

# The Annual Audit Letter for Torbay Council

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Year ended 31 March 2019

1 November 2019



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# Executive Summary

## Purpose

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at Torbay Council (the Council) and its subsidiaries (the group) for the year ended 31 March 2019.

This Letter is intended to provide a commentary on the results of our work to the group and 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 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 25 September 2019.

## Our work

## Respective 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 and group'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 and group's financial statements, we comply with International Standards on Auditing (UK) (ISAs) and other guidance issued by the NAO.

<b>Materiality</b>	We determined materiality for the audit of the group's financial statements to be £6,208k, which is 2% of the group's gross revenue expenditure.
<b>Financial Statements opinion</b>	We gave an unqualified opinion on the group's financial statements on 3 October 2019.
<b>Whole of Government Accounts (WGA)</b>	Work was not required on the Council's consolidation return as the Council did not exceed the threshold of £500m specified by the NAO.
<b>Use of statutory powers</b>	We did not identify any matters which required us to exercise our additional statutory powers.
<b>Value for Money arrangements</b>	We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources except for in relation to understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management in children's services and for planning, organising and developing the workforce effectively to deliver strategic priorities. We therefore qualified our value for money conclusion in our audit report to the Council on 3 October 2019.
<b>Certification of Grants</b>	We also carry out work to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions and the Teachers pensions claim. Our work on these claims is not yet complete and will be finalised by 30 November 2019. We will report the results of this work to the Audit Committee separately.
<b>Certificate</b>	We certified that we have completed the audit of the financial statements of Torbay Council in accordance with the requirements of the Code of Audit Practice on 3 October 2019.

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# Executive Summary

## Working with the Council

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

- Understanding your operational health – through the value for money conclusion we provided you with assurance on your operational effectiveness.
- Sharing our insight – we provided regular audit committee updates covering best practice. We also shared our thought leadership reports
- Providing training – we provided your teams with training on financial statements and annual reporting
- Supporting development – we participated in training for the Audit Committee on 26 June 2019

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 2019**

# Audit of the Financial Statements

## Our audit approach

### Materiality

In our audit of the group's financial statements, 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 the audit of the group financial statements to be £6,208k, which is 2% of the group's gross revenue expenditure. We determined materiality for the audit of the Council's financial statements to be £5,748k, which is 2% of the Council's gross revenue expenditure. We used this benchmark as, in our view, users of the group and Council's financial statements are most interested in where the group and Council has spent its revenue in the year.

We also set a lower level of specific materiality for senior officer remuneration of £20k.

We set a lower threshold of £310k, above which we reported errors to the Audit Committee in our Audit Findings Report.

### The scope of our audit

Our audit involves obtaining sufficient 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 accounting policies are appropriate, have been consistently applied and adequately disclosed;
- the 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 remainder of the financial statements and the narrative report and annual governance statement published alongside the financial statements to check it is consistent with our understanding of the Council and with the financial statements included in the Annual Report on which we gave our opinion.

We carry out our audit in accordance with ISAs (UK) and the NAO Code of Audit Practice. We believe that 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 group'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 Financial Statements

## Significant Audit Risks

These are the significant 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	Findings and conclusions
<p><b>Valuation of land and buildings</b></p> <p>The Council revalues its land and buildings on a rolling five-yearly basis. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved (£297m) and the sensitivity of this estimate to changes in key assumptions. Additionally, where a rolling programme is used, management need to ensure the carrying value in the Authority's financial statements is not materially different from the current value or the fair value (for surplus assets) at the financial statements date.</p> <p>We therefore identified valuation of land and buildings, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement, and a key audit matter.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"><li>• evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to the valuation expert and the scope of their work</li><li>• evaluated the competence, capabilities and objectivity of the valuation expert</li><li>• written to the valuer to confirm the basis on which the valuation was carried out</li><li>• challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding</li><li>• tested revaluations made during the year to see if they had been 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 has satisfied themselves that these are not materially different to current value at year end.</li></ul>	<p>Our audit work did not identify any significant issues in relation to the valuation of land and buildings.</p>

# Audit of the Financial Statements

## Significant Audit Risks

These are the significant 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	Findings and conclusions
<p><b>Valuation of net pension liability</b></p> <p>The Council's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements.</p> <p>The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£186m) in the Council's balance sheet) and the sensitivity of the estimate to changes in key assumptions.</p> <p>We therefore identified valuation of the Council's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement, and a key audit matter.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"><li>• updated our understanding of the processes and controls put in place by management to ensure that the Council's pension fund net liability is not materially misstated and evaluate the design of the associated controls</li><li>• evaluated the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work</li><li>• assessed the competence, capabilities and objectivity of the actuary who carried out the Council's pension fund valuation</li><li>• assessed the accuracy and completeness of the information provided by the Council to the actuary to estimate the liability</li><li>• tested the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary</li><li>• undertaken procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report</li><li>• obtained assurances from the auditor of Devon Pension Fund as to the controls surrounding the validity and accuracy of membership data; contributions data and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements</li><li>• considered the Council's arrangements in respect of the McCloud judgement and undertaken procedures to confirm the reasonableness of the actuary's estimate of the potential impact on the Council.</li></ul>	<p>Our work concluded that the actuary's estimate of £2,859k for the McCloud judgement should be adjusted for in the accounts. The Council opted not to adjust the accounts as it was not material.</p>

# Audit of the Financial Statements

## Significant Audit Risks

These are the significant 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	Findings and conclusions
<p><b>Management override of internal 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>We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p>As part of our audit work we have;</p> <ul style="list-style-type: none"><li>• evaluated the design effectiveness of management controls over journals</li><li>• analysed the journals listing and determine the criteria for selecting high risk unusual journals</li><li>• tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration</li><li>• gained an understanding of the accounting estimates and critical judgements applied made by management and considered their reasonableness with regard to corroborative evidence</li><li>• evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions.</li></ul>	<p>Our audit work did not identify any issues in relation to management override of controls.</p>



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# Audit of the Financial Statements

## **Audit opinion**

We gave an unqualified opinion on the group's financial statements on 3 October 2019.

## **Preparation of the financial statements**

The group presented us with draft financial statements in accordance with the national deadline, 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.

## **Issues arising from the audit of the financial statements**

We reported the key issues from our audit to the Council's Audit Committee on 25 September 2019.

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

We are required to review the Council's Annual Governance Statement and Narrative Report. It published them on its website alongside the Statement of Accounts in line with the national deadlines.

Both documents were prepared in line with the CIPFA Code and relevant supporting guidance. We confirmed that both documents were consistent with the financial statements prepared by the Council and with our knowledge of the Council.

## **Whole of Government Accounts (WGA)**

We issued an assurance statement which confirmed the Council was below the audit threshold.

## **Certificate of closure of the audit**

We certified that we have completed the audit of the financial statements of Torbay Council in accordance with the requirements of the Code of Audit Practice on 3 October 2019.

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# Value for Money conclusion

## Background

We carried out our review in accordance with the NAO Code of Audit Practice, following the guidance issued by the NAO in November 2017 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 risks where we concentrated our work.

The risks we identified and the work we performed are set out overleaf.

As part of our Audit Findings report agreed with the Council in September 2019, we agreed recommendations to address our findings.

## Overall Value for Money conclusion

We are satisfied that, in all significant respects, except for the matter we identified overleaf, the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2019.

# Value for Money conclusion

## Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p><b>OFSTED inspection of children's services</b></p> <p>Ofsted report issued in August 2018 rated Children's Services in Torbay as inadequate, following a previous inadequate rating in January 2016. As of 1 April 2018 Torbay's Children's Services have been managed by a single Director of Children's Services who is also the Director of Children's Services for Plymouth City Council.</p>	<p>We reviewed the progress being made by the Council under its new arrangements with Plymouth City Council, considering the actions being taken to address the continuing pressures on this service.</p> <p>The Council's Children's Services were rated as inadequate back in January 2016 and now have a contractual arrangement with Plymouth City Council, with a Joint Director for Children's Services (DCS) for Torbay Council and Plymouth City Council.</p> <p>Ofsted subsequently issued a follow-up report in August 2018 based on their July 2018 inspection visit, in which the inadequate rating remained in place. The report concluded that overall, the pace of change has been too slow and some recommendations from the previous inspection are not met. It stated that fundamental weaknesses remain in management oversight and supervision and in identification of and response to risk, as well as workforce development and capacity.</p> <p>Since the report was issued there have been two monitoring visits.</p> <p>The first of these was in January 2019. This concluded that "Senior leaders have failed to address the significant concerns identified during the re-inspection of Torbay children's services in June 2018."</p> <p>The most recent monitoring visit was in April 2019, with the letter being issued on 8 May 2019. This comments that "The local authority is starting to make some progress, from an extremely low base, in improving services for its children and young people, but these improvements remain exceedingly fragile."</p>	<p>Despite the re-inspection rating of inadequate and the revised structure under the joint DCS with Plymouth City Council, the monitoring visit in January 2019 concluded that the significant concerns identified in the re-inspection has not been addressed. There were some signs of improvement following the April 2019 visit but these were described as fragile.</p> <p><b>This is evidence of weaknesses in proper arrangements for understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management in children's services, and for planning, organising and developing the workforce effectively to deliver strategic priorities.</b></p>

# Value for Money conclusion

## Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p><b>Budget delivery and savings</b></p> <p>The Council is forecasting an overspend of £2.4m in 2018/19, due to budget pressures in Children's Services. While the budget consultation for 2019/20 is based on a balanced budget, the Council needs to identify savings in the region of £11m for 2020/21 and 2021/22 in order to achieve a balanced budget.</p>	<p>We reviewed the Council's latest MTRP and the 2019/20 budget, considering the assumptions that underpin the figures within them. We also reviewed the 2018/19 savings achieved against those originally planned.</p> <p>The revenue outturn for 2018/19 showed an surplus of £0.5m however this was after the application of one-off funding of £2.6m to counter the overspend in Children's Services of £5m in the year, offset by savings elsewhere. The Council monitors the savings being achieved against those planned throughout the year with a Savings tracker going to Senior Leadership Team (SLT) on a monthly basis.</p> <p>A balanced budget was set for 2019/20, which included savings of £6m. The Council's latest update to the Medium Term Resource Plan was in April 2019. This shows the budget gap in 2020/21 to 2022/23 to be £18.3m, with savings of £10.5m required in 2020/21. The MTRP is a public document and is updated regularly to reflect changes as they are known. It is a comprehensive document that clearly sets out the financial challenges facing Torbay over the next three years. The MTRP contains reasonable assumptions about the figures over the next four years. 2020/21 is a key challenge for the Council with the predicted budget gap of £10.5m and the Risk Share Agreement with the Integrated Care Organisation (ICO) running out in March 2020. Negotiations on a new RSA remain in progress at the time of audit.</p> <p>The Council are currently working on the development of the 2020/21 budget, with the consultation on the 2020/21 budget scheduled for October 2019.</p> <p>The LGA Finance Peer Challenge identified a number of key recommendations for the Council. An action plan has been agreed to take these forward.</p>	<p>The Council's MTRP has a gap of £18.3m over the 2020/21 - 2022/23 period. This represents a considerable challenge for the Council given the savings it has already had to make in recent years. The Council must urgently develop realistic savings plans to bridge the budget gap while carefully monitoring the achievement of planned savings in 2019/20.</p> <p>The agreement of a new Risk Share Agreement with the ICO is crucial for the Council with Adult Social Care being the Council's largest area of spend.</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>

# Value for Money conclusion

## Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p><b>Investment arrangements / commercialisation</b></p> <p>The Council has an Investment Fund of £200m was set up to maximise income generation, which has been financed by PWLB borrowing. A large commercial property portfolio may expose the Council's investments to volatility.</p>	<p>The Council has an investment fund of £200m, which was one of the areas identified as a way of bringing in additional income to offset reductions in central grant funding. The investment fund is financed by borrowing from PWLB, taking advantage of the low interest rates compared to the rental yields that are available from the investment property portfolio, which led to income of £2.9m in 2018/19.</p> <p>The Council has an Investment and Regeneration Fund Strategy (the Strategy) which sets out the objectives and scope of the strategy, part of which is to support the Council's Economic Strategy by delivering economic growth, tackling inequality and creating change for the benefit of residents. However, the Strategy also emphasises the importance of a balanced portfolio of investments to spread risk and notes that investment of the fund solely in Torbay would not achieve diversification of risk due to the small geographical location.</p> <p>Decisions to spend monies from this fund are not Executive decisions and Full Council have delegated this to the Investment and Regeneration Committee who can approve individual investments up to £25m. Proposals are considered under two categories:</p> <ul style="list-style-type: none"> <li>Investment opportunities that meet criteria set out in section 4 of the Strategy and deliver both a financial return to the Council and a benefit, improvement or development of the area</li> <li>regeneration investment opportunities that meet criteria set out in section 5 of the Strategy and deliver significant regeneration benefits to the area, including Town Centre proposals.</li> </ul> <p>The Council has further extend their area for the purchase of investment properties with a strategy statement that concluded that the Local Enterprise Partnership FEMA (Functional Economic Market Area) would be considered to be the Council area for investment purchases. This covers Devon, Cornwall, Somerset, Avon and Dorset. The Strategy updated in September 2018 also sets out that "opportunities in any geographic location will be considered if it can be objectively demonstrated that there are multiple benefits, including the improvement or development of Torbay, if supported by the Monitoring Officer and the Head of Finance."</p> <p>Appendix 1 of the Strategy sets out the framework for the due diligence process that the Council undertakes. This takes into accounts numerous factors and risks depending on the type of investment, and has led to the Council withdrawing from several purchases.</p> <p>The Council has an Investments dashboard, which shows their portfolio. All properties are reviewed by nominated officers (Monitoring Officer, Chief Finance Officer and the lead Council officer for Asset Management) on a quarterly basis to review each property for potential disposal or investment depending on both current and future asset values and rental streams. It is not clear if this process extends to detailed scenario planning for the Council's portfolio as a whole rather than considering individual properties in isolation.</p>	<p>The Council must ensure that scenario planning is carried out as part of its quarterly investment portfolio review that consider the entire portfolio as well as individual properties. As it looks to extend both the size of the investment fund value, and the geographic area, it must ensure it takes appropriate advice to cover itself in this fast moving developing area for local government.</p> <p><b>No issues identified that impact on our VFM conclusion.</b></p>

# Value for Money conclusion

## Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p><b>Transformation</b></p> <p>The Council is progressing a number of projects through its Transformation Programme as it seeks alternative methods of service delivery. The need to the Council to consider if it has adequate capacity to support and deliver its transformation programme was raised in our 2017/18 Audit Findings Report.</p>	<p>We reviewed the arrangements being put in place by the Council for these projects, including whether appropriate advice has been taken. This included new initiatives such as the Housing Company as well as the work being done by the Council on the TOR2 contract. We also considered whether the restructure and recruitment actions proposed by the Council in response to our 2017/18 recommendation were successful in creating additional capacity to support the transformation programme.</p> <p>The Council's Transformation Programme Manager reports to the Chief Executive, who is responsible for the Transformation Programme overall and chairs the Transformation Board.</p> <p>The Transformation Board consists of the members of Senior Leadership Team (SLT), with members being kept informed via Programme Manager reports and updates to the Executive Group and all member communications. The Board meets monthly and considers new projects in the pipeline as well as monitoring the progress on existing projects. The reporting includes a dashboard of progress on all projects, with RAG rating of the savings being achieved against those planned. "Hot topics" updates concentrate on the progress on current schemes, with the future for TOR2 being a live topic in the year.</p> <p>The Council has sought external advice previously, such as the development of the Housing Companies.</p> <p>The Council has previously attempted to recruit a Director of Transformation to increase its capacity in this crucial area but was unsuccessful in attracting suitable candidates. As a result there was an SLT restructure to bring in some additional capacity, which in turn brought some additional capacity to the Transformation Programme. The restructure means that individual members of SLT are now responsible for individual projects in the Programme. Additional Project Officer support was recruited to the Transformation Team in order to support SLT in ensuring delivery of the projects and the programme.</p>	<p><b>The Transformation Programme is critically important for the Council if it is going to deliver the changes and savings required in the medium term. We concluded that the Council has adequate arrangements in place for managing and monitoring its transformation programme but it must ensure that it continues to seek external advice, legal or otherwise, as it moves into new areas.</b></p>

# A. Reports issued and fees

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

## Reports issued

Report	Date issued
Audit Plan	February 2019
Audit Findings Report	September 2019
Annual Audit Letter	October 2019

## Fees

	Planned £	Actual fees £	2017/18 fees £
Statutory audit	78,581	78,581	102,053
Additional fees		9,000	9,310*
<b>Total fees</b>	<b>78,581</b>	<b>87,581</b>	<b>111,363</b>

\* An objection relating to 2016/17 and 2017/18 has been closed and the related fees are subject to PSAA approval

## Audit fee variation

As outlined in our audit plan, the 2018-19 scale fee published by PSAA of £78,581 assumes that the scope of the audit does not significantly change. There are a number of areas where the scope of the audit has changed, which has led to additional work. These are set out in the following table.

Area	Reason	Fee proposed
<b>Assessing the impact of the McCloud ruling</b>	The Government's transitional arrangements for pensions were ruled discriminatory by the Court of Appeal last December. The Supreme Court refused the Government's application for permission to appeal this ruling. As part of our audit we have reviewed the revised actuarial assessment of the impact on the financial statements along with any audit reporting requirements.	3,000
<b>Pensions – IAS 19</b>	The Financial Reporting Council has highlighted that the quality of work by audit firms in respect of IAS 19 needs to improve across local government audits. Accordingly, we have increased the level of scope and coverage in respect of IAS 19 this year to reflect this.	3,000
<b>PPE Valuation – work of experts</b>	As above, the Financial Reporting Council has highlighted that auditors need to improve the quality of work on PPE valuations across the sector. We have increased the volume and scope of our audit work to reflect this.	3,000
<b>Total</b>		<b>9,000</b>

Fee variations are subject to PSAA approval.

# A. Reports issued and fees continued

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

## Fees for non-audit services

Service	Fees £
<b>Audit related services</b>	
- Housing benefits work under Module X 2017/18	5,000
- Certification of 2018/19 Housing benefits grant	10,407
- Teacher's Pension	3,900
<b>Non-Audit related services</b>	
- Harbour authority audit	950

## Non- audit services

- For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the group. The table above summarises all non-audit services which were identified.
- We have considered whether non-audit services might be perceived as a threat to our independence as the group's auditor and have ensured that appropriate safeguards are put in place.

The above non-audit services are consistent with the group's policy on the allotment of non-audit work to your auditor.



