



# Annual Audit Letter

*Year ending 31 March 2018*

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Carlisle City Council  
August 2018



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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 Carlisle City Council (the Council) for the year ended 31 March 2018.

This Letter is intended to provide a commentary on the results of our work to the Council 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 30 July 2018.

## Our work

Materiality	We determined materiality for the audit of the Council's financial statements to be £1,188,000, which equates to 1.75% of the Council's gross revenue expenditure.
Financial Statements opinion	We gave an unqualified audit report opinion on the Council's financial statements on 30 July 2018.
Whole of Government Accounts (WGA)	We completed work on the Council's consolidation return following guidance issued by the NAO.
Use of statutory powers	We did not identify any matters which required us to exercise any of our additional statutory powers.

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

# Executive Summary

Value for Money arrangements	We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources. We reflected this in our audit report opinion to the Council on 30 July 2018.
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 2018 deadline. We will report the results of this work to the Audit Committee in our Annual Certification Letter.
Certificate	We certify that we have completed the audit of the accounts of Carlisle City Council in accordance with the requirements of the Code of Audit Practice.

## Working with the Council

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

- An efficient audit – we delivered an efficient audit with you in July 2018, completing the audit work well in advance of the deadline before signing the audit off on 30 July 2018, releasing your finance team for other work
- 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 technical update training on financial accounts and annual reporting
- Supporting development – we provided workshops for the Audit Committee in January and July 2018 on the role of external audit.

The Accounts have been produced to a good standard and the finance team have produced good working papers and have also been very responsive to our audit queries. A good achievement, especially in the context of a complex set of statements, and the shorter closedown period and tighter statutory deadlines

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  
August 2018

# Audit of the Accounts

## Our audit approach

### Materiality

In our audit of the Council'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 Council's accounts to be £1,188,000, which is 1.75% of the Council's gross revenue expenditure. We used this benchmark as, in our view, users of the Council's financial statements are most interested in where the Council has spent its revenue in the year.

We also set a lower level of specific materiality for senior officer remuneration and related party transactions.

We set a lower threshold of £59,000, 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
- the overall presentation of the financial statements gives a true and fair view.

We also read the remainder of the Statement of Accounts including the narrative report and the annual governance statement to check they are consistent with our understanding of the Council and with the financial statements included in the Statement of Accounts 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 is 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 significant risks and the results of this work.

# Audit of the Accounts

## 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 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 Council 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 identified management override of controls as a risk requiring special audit consideration.</p>	<p><b>As part of our audit work we have:</b></p> <ul style="list-style-type: none"> <li>gained an understanding of the accounting estimates, judgements applied and decisions made by management and considered their reasonableness</li> <li>obtained a full listing of journal entries, identified and tested unusual journal entries for appropriateness</li> <li>evaluated the rationale for any changes in accounting policies or significant unusual transactions.</li> </ul>	<p>We have not identified any issues, which require reporting through our work on management override of controls.</p>
<p><b>Valuation of property, plant and equipment</b></p> <p>The Council revalues its land and buildings and investment property on an annual basis to ensure that carrying value is not materially different from current value. This represents a significant estimate by management in the financial statements.</p> <p>We identified the valuation of land and buildings revaluations and impairments as a risk requiring special audit consideration.</p>	<p><b>As part of our audit work we have:</b></p> <ul style="list-style-type: none"> <li>reviewed management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work</li> <li>given consideration to the competence, expertise and objectivity of any management experts used</li> <li>discussed with the valuer the basis on which the valuation is carried out and challenge the key assumptions used</li> <li>reviewed and challenged the information used by the valuer to ensure it is robust and consistent with our understanding</li> <li>tested revaluations made during the year to ensure they are 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.</li> </ul>	<p>We have identified one amendment to the disclosure of asset lives, based on our review of the Council's Fixed Asset Register.</p> <p>In appendix A we have made one recommendation relating to the revaluation processes and controls in place. It was identified that two assets, which were intended to be revalued, were not included in the instructions sent to the valuation expert. Although these assets were not material, this indicates a potential control weakness in the process for supplying all of the appropriate assets, in line with the rolling programme, to be revalued by the valuation expert.</p>

# Audit of the Accounts

## 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 pension fund net liability</b> The Council's pension fund assets and liabilities as reflected in its balance sheet represent a significant estimate in the financial statements.</p> <p>We identified the valuation of the pension fund net liability as a risk requiring special audit consideration.</p>	<p><b>As part of our audit work we have:</b></p> <ul style="list-style-type: none"><li>• identified the controls put in place by management to ensure that the pension fund liability is not materially misstated</li><li>• assessed whether these controls were implemented as expected and whether they are sufficient to mitigate the risk of material misstatement</li><li>• evaluated the competence, expertise and objectivity of the actuary who carried out your pension fund valuation. We have gained an understanding of the basis on which the valuation is carried out</li><li>• undertaken procedures to confirm the reasonableness of the actuarial assumptions made</li><li>• checked the consistency of the pension fund asset and liability position and disclosures in notes to the financial statements with the actuarial report.</li></ul>	<p>We have not identified any issues, which requires reporting through our work on the valuation of pension fund net liability.</p>

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# Audit of the Accounts

## **Audit opinion**

We gave an unqualified audit report opinion on the Council's financial statements on 30 July 2018, in advance of the shorter revised national deadline.

## **Preparation of the accounts**

The Council presented us with draft accounts in accordance with the national deadline, and provided a good set of supporting working papers. The finance team responded promptly and efficiently to our queries during the course of the audit.

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

We reported the key issues from our audit to the Council's Audit Committee on 30 July 2018.

In addition, to the key audit risks reported above, we identified a number of issues throughout our audit that we have asked management to address for the next financial year, please refer to Appendix B.

We identified one material error which affected the Council's Comprehensive Income and Expenditure statement (CIES), but this did not impact the overall General Fund balance. The Council had included internally generated income and expenditure in the CIES, which should not have been included. Therefore, income and expenditure were reduced by £2.413 million. A prior period adjustment was made as well.

## **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, in 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 post audit amendments were consistent with the financial statements prepared by the Council and with our knowledge of the Council.

We identified that the Council did not have assurance gathering processes in place for all Directorates to support its AGS disclosures. In appendix B we recommend formalising these arrangements to allow the Council to easily demonstrate how its governance framework as outlined in the AGS is operating in practice.

## **Other statutory powers**

We also have additional powers and duties under the Local Audit and Accountability 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.

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

We are also required to certify that we have completed the audit of the accounts of Carlisle City Council in accordance with the requirements of the Code of Audit Practice. We issued our certificate as part of the audit report opinion given on 30 July 2018.

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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.*

## Our Work

AGN 03 requires us to disclose our views on significant qualitative aspects of the Council's arrangements for delivering economy, efficiency and effectiveness.

We have focused our work on the significant risk that we identified in the Council's arrangements. In arriving at our conclusion, our main key risk considerations were:

- the budgetary processes in place to be able to produce a robust Medium Term Financial Plan (MTFP)
- a review and challenge of the key assumptions underpinning the Council's MTFP.

## 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 overleaf.

As part of our Audit Findings Report presented to the Audit Committee on 30 July 2018, management agreed with the recommendations we raised to address our significant findings.

## Overall Value for Money conclusion

We are satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2018.

# Value for Money conclusion

## Key Value for Money Risks

Risks identified in our audit plan	Findings and conclusions
<p><b>Significant service transformation projects and the Medium Term Financial Plan (MTFP)</b></p> <ul style="list-style-type: none"><li>The Council's MTFP is predicated on delivering changes to the way in which services are delivered. The Council has identified proposals for reducing spending and increasing efficiency. The programme includes a number of key projects, including internally reshaping the Council.</li></ul>	<p>The Medium Term Financial Plan (MTFP) approved by Council in September 2017, demonstrated that appropriate steps were being taken to ensure a balanced budget position was maintained, despite reduced Government funding. A Savings Strategy is in place and continues to focus on assets, service delivery models and the 'Transformation Programme' to deliver the savings required to produce a balanced longer-term budget. The MTFP for 2018/19 to 2022/23 identified savings of £2.274 million. In addition, a savings requirement for 2017/18 of £0.795 million was identified, with £0.395 million achieved.</p> <p>£0.4 million of 2017/18 savings were not achieved due to the 'Rethinking Waste' initiative policy decision not being followed by the Council. A replacement savings initiative is yet to be identified by the Council, which will put further recurring savings pressures on 2018/19. However, this can be adequately absorbed by the General Fund in 2017/18, with a forecast balance well in excess of the £2 million minimum set by the Council in 2018/19.</p> <p>The Council should ensure that it remains agile to unexpected changes in policy, and proactively identifies alternative options to current funding streams or savings initiatives, should these become unachievable due to unexpected events, changes in the economic climate or Council policy decisions.</p> <p>In May 2018, the Council had to take emergency action to make safe a dangerous structure within Carlisle under section 78 of the Building Act 1984. This has led to a £0.650 million contribution from the Council's General Fund Reserves in 2018/19, putting further pressure on usable reserves. This instance, alongside the 'Rethinking Waste' policy decision, highlights the need for the Council to identify additional savings requirements and income generation initiatives beyond the minimum required in order to meet potential unforeseen budgetary pressures.</p> <p>During 2017/18 as part of the 2018/19 budget compilation process, a detailed base budget review including an analysis of core budgets was undertaken. This provided an additional level of challenge and rigour within the budget setting process, to ensure all potential savings were identified.</p> <p>The Council is faced with a continual reduction in Central Government funding, which is making identifying savings increasingly more difficult. It will be essential therefore to ensure that its savings plans continue to be clearly communicated, monitored, linked to specific policy decisions, service reviews and on-going rationalisation of the workforce. As well as reducing expenditure, the Council is under increasing pressure to identify innovative methods of income generation.</p> <p>The Council's involvement in wider economic regeneration schemes including the Borderlands Initiative and the St Cuthbert's Garden Village further highlights the requirement to be innovative in its approach to spending and generating income.</p> <p>The Council has a comprehensive approach to its medium term financial planning, budgeting and identification of saving plans, which are agreed at a corporate level, by senior officers and members. The strategy is aligned to the Council's corporate priorities, highlights the key financial risks, and adopts a prudent approach to funding streams.</p>

# Value for Money conclusion

## Key Value for Money Risks

Risks identified in our audit plan	Findings and conclusions
<b>Significant service transformation projects and the Medium Term Financial Plan (MTFP)</b>	<p>A proportion of the Council's income is received from rental income from its investment properties, with an element of this relating to retail units. City centres face increasing pressure from the downturn in profits of high street stores and the increase in online sales, with a number of high profile store closures occurring across the country, including some in Carlisle. Whilst the majority of the rental income is based on property leases with set rent, a significant element is contingent, based on the performance of the tenants holding the retail space. The Council should challenge the assumption of continual rental growth on these properties and ensure scenario planning is undertaken based on the potential future outcomes for the City centre. Evidence has been provided to support the income assumptions in the MTFP, but these should be continually reviewed and challenged going forward.</p> <p>During 2016/17 the Council undertook a review of their arrangements for the accounting for Minimum Revenue Provision (MRP) for 2017/18 onwards. As part of the review, the Council has taken a payment holiday for items identified totalling £1.1 million from 2003/04 to 2015/16 for voluntary MRP of £0.9 million, and a charge made in error for assets under construction of £0.2 million. The Council has reduced the MRP charge over the five year period from 2017/18, with a £0.226 million reduction in the current projected MRP charge in each year.</p> <p>During 2017/18, the Council has further reviewed their MRP policy for 2018/19 onwards. The Council has reviewed their calculation for 'Adjustment A', which was made on 1 April 2004, and identified a potential error in the calculation. The impact of this potential error is calculated by the Council as £2.146 million, with the MRP charge being reduced by £1.876 million over the five year period covered by the MTFP. The Council has sought legal advice on the above changes to the MRP policy due to its statutory nature, with the advice giving the opinion that the amendments are allowable.</p> <p>The change in MRP charged from 2018/19 onwards due to this potential error in 'Adjustment A' is still subject to audit, as the accounting impact is in 2018/19. Therefore, the Council should identify alternative methods of reducing expenditure or generating income, should this amendment be found to be inappropriate. Whilst reducing the MRP charged to the General Fund does improve the reserves position, this is short-term non-recurring solution to medium to long term financing challenges. Looking forward, the Council should seek to identify opportunities to reduce expenditure or generate further income through long-term focussed initiatives rather than reliance on accounting adjustments.</p> <p>The capital outturn for 2017/18 was £9.571 million against a £11.240 million budget. All of the £1.669 million underspend/ slippage on the capital programme has been carried forward and re-profiled over future years. The revenue outturn for 2017/18 was an underspend of £2.553 million. Of this amount £0.664 million is carried forward into the next period, and £1.276 million has been placed into earmarked reserves. The Council has a history of revenue underspends, generated through a combination of reduced expenditure as well as some income streams outperforming budgets.</p>

# Value for Money conclusion

## Key Value for Money Risks

Risks identified in our audit plan	Findings and conclusions
<b>Significant service transformation projects and the Medium Term Financial Plan (MTFP)</b>	<p>In the Audit Findings Report for 2016/17, a recommendation was made to the Council to re-profile the capital programme at regular intervals during the financial year. This recommendation has been adequately implemented in the quarterly budget monitoring report, which re-profiles the capital programme as necessary.</p> <p>The significant impact of the December 2015 floods upon assets continue to affect the Council's services and finances. As part of the 2015/16 outturn a flood reserve of £0.5 million was created for future non-insured costs of flood recovery. The flood reserve has increased by £1.514 million to £2.014 million at 31 March 2018, as flood insurance income was received in excess of the works carried out to date. The £2.014 million held in the flood reserve is to fund repairs to the Civic Centre and Bitts Park. During 2017/18 the Council has made progress on bringing affected assets back into use, most significant of which is the Sheepmount becoming operational again, and decisions being made on the future of the affected areas of the Civic Centre.</p> <p>The Council made significant progress during 2017/18 on the proposal to redevelop the Sands Centre to support the delivery of the Council's 'Sports Facilities Strategy'. The proposal was supported by a detailed options paper, which clearly communicated the potential cost of each option for the redevelopment. The cost is currently estimated to be £19.467 million, of which £17.467 million is to be funded by the Council, with the preferred financing option being through the use of external borrowing. This is in excess of the £5 million capital redevelopment costs, which were assumed in the initial MTFP. The full impact of the increased cost has been factored into the budget for 2018/19 in terms of the capital and revenue impact.</p> <p><b><u>Conclusion</u></b></p> <p><b>Based on the review of the arrangements in place during 2017/18 for the compilation of the MTFP including identified savings, we concluded that the overall risk was sufficiently mitigated and that the Council has proper arrangements in this area.</b></p>

# A. Reports issued and fees

We confirm below our final reports issued and fees charged for the audit. No non-audit services have been provided to the Council during 2017/18.

## Reports issued

Report	Date issued
Audit Plan	February 2018
Audit Findings Report	30 July 2018
Annual Audit Letter	August 2018




## Fees

	Planned £	Actual fees £	2016/17 fees £
Statutory Council audit	53,290	53,290	53,290
Grant Certification	16,852	TBC	14,093
<b>Total fees</b>	<b>70,142</b>	<b>TBC</b>	<b>67,383</b>




The planned fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA)

## B. Action Plan

We have identified two recommendations for the Council as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2018/19 audit. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.



	Assessment	Issue and risk	Recommendations
1	 Green	<ul style="list-style-type: none"> <li>It was noted through the review of the Council's Fixed Asset Register that a number of assets which had been either disposed of or fully depreciated, are being carried in the Fixed Asset Register at nil value.</li> </ul>	<ul style="list-style-type: none"> <li>Review the Fixed Asset Register and write-out any assets carried at nil value which are not in use by the Council.</li> </ul> <p><b>Management response</b></p> <ul style="list-style-type: none"> <li>Assets will be reviewed during 2018/19 to ensure any carried at nil value and are not in use are removed.</li> </ul>
2	 Amber	<ul style="list-style-type: none"> <li>From a completeness reconciliation of asset data provided to the external valuer for the purposes of the valuation, it was identified that two assets requiring valuation, were missed and as a result were not valued by the valuer. Whilst the value of these assets was immaterial, this is an indication of a potential control weakness.</li> </ul>	<ul style="list-style-type: none"> <li>Undertake a completeness reconciliation between the Fixed Asset Register and the instructions to the valuer to ensure all assets which are intended to be revalued are included.</li> </ul> <p><b>Management response</b></p> <ul style="list-style-type: none"> <li>Finance will confirm with Property Services that the asset revaluation instructions include all assets subject to revaluation.</li> </ul>
3	 Green	<ul style="list-style-type: none"> <li>We identified that the Council did not have assurance gathering processes in place for all Directorates. Formalising these arrangements allows the Council to easily demonstrate how its governance framework as outlined in the AGS is operating in practice.</li> </ul>	<ul style="list-style-type: none"> <li>Review the Council's assurance gathering arrangements to underpin future AGS disclosures on its governance framework.</li> </ul> <p><b>Management response</b></p> <ul style="list-style-type: none"> <li>Consideration will be given to developing and implementing a questionnaire to be sent to all directorates to ensure all potential issues to be included in the Annual Governance Statement are identified.</li> </ul>

### Controls




-  High – Significant effect on control system
-  Medium – Effect on control system
-  Low – Best practice

## B. Value for Money action plan

We have identified two Value for Money recommendations for the Council as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2018/19 audit.

	Assessment	Issue and risk	Recommendations
1	 <b>Amber</b>	<ul style="list-style-type: none"> <li>There are well documented challenges to City Centres across the country in the current economic climate due to the closure of several high profile retail outlets. Carlisle City Council generates a significant amount of revenue from rental income relating to retail properties.</li> </ul>	<ul style="list-style-type: none"> <li>Ensure that scenario planning is undertaken based on the potential future City Centre related revenue streams.</li> </ul> <p><b>Management response</b></p> <ul style="list-style-type: none"> <li>Consideration will continue to be given to the impact on the MTFP of the City Centre challenges throughout the budgetary cycle.</li> </ul>
2	 <b>Amber</b>	<ul style="list-style-type: none"> <li>Through our review of the Medium Term Financial Plan, we have identified a gap in the savings achieved for 2017/18 due to a change in Council priorities which has placed an increased savings pressure on 2018/19.</li> </ul>	<ul style="list-style-type: none"> <li>Proactively identify alternative savings or income generations initiatives for those identified which are based on policy decisions being followed through.</li> </ul> <p><b>Management response</b></p> <ul style="list-style-type: none"> <li>Consideration will be given to savings requirements and the impact of these on the MTFP during the budgetary planning cycle.</li> </ul>

### Controls

-  High – Significant effect on control system
-  Medium – Effect on control system
-  Low – Best practice

