



# The Annual Audit Letter for Torbay Council

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**Year ended 31 March 2016**

OCTOBER 2016

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# Executive summary

## **Purpose of this letter**

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at Torbay Council (the Council) for the year ended 31 March 2016.

This Letter is intended to provide a commentary on the results of our work to the Council and its external stakeholders, and to highlight issues that we wish to draw to the attention of the public. In preparing this letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice (the Code) and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'.

We reported the detailed findings from our audit work to the Council's Audit Committee as those charged with governance in our Audit Findings Report on 27 July 2016.

## **Our responsibilities**

We have carried out our audit in accordance with the NAO's Code of Audit Practice, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

- give an opinion on the Council's financial statements (section two)
- assess the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources (the value for money conclusion) (section three).

In our audit of the Council's financial statements, we comply with International Standards on Auditing (UK and Ireland) (ISAs) and other guidance issued by the NAO.

## **Our work**

### **Financial statements opinion**

We gave an unqualified opinion on the Council's financial statements on 28 July 2016.

This is a credit to the Finance team as the timetable was a week earlier than in 2014/15 enabling an early audit start date of 6 June 2016 with reporting to the Audit Committee at the end of July.

### **Value for money conclusion**

We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources during the year ended 31 March 2016 except for the matters reported in the Ofsted report on the Council's Childrens Services issued in January 2016. We concluded that these matters were weaknesses in proper arrangements for understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management, and for planning, organising and developing the workforce effectively to deliver strategic priorities.

We therefore qualified our value for money conclusion in our audit opinion on 28 July 2016.

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## **Certificate**

We certified that we had completed the audit of the accounts of Torbay Council in accordance with the requirements of the Code on 28 July 2016.

## **Certification of grants**

We also carry out work to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. Our work on this claim is not yet complete and will be finalised by 30 November 2016. We will report the results of this work to the Audit Committee in our Annual Certification Letter.

## **Other work completed**

We provided your teams with training on financial accounts and annual reporting. We also held a seminar on accounting for the Better Care Fund and Pooled Budgets, a new area in 2015/16.

## **Working with the Council**

During the year we have delivered a number of successful outcomes with you:

- An efficient audit –delivery of the accounts audit two months before the deadline
- VFM - we provided you with assurance and feedback on your arrangements for delivering efficiency, effectiveness and economy.
- Sharing our insight – we provided regular audit committee updates covering best practice. We also shared our sector insight via our National Reports.

We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Council's staff.

**Grant Thornton UK LLP**  
**October 2016**

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# Audit of the accounts

## **Our audit approach**

### **Materiality**

In our audit of the Council's accounts, we use the concept of materiality to determine the nature, timing and extent of our work, and in evaluating the results of our work. We define materiality as the size of the misstatement in the financial statements that would lead a reasonably knowledgeable person to change or influence their economic decisions.

We determined materiality for our audit of the Council's accounts to be £5,524,000, which is 1.95% of the Council's gross revenue expenditure. We used this benchmark, as in our view, users of the Council's accounts are most interested in how it has spent the income it has raised from taxation and grants during the year.

We also set a lower level of specific materiality for senior officer remuneration.

We set a lower threshold of £276,000, above which we reported errors to the Audit Committee in our Audit Findings Report.

### **The scope of our audit**

Our audit involves obtaining enough evidence about the amounts and disclosures in the financial statements to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error.

This includes assessing whether:

- the Council's accounting policies are appropriate, have been consistently applied and adequately disclosed;
- significant accounting estimates made by management are reasonable; and
- the overall presentation of the financial statements gives a true and fair view.

We also read the Narrative Report and Annual Governance Statement to check they are consistent with our understanding of the Council and with the accounts on which we give our opinion.

We carry out our audit in line with ISAs (UK and Ireland) and the NAO Code of Audit Practice. We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach was based on a thorough understanding of the Council's business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks and the results of this work.

# Audit of the accounts

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk
<p><b>Valuation of property plant and equipment</b></p> <p>The Council revalues its assets on a rolling basis over a five year period. The Code requires that the Council ensures that the carrying value at the balance sheet date is not materially different from the current value. This represents a significant estimate by management in the financial statements.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Reviewed management's processes and assumptions for the calculation of the estimate.</li> <li>• Reviewed the competence, expertise and objectivity of any management experts used.</li> <li>• Reviewed the instructions issued to valuation experts and the scope of their work</li> <li>• Discussed with the Council's valuer the basis on which the valuation was carried out, challenging the key assumptions.</li> <li>• Reviewed and challenged the information used by the valuer to ensure it was robust and consistent with our understanding.</li> <li>• Tested revaluations made during the year to ensure they were input correctly into the Council's asset register</li> <li>• Evaluated the assumptions made by management for those assets not revalued during the year and how management satisfied themselves that these were not materially different to current value.</li> </ul> <p><b>We did not identify any issues to report</b></p>
<p><b>Valuation of pension fund net liability</b></p> <p>The Council's pension fund asset and liability as reflected in its balance sheet represent significant estimates in the financial statements.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Documented the key controls that were put in place by management to ensure that the pension fund liability was not materially misstated.</li> <li>• Walked through the key controls to assess whether they were implemented as expected and mitigate the risk of material misstatement in the financial statements.</li> <li>• Reviewed the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation.</li> <li>• Gained an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made.</li> <li>• Reviewed the consistency of the pension fund asset and liability and disclosures in notes to the financial statements with the actuarial report from your actuary.</li> </ul> <p><b>We did not identify any issues to report</b></p>

# Audit of the accounts (Continued)

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk
<p><b>One-off/unusual transactions</b></p> <p>New PFI scheme - The Council is in partnership with Devon County Council and Plymouth City Council in an Energy from Waste (EfW) PFI scheme.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"><li>• Gained an understanding of the transaction including a review of supporting documentation</li><li>• Carried out a detailed assessment of whether the proposed accounting treatment for the scheme was in accordance with the accounting standards and was based on reasonable judgements by management, supported by the contract documentation</li><li>• Reviewed whether the PFI operator's financial model was producing reliable figures by entering the figures into the model used by Grant Thornton and comparing the results.</li><li>• Carried out testing of the transactions in the financial statements to ensure they were consistent with our understanding</li><li>• Reviewed the accounting entries to ensure they complied with the requirements of the CIPFA Code of Practice</li></ul> <p><b>Our audit work concluded that:</b></p> <ul style="list-style-type: none"><li>➤ <b>the accounting treatment for the scheme was reasonable</b></li><li>➤ <b>the figures produced by the PFI operator's financial model were materially accurate</b></li><li>➤ <b>The transactions in the financial statements were consistent with the financial model and our understanding, and</b></li><li>➤ <b>The accounting entries were compliant with the Code.</b></li></ul>

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# Audit of the accounts

## **Audit opinion**

We gave an unqualified opinion on the Council's accounts on 28 July 2016, well in advance of the 30 September 2016 national deadline.

The Council made the accounts available for audit in line with the agreed timetable, and provided a good set of working papers to support them. The finance team responded promptly and efficiently to our queries during the course of the audit.

The key messages arising from our audit of the Council's financial statements were:

- the draft accounts were again produced to a good standard
- the audit was facilitated by good supporting working papers and excellent assistance from the finance team.

As with last year's audit we also had a number of helpful early discussions with the Finance team around key technical issues. This enabled the early resolution of issues that would have been difficult to resolve promptly once the audit was in progress.

## **Issues arising from the audit of the accounts**

We reported the key issues from our audit of the accounts of the Council to the Council's Audit Committee on 27 July 2016.

## **Annual Governance Statement and Narrative Report**

We are also required to review the Council's Annual Governance Statement and Narrative Report. It published them on its website with the draft accounts in advance of the national deadlines.

Both documents were prepared in line with the relevant guidance and were consistent with the supporting evidence provided by the Council and with our knowledge of the Council.

## **Other statutory duties**

We also have additional powers and duties under the Act, including powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about the Council's accounts and to raise objections received in relation to the accounts.



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# Value for Money conclusion

## Background

We carried out our review in accordance with the NAO Code of Audit Practice (the Code), following the guidance issued by the NAO in November 2015 which specified the criterion for auditors to evaluate:

*In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.*

## Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the key risks where we concentrated our work.

The key risks we identified and the work we performed are set out in table 2 overleaf.

As part of our Audit Findings report agreed with the Council in July 2016, we agreed recommendations to address our findings.

1. The Council must formally agree a clear action plan to address the issues in the Ofsted report on Childrens Services. The action plan should be subject to appropriate oversight and scrutiny through the Council's corporate governance arrangements
2. The Council must develop realistic savings plans to bridge the budget gap in 2017/18 to 2019/20.
3. The Council must ensure that it allocates sufficient resources to enable the target dates in the CPC action plan for the Strategic Partnership Forum, and the development of the high level plan and communication and engagement strategy, to be achieved.
4. The Council must allocate a specific timeline for re-establishing clear governance practice and procedures.

## Overall VfM conclusion

We are satisfied that, in all significant respects, except for the matter we identified below, the Council had proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2016.

We concluded that the matters reported in the Ofsted report on the Council's Childrens Services issued in January 2016 were weaknesses in proper arrangements for understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management, and for planning, organising and developing the workforce effectively to deliver strategic priorities.

The Council's Policy Development and Decision Group (Joint Commissioning Team) received an update on the Children Services Improvement Plan on 18 October 2016, which included a comprehensive action plan to address the Ofsted recommendations.

# Value for Money

**Table 2: Value for money risks**

Risk identified	Work carried out	Findings and conclusions
<p><b>Ofsted inspection of children's services</b> Ofsted issued a report on the Council's children's services in 2015/16 which rated these as 'inadequate'. Until such time as Ofsted has confirmed that adequate arrangements are in place this remains a significant risk to the Council's arrangements.</p>	<p>We reviewed the action being taken by the Council in response to the issues in the Ofsted report.</p>	<p>The Council is undertaking a lot of work in this area but a formal action plan to address the issues from the Ofsted report has yet to be approved by Members. A detailed report on the Delivery of the Childrens Services Five Year plan is due to go to Council on 21 July 2016.</p> <p>The Council needs to formally agree a clear action plan to address the issues in the Ofsted report.</p> <p><b>We concluded that there were weaknesses in proper arrangements for understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management, and for planning, organising and developing the workforce effectively to deliver strategic priorities.</b></p> <p><i>The Council's Policy Development and Decision Group (Joint Commissioning Team) received an update on the Children Services Improvement Plan on 18 October 2016, which included a comprehensive action plan to address the Ofsted recommendations.</i></p>
<p><b>Medium term financial planning</b> The Council's Medium Term Resource Plan (MTRP) shows that the Council needs to identify further savings in the region of £20m over the next four years. This is after finding £10m of savings in the 2016/17 budget.</p>	<p>We reviewed the Council's latest MTRP and the 2016/17 budget, considering the assumptions that underpin the figures within them.</p>	<p>The Council has got robust financial planning processes in place. A four year Medium Term Resource Plan (MTRP) is in place covering 2016/17 to 2019/20. This is regularly reviewed and updated. The MTRP reflects the impact of the reductions in government grant and estimates that the Council will have a budget gap of £18.5m by 2019/20. A three year budget to address this gap is being developed.</p> <p><b>On that basis we concluded that while the level of savings needed represents a significant challenge for the Council, the risk was sufficiently mitigated and the Council has proper arrangements in place for planning finances effectively to support the sustainable delivery of strategic priorities and using appropriate cost and performance information to support informed decision making.</b></p> <p><i>The Efficiency Plan approved on 22 September 2016 identifies that the budget gap to 2019/20 is now £21.5m.</i></p>

# Value for Money (Continued)

**Table 2: Value for money risks (continued)**

Risk identified	Work carried out	Findings and conclusions
<p><b>Partnerships</b> The Corporate Peer Challenge (CPC) by the Local Government Association (LGA) in late 2015 noted that there are a range of progressive and inspiring partnerships, but also that many partners were disillusioned by the lack of common purpose and felt constrained. The Council is working with partners from different organisations and service areas with potentially conflicting priorities.</p>	<p>We reviewed the project management and risk assurance frameworks established by the Council to establish how it is identifying, managing and monitoring its partnerships. We will also review actions being taken by the Council in response to the CPC report.</p>	<p>The Council does not have a central register of its partnerships. The Council has actions in place to set up a Strategic Partnership Forum but this seems to be behind its original timescale of meeting before the end of June 2016. The timescale for developing its High Level Plan and a communication and engagement strategy by the end of August 2016, for a report to Council in September 2016, will be challenging if further progress is not made.</p> <p><b>The Council's work on this area is in progress and we do not consider that this is an issue that impacts on our VFM conclusion but the Council must ensure that it allocates sufficient resources to enable the target dates in the CPC action plan to be achieved.</b></p>
<p><b>Informed decision making</b> The CPC report raised issues around the Council's decision making and recommended that more effective working practices are implemented in respect of transparency and political decision making.</p>	<p>We reviewed the Council's response to the CPC report and considered any actions being planned.</p>	<p>The Council have detailed a number of actions which have been linked to the development of the training programme. However, the detailed actions for recommendation 14 refers to re-establishing clear governance practice and procedures with roles and responsibilities mapped out. While linked to the development of the training programme this is a separate piece of work that needs to be urgently addressed and it should be given a specific timeline for completion.</p> <p>There have also been recent instances of motions being brought directly to Council without supporting reports, which could leave the Council open to challenge on the transparency of its decision making process, which emphasises the importance of this review.</p> <p><b>The Council's work on this area is in progress and we do not consider that this is an issue that impacts on our VFM conclusion but the Council must allocate a specific timeline for re-establishing clear governance practice and procedures.</b></p>

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# Working with the Council

## Our work with you in 2015/16

We are really pleased to have worked with you over the past year. We have established a positive and constructive relationship. Together we have delivered some great outcomes.

An efficient audit – we delivered the accounts audit two months before the statutory deadline and in line with the timescale we agreed with you. Our audit team are knowledgeable and experienced in your financial accounts and systems. Our relationship with your team provides you with a financial statements audit that continues to finish on schedule releasing your finance team for other important work.

Understanding your operational health – through the value for money conclusion we provided you with assurance on your operational effectiveness. We highlighted the need for the Council to formally agree a clear action plan to address the issues in the Ofsted report on Childrens Services, which led to the qualification to our VFM conclusion, and the need to develop realistic savings plans to bridge the budget gap in 2017/18 to 2019/20.

We provided regular audit committee updates covering emerging issues and developments of relevance to the Council, including those from the National Audit Office (NAO) and CIPFA.

Thought leadership - we have shared our insights via our national publications. Areas we covered included:

- Innovation in public financial management
- Knowing the Ropes – Cross sector Audit Committee Effectiveness Review
- Making devolution work – A practical guide for local leaders
- Reforging local government – our summary findings from financial health checks and governance reviews
- Advancing closure – sharing the lessons learned from local government bodies who have advanced their financial reporting processes and closed their accounts early. We are holding a workshop on this topic in October where your Chief Finance Officer will be presenting jointly with your external audit manager on how we have worked together to achieve early closure of the Council's accounts.

We have also shared with you our publication on Building a successful joint venture and will continue to support you as you consider greater use of alternative delivery models for your services. Your Chief Finance Officer will be attending our income generation workshop in October.

Providing training – we provided your teams with training on financial accounts and annual reporting. The joint training with CIPFA was attended by your Chief Finance Officer and Principal Accountant. We also held a seminar on accounting for the Better Care Fund and Pooled Budgets, which was attended by Torbay finance staff.

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# Working with the Council

## Working with you in 2016/17

### Highways Network Asset

The Code of Practice on Local Authority Accounting (the Code) requires authorities to account for Highways Network Asset (HNA) at depreciated replacement cost (DRC) from 1 April 2016. The Code sets out the key principles but also requires compliance with the requirements of the recently published Code of Practice on the Highways Network Asset (the HNA Code), which defines the assets or components that will comprise the HNA. This includes roads, footways, structures such as bridges, street lighting, street furniture and associated land. These assets should always have been recognised within Infrastructure Assets.

The Code includes transitional arrangements for the change in asset classification and the basis of measurement from depreciated historic cost (DHC) to DRC under which these assets will be separated from other infrastructure assets, which will continue to be measured at DHC.

This is expected to have a significant impact on the Council's 2016/17 accounts, both in values and levels of disclosure, and may require considerable work to establish the opening inventory and condition of the HNA as at 1 April 2016.

Under the current basis of accounting values will only have been recorded against individual assets or components acquired after the inception of capital accounting for infrastructure assets by local authorities. Authorities may therefore have to develop new accounting records to support the change in classification and valuation of the HNA.

The nature of these changes means that Finance officers will need to work closely with colleagues in the highways department and potentially also to engage other specialists to support this work.

Some of the calculations are likely to be complex and will involve the use of external models, a combination of national and locally generated rates and a number of significant estimates and assumptions.

We have been working with the Council on the accounting, financial reporting and audit assurance implications arising from these changes. We have issued two Client Briefings which we have shared with your Chief Finance Officer. We will issue further briefings during the coming year to update the Council on key developments and emerging issues.

This major accounting development is likely to be a significant risk for our 2016/17 audit. The Council has an implementation plan in place for the Highways Network Asset and has carried out a lot of preparatory work for the changes. We will continue to have early discussions with Council staff on the progress being made in this area.

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# Working with the Council

We will continue to liaise closely with the senior finance team during 2016/17 on this important accounting development, with timely feedback on any emerging issues.

The audit risks associated with this new development and the work we plan to carry out to address them will be reflected in our 2016/17 audit plan.

We will also continue to work with you and support you over the next financial year.

Locally our focus will be on:

- An efficient audit – continuing to deliver an efficient audit
- Understanding your operational health – we will focus our value for money conclusion work on your progress in addressing the issues raised in the Ofsted report on Childrens Services and the implementation of the action plan arising from the LGA Corporate Peer Challenge. We will also concentrate on the Council's plans to address the budget gap in 2017/18 to 2019/20. Your Efficiency Plan approved in September 2016 identifies that additional income and savings of £21.5m are required.

# Appendix A: Reports issued and fees

We confirm below our final fees charged for the audit and confirm there were no fees for the provision of non audit services.

## Fees

	Planned £	Actual fees £	2014/15 fees £
Statutory audit of the Council	102,053	107,019*	136,070
Housing Benefit Grant Certification	7,954	7,954**	12,840
<b>Total fees (excluding VAT)</b>	<b>110,007</b>	<b>114,973</b>	<b>148,910</b>

\* The final audit fee included an additional fee of £4,966 for the work required in relation to the Energy from Waste PFI scheme. This is subject to approval from Public Sector Audit Appointments Ltd (PSAA).

\*\* This work is on-going and the final fee will be notified in the Certification Letter later this year.

## Fees for other services

Service	Fees £
<b>Audit related services:</b>	
• Teachers' Pension	<b>3,800</b>
<b>Non-audit services</b>	<b>Nil</b>

## Reports issued

Report	Date issued
Audit Plan	March 2016
Audit Findings Report	July 2016
Annual Audit Letter	October 2016



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