The Annual Audit Letter
For London Borough of Sutton

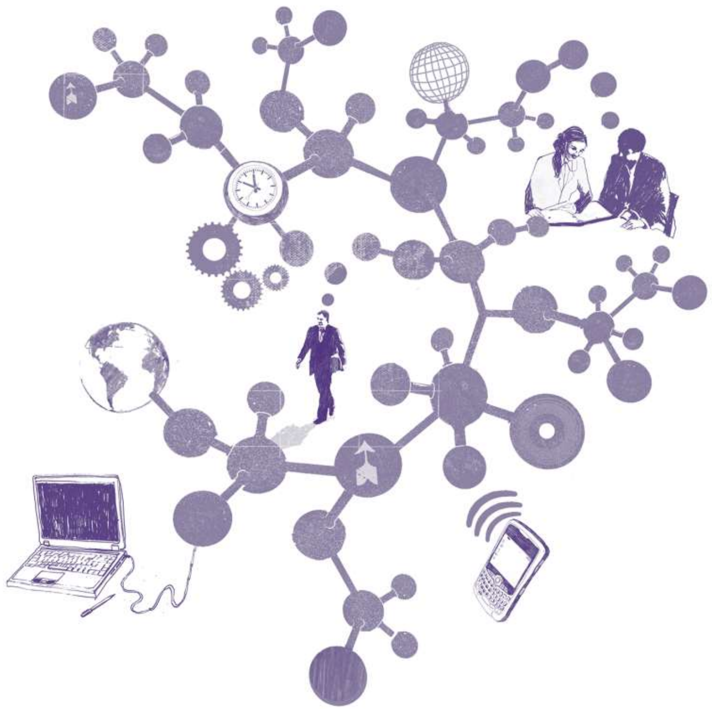
Year ended 31 March 2017

October 2017

Iain Murray
Engagement Lead
T 020 7728 3328
E iain.g.murray@uk.gt.com

Paul Jacklin
Senior Manager
T 020 7728 3263
E paul.j.jacklin@uk.gt.com

Keith Mungadzi
Executive
T 020 7728 2393
E keith.mungadzi@uk.gt.com



Contents

Executive summary

Purpose of this letter

Our Annual Audit Letter (Letter) summarises the key findings arising from the work we have carried out at London Borough of Sutton (the Council) for the year ended 31 March 2017.

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

We reported the detailed findings from our audit work to the Council's Audit Committee (as those charged with governance) in our Audit Findings Report on 21 September 2017.

Our responsibilities

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

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

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

Our work

Financial statements opinion

We gave an unqualified opinion on the Council's financial statements on 27 September 2017.

Value for money conclusion

We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources during the year ended 31 March 2017. We reflected this in our audit opinion on 27 September 2017.

Whole of government accounts
We completed work on the Council's consolidation return following guidance issued by the NAO and issued an unqualified report on 27 September 2017.

Certificate
We certified that we had completed the audit of the accounts of London Borough of Sutton in accordance with the requirements of the Code on 27 September 2017.

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 2017. We will report the results of this work to the Audit Committee in our Annual Certification Letter.

Working with the Council
From 2017/18, the statutory deadlines for preparation and audit of the financial statements will be brought forward and the Council will be required to produce draft statements by 31 May, and secure an audit opinion by 31 July 2018.
We will work in partnership with the Council to complete a substantial amount of early audit testing prior to March 2018 which will help to drive efficiencies within the year end audit process.
Moving towards an earlier deadline, particularly within the more complex environment within which you now operate, will require an element of redesign of some of the closedown processes, arrangements and internal business processes. The Council are currently reviewing the finance structure and financial processes as part of joint working with the Royal Borough of Kingston upon Thames. We have worked with many large clients to successfully implement faster close and will continue to work with the Council during the coming year to support the Council in achieving the earlier 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
October 2017

Audit of the accounts

Our audit approach

Materiality

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

We determined materiality for our audit of the Council's accounts to be £8.6 million, which is 2% of the Council's gross revenue expenditure. We used this benchmark, as in our view, users of the Council's accounts are most interested in how it has spent the income it has raised from taxation and grants during the year.

We set a lower threshold of £428,000, above which we reported errors to the Audit Committee in our Audit Findings Report.

Pension Fund

For the audit of the London Borough of Sutton’s Pension Fund accounts, we determined materiality to be £6.2 million, which is 1% of the Fund's net assets. We used this benchmark, as in our view, users of the Pension Fund accounts are most interested in the value of assets available to fund pension benefits.

We set a threshold of £309,000 above which we reported errors to the Audit Committee.

The scope of our audit

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

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

We also read the narrative report and annual governance statement to check they are consistent with our understanding of the Council and with the accounts included in the Statement of Accounts on which we gave our opinion.

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

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

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

Audit of the accounts - Council

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
The revenue cycle includes fraudulent transactions Under ISA (UK&I) 240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue. This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.	Having considered the risk factors set out in ISA240 and the nature of the Council's revenue streams, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because: • There is little incentive to manipulate revenue recognition. • Opportunities to manipulate revenue recognition are very limited • The culture and ethical frameworks of local authorities, including the Council, mean that all forms of fraud are seen as unacceptable.	Our audit work has not identified any issues in respect of revenue recognition.
Management over-ride of controls Under ISA (UK&I) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities.	We have undertaken the following work in relation to this risk: • Review of accounting estimates, judgments and decisions made by management. • Review of journal entry process and selection of large and unusual journal entries for testing back to supporting documentation. • Review of accounting estimates, judgements and decisions made by management. • Review of unusual significant transactions.	Our audit work has not identified any evidence of management over-ride of controls. In particular the findings of our review of journal controls and testing of journal controls and testing of journal entries has not identified any significant issues. .

Audit of the accounts - Council

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
The expenditure cycle includes fraudulent transactions Practice Note 10 requires us to consider the risk of material misstatement due to fraudulent financial reporting that may arise from manipulation of expenditure recognition, especially where the body is required to meet targets.	We considered the expenditure cycle risk and do not consider it to require additional audit procedures. The lack of specific performance targets which you are required to meet means there is limited incentive for fraudulent manipulation. The Council's culture means that such manipulation would be seen as unacceptable. The nature of expenditure streams also means that material fraud in expenditure recognition would be difficult to perpetrate and conceal. Our normal substantive audit procedures including work we completed in relation to the risk of management override of controls, operating expenses and employee remuneration adequately address the risk of fraud through provisions and accruals.	Our audit work has not identified any issues in respect of fraudulent expenditure transactions.
Valuation of property, plant and equipment The Council revalue assets on a rolling basis. over a five year period. The Code requires that you ensure that the carrying value at the balance sheet date is not materially different from the current value. This represents a significant estimate by management in the financial statements.	We have undertaken the following work in relation to this risk: • Review of management's processes and assumptions for the calculation of the estimate. • Review of the competence, expertise and objectivity of any management experts used. • Review of the instructions issued to valuation experts and the scope of their work. • Discussions with the Council's valuer about the basis on which the valuation was carried out, challenging the key assumptions. • Review and challenge of the information used by the valuer to ensure it was robust and consistent with our understanding. • Testing of revaluations made during the year to ensure they were input correctly into the Council's asset register. • Evaluation of the assumptions made by management for those assets not revalued during the year and how management satisfied themselves that these were not materially different to current value.	Our audit work has not identified any significant issues in relation to the risk identified.

Audit of the accounts - Council

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
Valuation of pension fund net liability The Council's pension fund net liability, as reflected in the balance sheet, represents a significant estimate in the financial statements.	We have undertaken the following work in relation to this risk: • Identifying the controls put in place by management to ensure that the pension fund net liability is not materially misstated and assessing whether those controls were implemented as expected and whether they were sufficient to mitigate the risk of material misstatement. • Review of the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation. • Gaining an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made. • Review of the consistency of the pension fund net liability disclosures in notes to the financial statements with the actuarial report from the Council's actuary.	Our audit work has not identified any significant issues in relation to the risk identified.

Audit of the accounts – Pension Fund

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

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
The revenue cycle includes fraudulent transactions Under ISA (UK&I) 240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.	Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the London Borough of Sutton Pension Fund, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because: • there is little incentive to manipulate revenue recognition; • opportunities to manipulate revenue recognition are very limited; and • the culture and ethical frameworks of local authorities, including the London Borough of Sutton Council as the administering body, mean that all forms of fraud are seen as unacceptable.	Our audit work has not identified any issues in respect of revenue recognition.
Management over-ride of controls Under ISA (UK&I) 240 it is presumed that the risk of management over-ride of controls is present in all entities.	We have undertaken the following work in relation to this risk: • review of journal entry process and selection of unusual journal entries for testing back to supporting documentation • review of accounting estimates, judgements and decisions made by management • review of unusual significant transactions.	Our audit work has not identified any evidence of management over-ride of controls. In particular our testing of journal controls and journal entries into the general ledger has not identified any significant issues.
Level 3 Investments (Valuation is incorrect) Under ISA 315 significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.	We have undertaken the following work in relation to this risk: • Updated our understanding of the processes and control in place to estimate the valuation of these assets. • For a sample of investments we tested valuations by obtaining and reviewing the audited accounts at latest date for individual investments and agreeing these to fund manager reports at that date. Reconciliation of those values to the values at 31st March with reference to known movements in the intervening period. • We reviewed the nature and basis of estimated values and consider what assurance management has over the year end valuation provided for these type of investments. • Reviewed the competence, expertise and objectivity and objectivity of management experts used. • Reviewed the qualifications of the fund managers as experts to value the level 3 investments at year end and gain an understanding of how the valuation of these investments has been reached.	Our work has not identified any significant issues in relation to the risk identified.

Audit of the accounts

Audit opinion

We gave an unqualified opinion on the Council's accounts on 27 September 2017, in advance of the 30 September 2017 national deadline.

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

- the draft financial statements were submitted for audit by the end of May 2017; this is a month earlier than the previous year and demonstrates the Council are well placed to meet the early close deadline for next year.
- working papers were provided in accordance with the agreed protocol. The overall quality of the working papers were good.
- we identified a small number presentation and disclosure issues in the draft financial statements which the Council subsequently amended.
- responses to audit queries were generally timely and we will continue to work with management to improve the process for next year when the deadlines are tighter

Issues arising from the audit of the accounts

We reported the key issues from our audit of the accounts of the Council to the Council's Audit Committee on 21 September 2017.

We identified one adjustment of £1,528k affecting the Council's reported financial position relating to the revaluation of Brandon Hill Woodfield Campus that was not correctly reflected in the financial statements. This had no impact on the Council's General Fund balance.

Pension fund accounts

We also reported the key issues from our audit of accounts of the Pension Fund hosted by the Council to the Council's Audit Committee on 21 September 2017. In addition to the key audit risks reported above, we identified a few minor presentational issues which the Council subsequently amended.

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 with the draft accounts in line with the national deadlines.

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

Whole of Government Accounts (WGA)

We carried out work on the Council's consolidation schedule in line with instructions provided by the NAO . We issued a group assurance certificate which did not identify any issues for the group auditor to consider on 27 September 2017.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice (the Code), following the guidance issued by the NAO in November 2016 which specified the criterion for auditors to evaluate:

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

Key findings

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

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

Overall VfM 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 2017.

Value for Money

Table 2: Value for money risks

Risk identified	Work carried out	Findings and conclusions
Financial sustainability and savings plans The Council have historically managed their finances well and have consistently achieved planned savings targets. The Council plan to set a balanced budget for 2017/18. However, the medium term financial strategy over the next three years shows that after a balanced budget in 2017/18 savings of £3.6m in 2018/19 and a further £2.2m in 2019/20 will be required to be identified. This is after a planned use of reserves of £5.2m over the period.	We undertook the following procedures: - reviewed the Council's progress in updating its medium term financial plan; - reviewed reports to Members; - reviewed the savings plans for 16/17 and 17/18; and - met with key officers to discuss the major strategic challenges and the Council's proposed response	The Council have a very good recent history of dealing with the challenges in their financial environment. However, the financial environment is becoming even more challenging and in 2016/17 the Council's outturn position is a net overspend of £2.5m which represents 1.7% against an approved net budget of £144.9m. The overspend is predominantly within Children's safeguarding due to continued pressure with placement costs, and costs associated with staff recruitment and retention into child protection teams. There have also been additional court costs arising from increased numbers of children being taken into care. The other major area of overspend in 2016/17 is against the Dedicated Schools Grant (DSG) budget. The Council had a carry forward balance from 2015/16 of £1.5m however, the overspend increased substantially in 2016/17 to £2.259m. This was primarily within the High Needs element, and results from costs of supporting educational attainment for children with Special Educational Needs (SEN) including increased pupil numbers and higher placement costs. There is a deficit of £0.735m to be carried forward into 2017/18. The DSG is a ring-fenced fund and the overspend does not currently impact the general fund balance. Such overspends would normally be expected to be recovered against future DSG allocations. The risk is if these overspends continue then there could be an impact on the Council's general fund. The Council have set a balanced budget for 2017/18 with a contribution from the risk reserve of £1.228m, a mixture of savings, adopting a 1.99% rise in council tax and adopting the 2% adult social care precept. There remains a budget gap during the period of the MTFP which is £2.2m in 2018/19 rising to £11.5m by 20/21. The budget gap arises largely from continued reductions in grant funding from central government, but also takes into account expected cost increases, demand pressures and unfunded or inadequately funded new responsibilities. The cumulative funding gap assumes that you will utilise the option of a 2% council tax 'precept' for social care in 2018/19 and 2019/20, but no other council tax increases are assumed over the period. It takes into account £6.1m of savings in 2018/19 and £6.5m in 2019/20 already planned. In order to balance the budget in 2020/21 additional savings of £11.5m will be required. The Council remain committed to achieving transformational service change and delivering savings via its Smarter Council programme. Part of this is manifested in closer working with local NHS bodies and the continued development of alternative delivery models with local authorities in the South West London area. Members and officers recognise that difficult decisions will need to be made as regards service provision, so that the Council are able to deliver a strong financial performance and delivery of recurrent financial savings. The Council's The Council is forecasting a £4.5m year end deficit after the first quarter in 2017/18.

Appendix A: Reports issued and fees

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

Fees

	Proposed fee £	Final fee £
Council audit	94,290	94,290
Grant certification	15,068	TBC
Total audit fees (excluding VAT)	**109,358**	**TBC**

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

Reports issued

Report	Date issued
Audit Plan	16 March 2017
Audit Findings Report	21 September 2017
Annual Audit Letter	October 2017

Fees for other services

Service	Fees £
Audit related services:	
• Pooling of Capital Receipts Return	**TBC**
• Teachers Pension certification 2016/17	**TBC**
Non-audit services • **none**	**Nil**

Non- audit services

- For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The table above summarises all other services which were identified.

- We have considered whether other services might be perceived as a threat to our independence as the Council's auditor and have ensured that appropriate safeguards are put in place, as reported in our Audit Findings Report.

Reports issued and fees continued

We have considered whether other services might be perceived as a threat to our independence as the Council's auditor and have ensured that appropriate safeguards have been applied to mitigate these risks.

	Service provided to	Fees	Threat?	Safeguard
Audit related services				
	Pooling of Capital Receipts Return and Teachers Pension Certification	TBC	No	Level of fees are significantly below the audit fee. You prepare all the figures for the claim which we independently audit
Non-audit services				
	None			
	TOTAL	TBC		

The above non-audit services are consistent with the Council's policy on the allotment of non-audit work to your auditor and have been approved by the Audit Committee.