.</p> <p>We have completed the majority of work under the Code, however we will be unable to certify the completion of the audit until we complete the outstanding work on the opinion and VFM conclusion and the required work in relation to the Whole of Government Accounts return.</p>

# Summary

## Overview of the scope of our audit

This Audit Findings Report presents the observations arising from the audit that are significant to the responsibility of those charged with governance to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Its contents have been discussed with management and the Audit Committee.

As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK) and the Code, which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

## Audit approach

Our audit approach was based on a thorough understanding of the group business and is risk based, and in particular included:

- An evaluation of the group internal controls environment, including its IT systems and controls;
- An evaluation of the components of the group based on a measure of materiality considering each as a percentage of the group's gross revenue expenditure to assess the significance of the component and to determine the planned audit response. From this evaluation we determined the following:
  - Nottingham City Council is of course a significant component of the group, with a full scope UK statutory audit to be performed by Grant Thornton UK LLP
  - Bridge Estate Trust is not a significant component, but there are material balances at the group level, where we have assessed there to be a significant risk of material misstatement. We requested specific procedures to be carried out by the component auditor (Rogers Spencer) in relation to PPE balances. This is a change from the approach as communicated in the audit plan.
  - Nottingham City Homes is not a significant component, but there are material balances at the group level, where we have assessed there to be a significant risk of material misstatement. We requested specific procedures to be carried out by the component auditor (RSM) in relation to pension liabilities and PPE balances. This is a change from the approach as communicated in the audit plan.

- Nottingham City Transport Ltd is not a significant component but there are material balances at the group level, where we have assessed there to be a significant risk of material misstatement. We requested specific procedures to be carried out by the component auditor (BDO) in relation to turnover and PPE balances.
- Robin Hood Energy, while not a significant component, there are material balances at the group level, where we have assessed there to be a significant risk of material misstatement. We requested specific procedures to be carried out by the component auditor (BDO) in relation to turnover and operating expenses balances.
- Substantive testing on significant transactions and material account balances, including the procedures outlined in this report in relation to the key audit risks.

We have not had to alter or change our audit plan, as communicated to you on 22 February 2019, except for the additional audit procedures in relation to the group components as outlined about. A further review of the group arrangements identified that the transactions in relation to the subsidiary Futures Advice, Skills and Employment Ltd fell below the group materiality and therefore the risk in relation to this subsidiary reduced and therefore we have not asked the component auditor to perform any specified procedures, which is a change to our initial audit plan.

In addition, as part of our ongoing risk assessment, we have also added an additional significant risk in relation to the valuation of investment properties. Our work in this area is included on page 9.

## Conclusion

Our audit field work is substantially complete, however at the time of writing there remains a level of uncertainty in relation to the group accounts, This is because the auditor of Robin Hood Energy has not been able to conclude their audit of this subsidiary company. We are working with both officers and the other auditors to conclude this matter as soon as possible, however we are unable to give our opinion until this work is complete.

**Our approach to materiality**

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

Materiality calculations remain the same as reported in our audit plan. We detail in the table below our determination of materiality for Nottingham City Council.

	Group Amount (£)	Council Amount (£)	Qualitative factors considered
Materiality for the financial statements	18m	16m	<ul style="list-style-type: none"> <li>Materiality has been based on 1.75% of the Authority's gross expenditure</li> </ul>
Performance materiality	11.7m	10.4	<ul style="list-style-type: none"> <li>Our performance materiality has been set at 65% of our overall materiality</li> </ul>
Trivial matters	900k	800k	<ul style="list-style-type: none"> <li>This is set at 5% of financial statements materiality and reflects a level below which stakeholder are unlikely to be concerned by uncertainties.</li> </ul>
Materiality for senior officer remuneration		100k	<ul style="list-style-type: none"> <li>The senior officer remuneration disclosure in the statement of accounts has been identified as an area requiring lower materiality due to its sensitive nature</li> </ul>

# Significant findings – audit risks

Risks identified in our Audit Plan	Commentary
<p><b>1</b> <b>The revenue cycle includes fraudulent transactions</b></p> <p>Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.</p>	<p><b>Auditor commentary</b></p> <p>Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Authority, we have determined that the risk of fraud arising from revenue recognition can be rebutted in relation to the Council itself, because:</p> <ul style="list-style-type: none"> <li>• there is little incentive to manipulate revenue recognition</li> <li>• opportunities to manipulate revenue recognition are very limited, as the Council has a sound overall control environment.</li> <li>• The culture and ethical frameworks of local authorities, including Nottingham City Council, mean that all forms of fraud are seen as unacceptable</li> </ul> <p>Therefore we do not consider this to be a significant risk for Nottingham City Council. We have not been able to rebut the risk in relation for a number of the group companies where revenue recognition appears more susceptible to manipulation. Our work in relation to group companies remains ongoing at the time of writing this AFR.</p>
<p><b>2</b> <b>Management override of controls</b></p> <p>Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities. . The Authority faces external scrutiny of its spending, and this could potentially place management under undue pressure in terms of how they report performance.</p> <p>Management over-ride of controls is a risk requiring special audit consideration.</p>	<p><b>Auditor commentary</b></p> <p>We have:</p> <ul style="list-style-type: none"> <li>• Gained an understanding of the accounting estimates, judgements applied and decisions made by management and consider their reasonableness;</li> <li>• obtained a full listing of journal entries, identify and test unusual journal entries for appropriateness; and</li> <li>• evaluated the rationale for any changes in accounting policies or significant unusual transactions</li> </ul> <p><b>Findings</b></p> <p>Our work to date has not identified any issues in respect of the management override of controls. The fieldwork is complete in this area, and awaiting our quality review processes.</p>

# Significant findings – audit risks

## Risks identified in our Audit Plan

## Commentary

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### Valuation of property, plant and equipment

The Authority revalues its land and buildings on an five year rolling programme basis to ensure that the carrying value is not materially different from fair value. This represents a significant estimate by management in the financial statements.

We identified the valuation of land and buildings revaluations and impairments as a risk requiring special audit consideration and a key audit matter.

### Auditor commentary

We have:

- Reviewed management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work;
- considered the competence, expertise and objectivity of any management experts used;
- reviewed the basis on which the valuation is carried out and challenged the key assumptions;
- reviewed and challenged the information used by the valuer to ensure it is robust and consistent with our understanding;
- tested revaluations made during the year to ensure they are input correctly into the Council's asset register; and
- evaluated the assumptions made by management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value.

### Findings

Our fieldwork in this area is substantially complete and is awaiting our quality review checks to be completed. We will provide a verbal update on this area to the audit committee.

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### Valuation of pension fund net liability

The Authority's pension fund asset and liability as reflected in its balance sheet represent a significant estimate in the financial statements.

We identified the valuation of the pension fund net liability as a risk requiring special audit consideration and a key audit matter.

### Auditor commentary

We have:

- Identified the controls put in place by management to ensure that the pension fund liability is not materially misstated. We will also assess whether these controls were implemented as expected and whether they are sufficient to mitigate the risk of material misstatement;
- evaluated the competence, expertise and objectivity of the actuary who carried out your pension fund valuation. We will gain an understanding of the basis on which the valuation is carried out, including what considerations the actuary has made in relation to asset valuation at the balance sheet date due to the impact of Brexit.
- undertaken procedures to confirm the reasonableness of the actuarial assumptions made; and
- checked the consistency of the pension fund asset and liability and disclosures in notes to the financial statements with the actuarial report from your actuary

### Findings

We have worked with officers to ensure an appropriate resolution is reached in relation to the McCloud ruling. The Council have obtained a revised actuarial report and made the amendments to the draft financial statements. This revised actuarial estimate also used an updated figure for the rate of return on pension assets – the original report used an estimated figure of approximately 10% used in the actuary's original report was based on an estimate return before the year end, whereas the actual reported return was 1% lower than this. Both of these figures also include approximately 4% which is a correct of an overestimate made in the 2017/18 actuary's report.

# Significant findings – audit risks

## Risks identified in our Audit Plan

## Commentary

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### Accounting of Private Finance Initiative (PFI) schemes

### Auditor commentary

The Authority has a number of complex PFI schemes, the largest and most complex being in relation to the tram network. This being the first year of our audit, we will need to understand these arrangements and obtain evidence to ensure there is no material misstatement in the financial statements.

We identified the accounting for PFI schemes as a risk requiring special audit consideration and a key audit matter.

We have:

- Reviewed the accounting treatment of all material PFI schemes and ensure disclosures in the financial statements are in accordance with Code requirements.

### Findings

Our work to date has not identified any issues in respect of PFI. The fieldwork is complete in this area, and awaiting our quality review processes.

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### Preparation of group accounts

### Auditor commentary

The Authority has a relatively complex group structure. In 2017/18 the Authority consolidated within its group accounts, six subsidiaries, two joint ventures and one trust fund.

There are a number of logistical challenges that need to be managed, ensuring that any third parties (subsidiaries and subsidiary auditors) involved in the production of the accounts are aware of the arrangements to provide the output of their work in accordance with the closedown timetable.

We identified the preparation of group accounts as a risk requiring special audit consideration and a key audit matter.

We have:

- Reviewed consolidation procedures in place at the Authority, and the Authority's assessment of all entities over which the Authority has control or significant influence and the Authority's subsequent consideration whether or not to consolidate each entity within the group accounts;
- Liaised formally with group auditors to enable us to make use of the outcomes of their audit (including their opinion) for our audit opinion on the Authority's group accounts; and
- Agreed the final accounts consolidation back to audited financial statements for each subsidiary, joint venture and trust fund consolidated within the group accounts

### Findings

Our work remains ongoing in this area due to the nature of the issues in relation to Robin Hood Energy and Nottingham City Homes.

# Significant findings – audit risks

## Risks identified in our Audit Plan

### Valuation of Investment Properties

The Authority revalues its Investment Properties on an annual basis, however there have been significant additions to the portfolio this year. The valuation of investment properties represents a significant estimate by management in the financial statements.

We identified the valuation of Investment Properties as a risk requiring special audit consideration.

## Commentary

### Auditor commentary

We have:

- Reviewed management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work;
- considered the competence, expertise and objectivity of any management experts used;
- reviewed the basis on which the valuation is carried out and challenge the key assumptions, including the consideration of the potential impact of Brexit on asset values at year end;
- reviewed and challenge the information used by the valuer to ensure it is robust and consistent with our understanding; and
- tested revaluations made during the year to ensure they are input correctly into the Council's asset register.

### Findings

Our work remains ongoing in this area, and we will provide a verbal update at the audit committee.

## Significant findings arising from the group audit

Component	Component auditor	Findings	Group audit impact
<b>Bridge Estate Trust</b>	Rogers Spencer	<ul style="list-style-type: none"> <li>An unqualified audit opinion of Bridge Estate Trust was issued by Rogers Spencer on 18 July 2019. No significant issues were identified.</li> </ul>	We have reviewed the working papers of the component auditor for the areas where the audit team are seeking to place reliance on their work. We have gained sufficient assurance over the balances as required.
<b>Nottingham City Homes</b>	RSM	<ul style="list-style-type: none"> <li>An unqualified audit opinion on Nottingham City Homes was issued by RSM on 1 July 2019. The audit identified no significant issues.</li> </ul>	We have reviewed the working papers of the component auditor, and raised a number of queries about the work that has been performed and how that impacts on the group consolidation. As part of this work we have identified an unadjusted error in the Group financial statements; further information is included on page 29. We continue to work with RSM to understand the extend of the procedures they have performed on material group balances.
<b>Nottingham City Transport</b>	BDO	<ul style="list-style-type: none"> <li>An unqualified audit opinion on Nottingham City Transport was issued by BDO on 14 June 2019.</li> </ul>	We are awaiting a formal response from BDO in relation to our group auditor communications. We will work with BDO auditors to secure a formal response and also arrange to review the working papers that support the identified group balances.
<b>Robin Hood Energy</b>	BDO	<ul style="list-style-type: none"> <li>The audit of Robin Hood Energy has not yet been completed</li> </ul>	We are unable to sign off the group financial statements until the audit of Robin Hood Energy has been completed, and we have considered the impact of their findings on the subsidiary company in relation to both the Group and single entity accounts.

## Significant findings – key judgements and estimates

Accounting area	Summary of management's policy	Audit Comments	Assessment
<b>Land and Buildings – Council Housing - £1,000m</b>	The Council owns 25,535 dwellings and is required to revalue these properties in accordance with DCLG's Stock Valuation for Resource Accounting guidance. The guidance requires the use of beacon methodology, in which a detailed valuation of representative property types is then applied to similar properties. The Council has engaged Freeman Mitchell to complete the valuation of these properties. The year end valuation of Council Housing was £1,000m, a net increase of £79m from 2017/18	<ul style="list-style-type: none"> <li>We have assessed Freeman Mitchell as the valuer appointed for Council Houses and consider them to be competent, capable and objective</li> <li>We have carried out completeness and accuracy testing of the underlying information provided to the valuer to determine the estimate and have no issues to report.</li> <li>We confirmed the valuation method remains consistent with the prior year and assessed the reasonableness of the estimates made by management.</li> <li>We have tested that properties are included in the correct beacon, and that the valuations used are appropriate.</li> </ul>	
<b>Land and Buildings – Other - £894m</b>	<p>Other land and building comprises £894 million of specialised assets such as schools and libraries, which are valued at current value, which is the amount that would be paid for the asset in its existing use. Where insufficient market based evidence of current value is available because the asset is considered to be specialised a depreciated replacement cost basis has been applied.</p> <p>The Council use an internal valuer to complete asset valuations on a rolling programme, ensuring that all assets carried at current value are revalued at least every 5 years. In addition, the internal valuers complete reviews outside of this cycle where there has been evidence of a significant change, such as capital investment of material impairment. A desktop review is also carried out for all assets not revalued in year, and where evidence suggests a potential material difference further valuations are carried out to ensure that the year end carrying value is materially correct.</p> <p>86% (by value) of other land and buildings has been revalued in the current year, resulting in a net revaluation gain of £102m.</p>	<ul style="list-style-type: none"> <li>We have assessed the Council's internal valuer and consider them to be competent, capable and objective.</li> <li>We have carried out completeness and accuracy testing of the underlying information provided to the valuer to determine the estimate and have no issues to report.</li> <li>We confirmed the valuation method remains consistent with the prior year and assessed the reasonableness of the estimates made by management in determining the movement of assets that have not been revalued in the current year.</li> </ul>	

### Assessment

-  We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
-  We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
-  We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
-  We consider management's process is appropriate and key assumptions are neither optimistic or cautious

## Significant findings – key judgements and estimates

	Summary of management's policy	Audit Comments	Assessment
<b>Net pension liability – £722m</b>	<p>The Council's net pension liability at 31 March 2019 as per the draft financial statements is £772m (prior year £782m) comprising the Nottinghamshire County Council Pension Fund Local Government defined benefit pension scheme obligations.</p> <p>The Council uses Barnett Waddingham to provide actuarial valuations of the Council's assets and liabilities derived from this scheme. A full actuarial valuation is required every three years. The latest full actuarial valuation was completed in 2016. A roll forward approach is used in intervening periods, which utilises key assumptions such as life expectancy, discount rates, salary growth and investment returns. Given the significant value of the net pension fund liability, small changes in assumptions can result in significant valuation movements. There has been a £20m actuarial gain during 2018/19.</p>	<ul style="list-style-type: none"> <li>• We have assessed the Council's actuary to be competent, capable and objective</li> <li>• We have performed additional tests in relation to the actuary on contribution figures, benefits paid and investment returns to gain assurance over the 2018/19 roll forward calculation carried out by the actuary. We are working through one issue in relation to benefit payments at the time of writing this report.</li> <li>• The Council has considered that the impact of GMP equalisation is not material to the Statement of Accounts. Based on our review of this area, we concur with this view.</li> <li>• As highlighted throughout this report the net pension liability has increased as a result of a legal case (McCloud), which has national implications.</li> </ul>	●

### Assessment

- We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
- We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
- We consider management's process is appropriate and key assumptions are neither optimistic or cautious

# Significant findings – matters discussed with management

This section provides commentary on the significant matters we discussed with management during the course of the audit.

Significant matter	Commentary	Auditor view
<p><b>1 Potential impact of the McCloud judgement</b></p> <p>The Court of Appeal has ruled that there was age discrimination in the judges and firefighters pension schemes where transitional protections were given to scheme members.</p> <p>The Government applied to the Supreme Court for permission to appeal but this has now been denied by the High Court.</p> <p>The decision as to the appropriate accounting treatment is one for the Council, but our national technical advice is that we are expecting this adjustment to be made to the accounts if the estimated increase in liabilities is material.</p> <p>The legal ruling around age discrimination (McCloud - Court of Appeal) has implications not just for pension funds, but also for other pension schemes where they have implemented transitional arrangements on changing benefits.</p>	<p>This issue has been an emerging issue following receipt of the draft financial statements and it is one that by its nature is sector wide. We have been working with management to determine the most effective way to deal with this issue, recognising that pension estimates are high value, complex and important figures within the financial statements. As a result they require an appropriate degree of focus and challenge from both management and auditors alike.</p> <p>We have asked management to work with their actuary to gain the necessary information to determine whether the potential impact of this judgement would have a material impact to the financial statements.</p> <p>Management have commissioned an updated valuation from the actuary, to take account of the impact of McCloud and also to update the report to take account of the actual rate of return on assets, rather than an estimated position which was used in the original report used for the draft financial statements.</p>	<p>Officers have demonstrated that the impact of the revised actuary report is to increase past service liabilities by £15.3. While not material, given the magnitude of these amendments the Council have amended the draft financial statements for these movements.</p> <p><b>Management response</b></p> <ul style="list-style-type: none"> <li>[...]</li> </ul>
<p><b>2 Disclosure of the performance of group companies</b></p> <p>We have flagged with officers that the current disclosures in the draft financial statements do not meet the requirements of the Code.</p>	<p>The disclosure requirements of the Code are such that the reporting authority needs to disclose information that enables users of its financial statements to evaluate;</p> <ul style="list-style-type: none"> <li>The nature of, and risks associated with, its interests in other entities, and</li> <li>The effects of those interests on its financial position, financial performance and cash flows.</li> </ul> <p>We have discussed with officers the need to improve the disclosures.</p>	<p><b>Auditor view</b></p> <ul style="list-style-type: none"> <li>Officers are working on the improved disclosures required.</li> </ul> <p><b>Management response</b></p> <ul style="list-style-type: none"> <li>[...]</li> </ul>

# Going concern

## Our responsibility

As auditors, we are required to “obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern” (ISA (UK) 570).

## Going concern commentary

### Management's assessment process

The Chief Financial Officer as s151 officer has a reasonable expectation that the Council will continue for the foreseeable future. Members concur with this view. For this reason, the Council continues to adopt the going concern basis in preparing the financial statements.

Management have confirmed that:

- they have taken into account all available information about the future, which is at least, but is not limited to, twelve months from the date when the financial statements are authorised for issue.
- no material uncertainties related to events or conditions that cast significant doubt upon the Council's ability to continue as a going concern exist that require disclosure

### Auditor commentary

Chapter 6 Section 3.4 of the CIPFA Code on the “*Presentation of Financial Statements for Pension Funds*” notes going concern as a particularly important reporting requirement and that para 3.4.2.23 of the Code applies. The CIPFA Code of Practice 2017/18 Code para 3.4.2.23 states “Local authorities that can only be discontinued under statutory prescription shall prepare their financial statements on a going concern basis of accounting; that is, the financial statements shall be prepared on the assumption that the functions of the authority will continue in operational existence for the foreseeable future”.

Management have carried out an assessment in respect of the going concern of the Council and have identified:

- The Council produce financial plans and budgets for members to approve, which continue into the medium term,
- The plans include an assessment of the level of balances and reserves held by the Council, with the Chief Financial Officer considers to be sufficient,
- The Council do monitoring of the cash position and this has been estimated going forward to cover the 12 months from the date of approval to the financial statements. This shows the Council have appropriate cash balances.

As such we consider that the preparation of accounts on a going concern basis is a reasonable and valid one and there are no indications of material uncertainty.

### Work performed

We have reviewed the:

- Written assessment provided by management, including the supporting documentation provided, and
- The cash flow forecast which covers 12 months from the date of approval of the financial statements.

### Auditor commentary

Our audit did not identify any events or conditions which may cast significant doubt on the going concern assumption.

### Concluding comments

### Auditor commentary

We propose to issue an unmodified opinion for 2018/19

## Other communication requirements

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

Issue	Commentary
1 <b>Matters in relation to fraud</b>	<ul style="list-style-type: none"> <li>We have previously discussed the risk of fraud with the Audit Committee and have not been made aware of any other incidents in the period and no other issues have been identified during the course of our audit procedures.</li> </ul>
2 <b>Matters in relation to related parties</b>	<ul style="list-style-type: none"> <li>We are not aware of any related parties or related party transactions which have not been disclosed</li> </ul>
3 <b>Matters in relation to laws and regulations</b>	<ul style="list-style-type: none"> <li>You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.</li> </ul>
4 <b>Written representations</b>	<ul style="list-style-type: none"> <li>A letter of representation has been requested from the Council.</li> </ul>
5 <b>Confirmation requests from third parties</b>	<ul style="list-style-type: none"> <li>We requested from management permission to send confirmation requests to all institutions where the Council holds case or investment balances and those who lend the Council money. This permission was granted and the requests were sent. We have received positive confirmation in all cases, except for Lloyds bank. We are working with officers to gain the necessary third party assurance.</li> <li>We requested from management permission to send confirmation requests to the pension fund auditor. This permission was granted and the requests were sent. We have not yet received the final response from the pension fund audit and we will require this prior to issuing our opinion.</li> </ul>
6 <b>Disclosures</b>	<ul style="list-style-type: none"> <li>Our initial review of the draft financial statements identified some omissions in the financial statements. We have made recommendations to assist the Council in achieving greater compliance with the Code. Where disclosure amendments have been made to the statement of accounts, these are set out in Appendix C.</li> </ul>
7 <b>Audit evidence and explanations/significant difficulties</b>	<ul style="list-style-type: none"> <li>All information and explanations requested from management was provided.</li> </ul>

## Other responsibilities under the Code

Issue	Commentary
① <b>Other information</b>	<ul style="list-style-type: none"> <li>We are required to give an opinion on whether the other information published together with the audited financial statements (including the Annual Governance Statement and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</li> <li>Inconsistencies have been identified but have been adequately rectified by management. We plan to issue an unmodified opinion in this respect</li> </ul>
② <b>Matters on which we report by exception</b>	<p>We are required to report on a number of matters by exception in a numbers of areas:</p> <ul style="list-style-type: none"> <li>If the Annual Governance Statement does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the other information of which we are aware from our audit</li> <li>If we have applied any of our statutory powers or duties</li> </ul> <p>We have nothing to report on these matters to date, however are awaiting the outcome of our work on company governance before concluding our work in this area.</p>
③ <b>Specified procedures for Whole of Government Accounts</b>	<p>We are required to carry out specified procedures (on behalf of the NAO) on the Whole of Government Accounts (WGA) consolidation pack under WGA group audit instructions.</p> <p>As the Council exceeds the specified group reporting threshold of we examine and report on the consistency of the WGA consolidation pack with the Council's audited financial statements.</p> <ul style="list-style-type: none"> <li>Note that work is not yet completed and the planned timescale for the work has been agreed with the Council to meet the statutory deadline.</li> </ul>
④ <b>Certification of the closure of the audit</b>	<p>We are unable to certify the closure of the 2018/19 audit of Nottingham City Council at this stage, as work is outstanding.</p>

## Independence and ethics

- We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. The firm, its partners, senior managers, and managers have complied with the Financial Reporting Council's Ethical Standards and confirm that we are independent and are able to express an objective opinion on the financial statements.
- We wish to highlight a judgement that we have made in relation to the independence of a member of the audit team. The audit member has a brother who is employed by Nottingham City Council. The brother's role is not in senior management, nor of a financial oversight role, therefore we have determined that he does not pose a significant independence threat to the audit. In addition, he does not meet the definition of a person 'closely associated' under the ethical standards but is still a close family member. In consultation with our internal ethics team, we have agreed appropriate safeguards to ensure our independence is not compromised, which includes informing the whole audit team of the relationship, so that in the unlikely event that a transaction that relates to the brother is selected for audit testing, then this member of the audit team would have no involvement in its scrutiny or review.
- We confirm that we have implemented policies and procedures to meet the requirement of the Financial Reporting Council's Ethical Standard.
- We have received confirmation that BDO, RSM and Rogers Spencer are all independent.
- We have received confirmation that Barnett Waddingham LLP is independent.

We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements.

Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in December 2017 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

Details of fees charged are detailed in Appendix D

# Independence and ethics

## Non-audit services

For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The following non-audit services were identified, as well as the threats to our independence and safeguards that have been applied to mitigate these threats.

	Fees £	Threats identified	Safeguards
<b>Audit related</b>			
<b>Certification of Housing Benefit Grant Claim</b> While we have not been formally engaged to complete this audit, we have had discussions with officers of likelihood of us completing this work for 2018/19.	TBC	Self- Interest (because this is a recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work in comparison to the total fee for the audit, and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level.
<b>Certification of Teachers' Pension return</b> While we have not been formally engaged to complete this audit, we have had discussions with officers of likelihood of us completing this work for 2018/19.	TBC	Self-Interest (because this is a recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is low in comparison to the total fee for the audit of £132,531 and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level.
<b>Non-audit related</b>			
<b>CFO Insights</b>	10,000	Self-Interest	This is a subscription for the CFO insights tool and represents the renewal for the third year of the contract. This is a recurring fee and therefore a small self interest threat exists. However, the level of this recurring fee taken on its own is not considered to be a significant threat to independence as the fee for this work in comparison to the total fee for the audit £132,531 for the Authority and in particular to Grant Thornton UK LLP overall turnover. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level.

## Follow up of prior year recommendations

The prior year auditor identified the following issues in the audit of Nottingham City Council's 2017/18 financial statements. We have considered the progress the Council has made against these recommendations in the context of our audit, and commented below.

Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
✓	<p>Sustainable financial budget</p> <p>CLT needs to monitor the financial position within 2018/19 and work together to deliver solutions to any issues that arise. Whenever non-recurrent measures are used to address recurrent issues there should be a clear plan as to the proposed solution for the future.</p>	<ul style="list-style-type: none"> <li>The approach taken to the sustainability of the financial budget has been reviewed as part of the VFM conclusion. See page 19 for further details.</li> </ul>
✓	<p>Group Governance Arrangements</p> <p>The Authority should ensure that the new group governance framework is in place by September 2019</p>	<ul style="list-style-type: none"> <li>A report was taken to the Audit Committee in February 2019 which updated the position on governance of group companies. New arrangements were put in place that were implemented from May 2019.</li> </ul>
✓	<p>Capital Investment Strategy</p> <p>The Authority should develop and appropriately approve a capital investment strategy document as soon as possible, given the growth of its investment property portfolio and associated borrowing costs.</p>	<ul style="list-style-type: none"> <li>The Capital Investment Strategy has been taken to the Executive Board in February 2019</li> </ul>
✓	<p>Journals Authorisation</p> <p>The Authority should investigate and seriously consider the implementation of electronic journal authorisation within the new general ledger system.</p>	<ul style="list-style-type: none"> <li>As part of our work on journals during 2018/19 we have also noted that there is no journal authorisation process in place. We note that officers are looking at this in relation to the implementation of the new system, with some form of journal authorisation anticipated.</li> </ul>
✓	<p>Capital Cut-Off</p> <p>The Authority should review its process for capturing and accounting for capital accruals, to ensure costs are capitalized in the correct period, notably in relation to internally delivered schemes.</p>	<ul style="list-style-type: none"> <li>Our testing has not identified any issues in relation to capital cut off.</li> </ul>

## Follow up of prior year recommendations

Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
✓	Capitalising project management costs and surplus recovery fees The authority should review how it calculates its capitalised project management costs, and review the basis of the 'surplus recovery fee'	<ul style="list-style-type: none"> <li>Our testing has not identified any issues in relation to capitalisation</li> </ul>
✓	Documenting senior review and approval of actuarial assumptions Actuarial assumptions should be reviewed and signed off by senior management at the Authority before the production of draft accounts.	<ul style="list-style-type: none"> <li>We have reviewed the arrangements around approval of actuarial assumptions as part of our work on pension liabilities and have no issues to raise.</li> </ul>
✓	Environenergy The Authority should review and confirm that the service level agreement it has with Environenergy is still fit for purpose. The bad debt provision against Environenergy should be reviewed.	<ul style="list-style-type: none"> <li>Officers have confirmed that the bad debt provision (now effectively called the loss allowance under IFRS 9) has been reviewed and adjusted,</li> </ul>
X	IT security policy The IT security policy should be reviewed annually as determined by the Authority.	<ul style="list-style-type: none"> <li>The IT security policy on the intranet is still dated March 2015.</li> </ul>
	<p>IT access recommendations</p> <p>The prior year auditor made further recommendations around IT access review. We have not specifically followed these up as we have undertaken our own review of the IT control environment. While a separate report has been produced and agreed with management, none of the recommendations are considered significant enough to warrant reporting to those charged with governance.</p>	

### Assessment

- ✓ Action completed
- X Not yet addressed

# Audit Adjustments

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

## Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the key statements and the reported net expenditure for the year ending 31 March 2019.

Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000
1 Following a review of the McCloud judgement, the Council have worked with their actuary to revise their estimate in respect of pension liabilities. The impact of this is to increase past service liabilities by £15.280m	30,349	30,349	15.333
<b>Overall impact</b>	<b>£30,349</b>	<b>£30,349</b>	<b>£15,333</b>

## Impact of unadjusted misstatements

The table below provides details of adjustments identified during the 2018/19 audit which have not been made within the final set of financial statements. The Audit Committee is required to approve management's proposed treatment of all items recorded within the table below:

Detail	Reason for not adjusting
1 At the group level the Council consolidate the balances from Nottingham City Homes. In reviewing the auditors working papers it was identified that the impact of the McCloud decision had not been taken into account. Officers at the Council have estimated the potential impact of this for Nottingham City Homes and therefore the consolidated group position. The likely impact for Nottingham City Homes pension liability is estimated to be an increase of £3.825m	The balance is not material
<b>Overall impact</b>	

# Audit Adjustments

## Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Disclosure omission	Detail	Adjusted?
<b>Presentation and disclosure</b>	<p>This year has been the first year we have worked with the Council, and as a result we have undertaken a detailed review of the draft accounts. While overall the accounts are considered to have a high degree of compliance with the Code, we have identified a number of areas where improvements could be made. In particular additional disclosure has been made in relation to the following items;</p> <ul style="list-style-type: none"> <li>• Fair Value of surplus assets.</li> <li>• Inclusion of an accounting policy in relation to a de minimus level for accruals</li> <li>• Pooled budgets</li> </ul> <p>In addition, the previously separate critical and other accounting policies have been brought together within the document.</p>	Yes
<b>Critical Judgements</b>	<p>The critical judgements presented in the draft financial statements in a number of cases were either not material to the financial statements, or did not clearly articulate what judgement management had made in relation to applying their accounting policies. The FRC recently carried out a thematic review in this area, and highlighted that in many cases disclosures in relation to critical judgements were not sufficient.</p> <p>Officers have amended the note in the final version of the accounts. There remain some disclosures that the audit team do not consider material or critical judgements, however the Council have chosen to disclose these due to the complexities associated with the balances. The audit team consider this a reasonable approach.</p>	Yes

# Audit Adjustments

## Misclassification and disclosure changes continued

Disclosure omission	Detail	Adjusted?
<b>Estimates</b>	<p>As for critical judgements, the FRC recently carried out a thematic review in this area, and highlighted that in many cases disclosures in relation to estimates were not clear enough.</p> <p>Officers have agreed to remove the disclosures in relation to both the NNDR provision and Council Dwellings. In addition some further narrative has been made to the PFI disclosure to highlight the associated sensitivities.</p>	Yes
<b>Financial Instruments</b>	<p>2018/19 saw the introduction of IFRS 9 in relation to financial instruments. This was a fundamental accounting change. The Council has reviewed the Code and associated guidance notes and generally made the appropriate disclosures within the accounts. As this is the first year of the standard it is inevitable that improvements could be made. Officers have made amendments to improve the disclosures, however this is an area that requires improvement in futures years. We do not consider this a material omission for the purpose of the opinion.</p>	Yes
<b>CIES comparatives</b>	<p>Each year the portfolios that the Council use to report against are re-aligned. The impact of this is that the CIES needs to be restated, as well as the EFA and its supporting notes. We recommended that officers improve the disclosure for the restatement and they have made the adjustments.</p>	Yes

## Fees

We confirm below our final proposed fees charged for the audit and provision of non-audit services.

Audit fee	Planned 2018/19 fee	Final 2018/19 fee
<b>Council Audit</b>	£132,531	132,531
<b>Additional Audit Fee</b>		TBC
<b>Total audit fees (excl VAT)</b>	<b>£132,531</b>	<b>TBC</b>

Due to the complexity of a number of the issues on the audit, we have discussed with the s151 officer the need to charge additional fees to cover the cost of the audit work associated with them. As the audit remains ongoing we are yet to be able to conclude what these overrun fees will be. Any additional audit fees will be agreed with the s151 officer prior to agreements by PSAA.

The fees reconcile to the financial statements as per the reconciliation below.

- fees per financial statements £166k
- reconciling item – certification of housing benefit in relation to prior years £12k
- reconciling item – certification of other claims and returns in relation to prior years £11k
- reconciling item – fees for other audit services £10k
- total fees per above £133k

### Non Audit Fees

Fees for other services	Fees
<b>Audit related services:</b>	
• Certification of Housing Benefit Grant Claim	TBC
• Certification of teachers' pension return	TBC
<b>Non-audit services</b>	
• CFO Insights	£10,000
	<b>TBC</b>



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