



The Annual Audit Letter for Waverley Borough Council

Year ended 31 March 2020

15 December 2020



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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 Waverley Borough Council (the Council) and its subsidiaries (the group) for the year ended 31 March 2020.

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 November 2020.

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.

Working with the Council

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

Our work

Materiality	We determined materiality for the audit of the group's financial statements to be £1,911k, and £1,905k for the Council's financial statement. This is 2% of the group and Council's gross cost of services.
Financial Statements opinion	We gave an unqualified opinion on the group's financial statements on 2 December 2020. We included an emphasis of matter paragraph in our report in respect of the uncertainty over valuations of the Council and group's land and buildings and the property assets of its pension fund given the Coronavirus pandemic. This does not affect our opinion that the statements give a true and fair view of the Group's financial position and its income and expenditure for the year.
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 our additional statutory powers.
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 to the Council on 30 November 2020.
Certificate	We certified that we have completed the audit of the financial statements of Waverley Borough Council, in accordance with the requirements of the Code of Audit Practice on 2 December 2020.

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 £1,911k, which is 2% of the group's gross cost of services. We determined materiality for the audit of the Council's financial statements to be £1,905k which is 2% of the Council's gross cost of services. 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 set a lower threshold of £91k, 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 Statement of Accounts to check it is 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 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>Covid-19</p> <p>The global outbreak of the Covid-19 virus pandemic has led to unprecedented uncertainty for all organisations, requiring urgent business continuity arrangements to be implemented. We expect current circumstances will have an impact on the production and audit of the financial statements for the year ended 31 March 2020, including and not limited to;</p> <ul style="list-style-type: none"> - Remote working arrangements and redeployment of staff to critical front line duties may impact on the quality and timing of the production of the financial statements, and the evidence we can obtain through physical observation - Volatility of financial and property markets will increase the uncertainty of assumptions applied by management to asset valuation and receivable recovery estimates, and the reliability of evidence we can obtain to corroborate management estimates - Financial uncertainty will require management to reconsider financial forecasts supporting their going concern assessment and whether material uncertainties for a period of at least 12 months from the anticipated date of approval of the audited financial statements have arisen; and - Disclosures within the financial statements will require significant revision to reflect the unprecedented situation and its impact on the preparation of the financial statements as at 31 March 2020 in accordance with IAS1, particularly in relation to material uncertainties. <p>We therefore identified the global outbreak of the Covid-19 virus 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"> • worked with management to understand the implications the response to the Covid-19 pandemic had on the organisation's ability to prepare the financial statements and update financial forecasts and assessed the implications for our materiality calculations. No changes were made to materiality levels previously reported in respect of Covid-19, although it was reduced to reflect the lower gross revenue expenditure of the Council. The draft financial statements were provided on 17 July 2020; • liaised with other audit suppliers, regulators and government departments to co-ordinate practical cross-sector responses to issues as and when they arose. Examples include the material uncertainty disclosed by the Council's property valuation expert • evaluated the adequacy of the disclosures in the financial statements that arose in light of the Covid-19 pandemic; • evaluated whether sufficient audit evidence could be obtained through remote technology; • evaluated whether sufficient audit evidence could be obtained to corroborate significant management estimates such as assets and the pension fund liability valuations ; • evaluated management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment; • discussed with management the implications for our audit report where we have been unable to obtain sufficient audit evidence. <p>Management produced the draft financial statements and working papers in line with the agreed timetable ahead of the audit commencing. This is a significant achievement with all of the Council's staff working remotely, although our audit did identify improvements that could be made to the Council's arrangements for supporting the audit. We completed our audit remotely and, while it took longer than normal as a result, we were able to utilise technology to corroborate information produced by the Council.</p>	<p>We did not identify any implications for our audit report resulting from Covid-19, however our report includes standard reference to the macroeconomic conditions arising from Brexit and Covid-19.</p>

Audit of the Financial Statements

Significant Audit Risks - continued

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>Valuation of land and buildings</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 (£512 million) and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the Council and group financial statements is not materially different from the current value at the financial statements date, where a rolling programme is used</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.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work evaluated the competence, capabilities and objectivity of the valuation expert discussed with the valuer the basis on which the valuation was carried out challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding of the Council's valuer's report and the assumptions that underpin the valuation. tested revaluations made during the year to see if they had been input correctly into the Council's asset register 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. 	<p>Our work identified the following issues:</p> <ul style="list-style-type: none"> Indexation had not been applied to the council dwellings for the 2019/20 year. We challenged the valuer on the rationale and the supporting evidence supporting the decision, which was not in line with previous practice. The Council has now decided to apply indexation to the value of its council dwellings, which is a material adjustment. The Council's leisure centres had been revalued downwards by the valuer, in consultation with the Council's engineer, due to changes in the judgements made in respect of overall asset lives and remaining useful economic lives (UJEL) in 2019/20. When these judgements were challenged by the audit team, management and the valuer have revisited the valuations and underlying assumptions. This led to a material adjustment to the accounts. Our testing of the floor area source data used for the valuation of Haslemere Leisure Centre identified a discrepancy in the calculation. Using the floor area that was evidenced resulted in a difference of £331k. This is shown as an unadjusted item in Appendix C. Management provided a description of the logic and process of how they had considered the year end value of properties that have not been valued, and their reasonableness. They were however unable to provide supporting evidence or figures to demonstrate the potential change in valuation of these properties. Therefore we carried out our own procedures, applying indices to the assets not revalued. Our work identified a variance of £955k from our expectation, thereby providing assurance that the value of properties not revalued in the year were not materially different from the current value at year end. A member of the finance team on secondment from finance was closely involved in the decision making process of the internal valuer. Whilst clear separation of roles can be difficult for relatively small councils, in future greater demarcation of these respective roles should be put in place, as the valuation expert should be objective and separate from the preparation of the financial statements. <p>Management are required to ensure that they have the assurance that they require that the accounts are free from material misstatement. This would include assurances over the work of management's experts, including the valuer and the actuary. This is the second successive year where there has been material adjustments to PPE valuations.</p> <p>We will be including an emphasis of matter paragraph in our audit opinion in respect of the material uncertainty in the internal valuer's report.</p>

Audit of the Financial Statements

Significant Audit Risks - 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	Findings and conclusions
<p>Valuation of the net pension liability 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 and group accounts.</p> <p>The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£68 million 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.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> 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; evaluated the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work; assessed the competence, capabilities and objectivity of the actuary who carried out the Council's pension fund valuation; assessed the accuracy and completeness of the information provided by the Council to the actuary to estimate the liability; 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; undertook 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; and obtained assurances from the auditor of Surrey 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. 	<p>Our work identified that the pension liability in the financial statements and the figure in the actuary's IAS19 report differ by £586k, which is due to the Council reflecting actual cumulative payments to the fund of £102,186, as opposed to £102,772k per the actuary's report. This difference however cannot be estimated with certainty by the Council, who have agreed to adjust this in the 2020/21 accounts. The uncertainty, which is not material, is therefore shown as an unadjusted item in Appendix C.</p> <p>We will be including an emphasis of matter paragraph in our audit opinion in respect of the material uncertainty in Surrey Pension Fund's valuation reports for pooled property and private equity investments.</p>

Audit of the Financial Statements

Significant Audit Risks - 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	Findings and conclusions
<p>Management override of internal controls</p> <p>Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management override 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 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"> evaluated the design effectiveness of management controls over journals analysed the journals listing and determined the criteria for selecting high risk unusual journals tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration gained an understanding of the accounting estimates and critical judgements applied made by management and consider their reasonableness with regard to corroborative evidence evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions. 	<p>Our audit work on journals has not identified any issues in respect of management override of controls.</p>

Audit of the Financial Statements

Audit opinion

We gave an unqualified opinion on the group's financial statements on 2 December 2020.

Preparation of the financial statements

The Council presented us with draft financial statements in July in accordance with the agreed timescale. All information and explanations requested from management was provided. However there were a number of delays in some areas during the audit where there were difficulties in the provision of detailed population breakdowns for some areas and in the subsequent sample evidence. HRA debtors and PPE revaluations were particular areas where we encountered delays.

Issues arising from the audit of the financial statements

We reported the key issues from our audit to the Council's Audit Committee on 30 November 2020.

As a result of the issues arising from our work on the valuation of land and buildings we recommended that management must ensure that their processes for how they gain assurance over the PPE valuation work are robust. This should include senior officer review and challenge of the work and findings of management's experts. The recommendation was accepted by management.

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 alongside the draft Statement of Accounts in July.

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 carried out work in line with instructions provided by the NAO. 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 Waverley Borough in accordance with the requirements of the Code of Audit Practice on 2 December 2020.

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 April 2020 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 November 2020, we agreed recommendations to address our 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 2020.

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	Findings and conclusions
<p>Financial sustainability</p> <p>The Council has set a balanced budget for 2020/21, which includes a challenging savings target of £1.9m. The Medium Term Financial Plan shows a cumulative projected budget shortfall of £5.4m over the 2020/21 to 2023/24 period.</p>	<p>Due to the Covid-19 crisis, the Council took a Contingency Revised budget for 2020/21 to Council on 11 August 2020. This was to address some significant adverse variances to the original approved budget that had been caused by the coronavirus. The impact on the budget was identified by management as £6.6m. This results from direct costs of the Council deploying staff to its own services and to implement government mandated schemes, and then direct income losses due to enforced closures of facilities, including leisure centres and museums and consequential losses such as car park income and slow recovery after reopening facilities. The Council has not used the furlough scheme but has incurred overtime costs.</p> <p>The Council stopped all recruitment and non-essential spending as an interim measure in April 2020 to combat these challenges and has received Covid-19 support grant of £1.4m to date from the Government, leaving £5.2m of the budget gap to be mitigated by the Council. The report sets out that £2.9m is being drawn from the Council's reserves and £2.3m from budgetary savings in the year.</p> <p>This unplanned draw down on reserves has put additional pressure on the Council, when it already had to identify savings of £5.4m over the life of the Medium Term Financial Plan (MTFP). As a result the Council launched its Recovery Change and Transformation (RCT) programme, phase 1 of which was the Contingency Revised Budget. Phase 2 of the Programme is looking at the medium term impacts of Covid. This will include new working practices, to see what can be learned from the experiences of delivering the Council's services during lockdown. There are ten separate projects included within the RCT Programme. As part of this process the MTFP will also be reviewed, which is critical given the revised budget that had to be set in the year and the knock on impact of this on the assumptions within the MTFP.</p> <p>We are satisfied that the Council has suitable arrangements in place for financial resilience but as with other councils there are significant challenges to be resolved. The Council's current MTFP has a gap of £5.4m over the 2020/21 - 2023/24 period. This was before the Covid-19 crisis that has led to contingency revised budget for 2020/21 to address a budget gap of £6.6m. The Council is now considering the impact of Covid-19 and the associated budget changes in 20/21 on its medium term financial position. The Recovery Change and Transformation Programme is a critical piece of work for the Council to determine how it will deliver its services going forward. This represents a considerable challenge for the Council given the savings it has had to make in recent years.</p>

Value for Money conclusion

Value for Money Risks - continued

Risks identified in our audit plan	Findings and conclusions
<p>Commercial Property Portfolio</p> <p>The Council are looking to invest further in property beyond its Local Enterprise Partnership (LEP) area into what it defines as its “area of economic opportunity” to provide a source of revenue to support the delivery of its Corporate Strategy. This is a developing area of activity for local government as highlighted by the recent NAO report “Local authority investment in commercial property”. The Council needs to ensure that such investments do not expose it to unnecessary risks within the commercial property sector.</p>	<p>We have reviewed the arrangements that the Council have put in place when considering its commercial property investments.</p> <p>The Council sets its Capital Strategy for 2020/21 in February 2020. The Council’s Property Investment Strategy is an Annex to the overarching Capital Strategy and is subject to the review of the Property Investment Advisory Board.</p> <p>The Executive has the authority to bid, negotiate and complete on property acquisitions and investments, with the performance being monitored by the Value for Money Overview and Scrutiny Committee. A business case must be produced for all cases, supported by financial modelling. Before the investment proceeds it must determine:</p> <ul style="list-style-type: none"> • The reason for the investment • The powers under which the investment is made • The extent to which the capital invested is placed at risk • The impact of any potential losses on financial sustainability <p>There is then a governance framework in place, with the Property Investment Advisory Board playing a key role in scrutinising and challenging proposals, and ensuring that appropriate due diligence has been carried out. They also ensure that the strategic direction of the portfolio and investment principles are in line with the strategy.</p> <p>Each property will have an exit strategy in place to ensure that the Council can take action to prevent further loss should its objectives/required return not be achieved.</p> <p>The Property Investment Strategy arrangements would appear to be appropriate but there has been no activity outside of the Waverley area to assess how this is working in practice for property outside the LEP area.</p> <p>The Council have obtained legal advice from a QC who has advised a number of councils who are looking at extending their commercial property portfolio outside of their area. This advice is supportive of the Council’s plans but it should be noted that this continues to be a area where guidance is developing. Investment property remains a priority in the Council’s Medium Term Finance Plan, however due to the recent consultation on public sector borrowing and the potential exclusion of investment for purely return from PWLB, the Investment Strategy is being revisited alongside the MTFP revision.</p> <p>The Council has not invested in property outside of the Waverley area currently, although its Property Investment Strategy would allow it to do so. This continues to be a fast moving area in Local Government and the Council is revisiting its strategy in the light of potential changes to regulations for investments funded from PWLB as part of the review of the MTFP. We have not identified a risk to our VFM conclusion.</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 2020
Audit Findings Report	November 2020
Annual Audit Letter	December 2020

Fees

	Planned £	Actual fees £	2018/19 fees £
Statutory audit	41,494	41,494	41,494
Audit fee variations	7,500	29,885	7,200
Total fees	48,994	71,379	48,694

Audit fee variation

As outlined in our audit plan, the 2019-20 scale fee published by PSAA of £41,494 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.

Fee variations are subject to PSAA approval.

Area	Reason	Fee proposed
Pensions – IAS 19	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.	1,750
PPE Valuation – work of experts	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.	1,750
Raising the bar	The Financial Reporting Council (FRC) has highlighted that the quality of work by all audit firms needs to improve across local audit. This will require additional supervision and leadership, as well as additional challenge and skepticism in areas such as journals, estimates, financial resilience and information provided by the entity.	2,500
New standards / developments	New standards have been introduced since PSAA's original scale fee was set in March 2018. We did not raise fees in 2018/19 but we are no longer able to sustain this position for 2019/20.	1,500
Additional time needed to complete the audit	Additional audit time as a result of the underlying additional time requirements of working through the lockdown and other restrictions on movement during the pandemic, as well as additional time required to resolve the valuation and other issues encountered during the audit, offset by a reduction for us not needing to travel to undertake the audit (time and expenses).	22,385
Total		29,885

A. Reports issued and fees continued

Fees for non-audit services

Service	Fees £
Audit related services	
- Certification of Housing benefits grant	29,000*
- Certification of Housing capital receipts grant	3,000*
Non-Audit related services	
- None	-

* Final fees TBC – Work is in progress

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.



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