



# The Annual Audit Letter for South Lakeland District Council

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**Year ended 31 March 2019**

**August 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 South Lakeland District Council (the Council) for the year ended 31 March 2019.

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 25 July 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 financial statements as set out in section two
- assess the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources, known as the value for money conclusion, as set out in 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.

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<b>Materiality</b>	We determined materiality for the audit of the Council's financial statements to be £1,372,000, which is 2% of the Council's gross revenue expenditure.
<b>Financial Statements opinion</b>	We gave an unqualified opinion on the Council's financial statements on 30 July 2019.
<b>Whole of Government Accounts (WGA)</b>	We completed work on the Council's consolidation return following guidance issued 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. We reflected this in our Audit Report opinion to the Council on 30 July 2019.
<b>Certificate</b>	We certified that we have completed the audit of the financial statements of South Lakeland District Council in accordance with the requirements of the Code of Audit Practice on 30 July 2019.

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# Executive Summary

## 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 June and July 2019, delivering the financial statements before the deadline.
- 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 updates to the Audit Committee covering best practice. We also shared our thought leadership reports and wider sector insights
- Providing training – we provided your teams with access to training on financial statements and annual reporting.

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 2019

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# Audit of the Financial Statements

## 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 financial statements to be £1,372,000, which is 2% 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, due to the sensitivity of this balance. We set a lower threshold of £5,000, 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 financial statements to check it is consistent with our understanding of the Council, such as the Narrative 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 Council's business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks as well as 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>Income from fees and charges</b></p> <p>Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. For South Lakeland District Council, we have concluded that the greatest risk of material misstatement relates to fees and charges income. We have therefore identified the occurrence and accuracy of fees and charges income as a significant risk, which was one of the most significant assessed risks of material misstatement and a key audit matter.</p> <p>We have rebutted this presumed risk for the other revenue streams of the Council, as other income streams are primarily derived from grants or formula based income from central government and tax payers.</p>	<p>We have:</p> <ul style="list-style-type: none"> <li>evaluated the Council's accounting policy for recognition of income from fees and charges for appropriateness</li> <li>gained an understanding of the Council's system for accounting for income from fees and charges and evaluated the design of the associated controls</li> <li>agreed, on a sample basis, amounts recognised as income from fees and charges in the financial statements to gain assurance over occurrence and accuracy.</li> </ul>	<p>Our audit work has not identified any issues in respect of the risk that revenue may be misstated as a result of the improper recognition of income.</p>
<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.</p>	<p>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 to supporting evidence</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 has not identified any issues in respect of management override of controls.</p>

# Audit of the Financial Statements

## Significant Audit Risks - continued

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p><b>Valuation of land, buildings and investment property</b></p> <p>The Council revalues its land and buildings on a rolling four-yearly basis. This valuation represents a significant estimate by management in the financial statements due to the size of the asset base, numbers involved and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the financial statements is not materially different from the current value or the fair value (for surplus assets) 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, and a key audit matter.</p>	<p>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 valuation experts and the scope of their work</li> <li>evaluated the competence, capabilities and objectivity of the valuation expert</li> <li>discussed with the valuer 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>compared asset valuation movements against valuation indices to assess reasonableness of asset valuation movements.</li> </ul>	<p>Our work identified one control weakness in relation to the overall review of the external valuer's report. At the year-end the final report had not been compared with the asset valuation changes made on the asset register/ledger. As a result the revaluation of the lake assets had not been processed.</p> <p>Other than this matter, our audit work has not identified any issues in respect of valuation of land, buildings and investment property.</p>

# Audit of the Financial Statements

## Significant Audit Risks - continued

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p><b>Valuation of pension fund net 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 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>The legal ruling around age discrimination (McCloud - Court of Appeal) has implications for pension schemes where they have implemented transitional arrangements on changing benefits, such as the Local Government Pension Scheme. During June 2019 the Supreme Court rejected the Government's application to appeal the ruling, therefore the Council had to assess the potential impact on its pension fund net liability.</p>	<p>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 evaluated the design of the associated controls</li> <li>evaluated the instructions issued by management to their management expert (an actuary - Mercer) 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>undertook procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as our auditor's expert) and performing any additional procedures suggested within the report</li> <li>obtained assurances from the auditor of Cumbria Local Government Pension Scheme 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> </ul> <p>Due to the impact of the McCloud ruling, we also:</p> <ul style="list-style-type: none"> <li>reviewed the processes used by management in the evaluation of the impact of the McCloud judgment and the quantification of the potential impact on the financial statements, including how management confirmed the adequacy of work carried out by its actuary</li> <li>assessed and challenged the relevance and reasonableness of all significant assumptions and methods used to generate the McCloud estimate by the actuary, including understanding how the organisation's workforce profile could affect this as the matter centres around age discrimination and potential increases in pension liability</li> <li>considered whether the estimate of the potential impact is in line with our expectations</li> <li>checked management's amendments to the financial statements for the impact calculated by Mercer.</li> </ul>	<p>The Council engaged Mercer its Actuary to estimate the potential impact on the pension fund net liability as a result of the McCloud ruling. The outcome of this was an estimated increase in the net liability of £0.608m.</p> <p>Management has assessed the work undertaken by Mercer and judged that the potential impact on the Council is sufficiently material to have updated the financial statements in relation to these amounts.</p> <p>We have reviewed the analysis performed by the actuary, and consider that the approach that has been taken to arrive at this estimate is reasonable. We are satisfied that the Council has appropriately accounted for this liability increase.</p>



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# Audit of the Financial Statements

## Audit opinion

We gave an unqualified opinion on the Council's financial statements on 30 July 2019.

## Preparation of the financial statements

The Council 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 July 2019.

In addition to the key audit risks reported above, we identified a number of minor disclosure changes required to the financial statements, which did not impact the Council's primary financial statements. We also made one control recommendation relating to the valuation of land and buildings, which is included in Appendix B.

## 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 to a good standard, in line with the CIPFA Code and relevant supporting guidance. The Council did update its Narrative Report post audit to make it clear on its value created as well as the its significant risks and opportunities. 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 on the Council's Data Collection Tool in line with instructions provided by the NAO. We issued an assurance statement, which confirmed the Council was below the audit threshold on 30 July 2019.

## Other statutory powers

We also have additional powers and duties under the Local Audit and Accountability Act 2014, 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.

We did not have to use any of our other statutory powers during 2018/19.

## Certificate of closure of the audit

We certified that we have completed the audit of the financial statements of South Lakeland District Council in accordance with the requirements of the Code of Audit Practice on 30 July 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.

## 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 2019.

# Value for Money conclusion

## Value for Money Risks

Significant risk	Findings
<p data-bbox="45 292 93 335">1</p> <p data-bbox="140 292 414 321"><b>Financial sustainability</b></p> <p data-bbox="140 321 513 628">On 24 July 2018 the Council approved the business case, including the new operating model for the Council, under the Customer Connect Programme. A key part of this change programme relates to a management restructure, with the key focus on bringing the operational decision making closer to the customer.</p> <p data-bbox="140 649 513 935">The new structure will take effect from 1 April 2019 and it is expected to contribute £0.740m of savings in 2019/20 and £1.55m from 2020/21. The MTFP presented to Council on 26 February 2019 showed that, after inclusion of the Customer Connect savings a balanced budget can be achieved in 2019/20.</p> <p data-bbox="140 949 513 1235">However, from 2020/21 additional efficiencies are required of £0.62m and this rises to £1.985m in 2023/24. Some savings have been identified from the capital programme from 2019/20 onwards but there are still significant efficiencies to be identified to achieve a medium term balanced position.</p>	<p data-bbox="528 292 714 321"><b>2018/19 outturn</b></p> <p data-bbox="528 321 1995 406">The Council has a comprehensive approach to its medium term financial planning and budgeting. The strategy is aligned to the Council's corporate priorities and aims and takes into account the major service strategies and plans, the external financial environment, the overall financial demands of services and the Council's existing and projected financial resources.</p> <p data-bbox="528 421 1995 556">The Council delivered a balanced budget in 2018/19. Whilst service expenditure was £210,000 more than budget when the impact of the carry forward amounts are taken into account there is a surplus of £270,000 on the general fund. The full details of service variances have been reported through the out-turn report to Cabinet on 17 July 2019 and Council 23 July 2019. The largest service variance relates to Performance and Innovation, where Customer Connect costs were higher than budget as a result of the transitional staff costs. However, these were offset by management of staff costs elsewhere across services.</p> <p data-bbox="528 571 1995 678">The capital outturn for 2018/19 was £4.025m against a budget of £7.661m. All of the £3.636m underspend/slippage on the capital programme has been carried forward and re-profiled over future years. The majority of this reprofiling relates to schemes where the Council is working with other partners to deliver projects and it has been waiting for the completion of actions by these other parties before the project could progress.</p> <p data-bbox="528 692 1995 778">The Council's capital programme included two major new schemes funded from capital grants – the Coastal Communities Fund project at Grange over Sands and the Kendal ERDF funded flood works. Other recurring sources of capital income have declined significantly over the last five years.</p> <p data-bbox="528 792 1995 849">Approximately half of the Council's income is received from car parking and lake income. However, overall income from car parking has not increased since 2011/12. The MTFP has included an increase in income levels in line with RPI.</p> <p data-bbox="528 863 1995 999">Overall total usable reserves at 31 March 2019 remain consistent with the balance as at 31 March 2018 at a value of £24.5m. The Council's earmarked reserves stand at £16.4m at 31 March 2019 and these include two general fund reserves; a general fund working balance of £1.5m and a general reserve which stands at £4.8m at 31 March 2019. Whilst this general reserve decreased by £1.2m (20%) in year there has been a £0.8m of an increase in other revenue reserves fulfilling the decision to remove carried forward balances sitting in the general reserve into appropriate earmarked reserves.</p> <p data-bbox="528 1013 859 1042"><b>Medium Term Financial Plan</b></p> <p data-bbox="528 1042 1995 1270">The Medium Term Financial Plan (MTFP) for 2019/19 to 2023/24 was approved by the Council in July 2018 and updated in February 2019, demonstrates that appropriate steps were being taken to ensure a balanced budget position was maintained despite reduced Government funding. The Council has adopted a prudent approach to predicting changes to the future of funding, given the uncertainty caused by the Fair Funding Review and review of the Business Rates Retention Scheme, the outcomes of which are not expected until later in 2019/20, at the earliest. After use of reserves set aside for the Customer Connect programme the MTFP forecasts a balanced position for 2019/20 but cumulative budget gaps rising from £620,000 in 2020/21 to £1.985m in 2023/24. £500,000 per year of this budget gap arises directly from the assumptions made in the MTFP in relation to the funding reductions. We consider this to be prudent and a best practice approach.</p> <p data-bbox="528 1285 1995 1358">The level of earmarked reserves is expected to reduce from £16.4m at 31 March 2019 to £11.8m at 31 March 2020. This reduction is planned and is a result of the utilisation of the customer connect reserve and associated capital reserves. Reserves across the remainder of the period of the MTFP remain stable.</p>

# Value for Money conclusion

## Value for Money Risks

Significant risk	Findings
① Financial sustainability	<p data-bbox="526 319 741 344"><b>Customer Connect</b></p> <p data-bbox="526 348 1991 515">Customer Connect is the Council's digital innovation programme, which aims to provide customers with digital access to all council services 24/7, 7 days a week. As the streamlining of services progresses, this will release financial and other savings to meet budget pressures. Efficiencies from Customer Connect of £740,000 are included in the 2019/20 budget; this increases to £1.55m as a recurrent saving in 2020/21 and beyond. There are also expected to be indirect savings as a result of new ways of working, which have not yet been identified. The programme includes the preparation and implementation of a commissioning framework to review the need for services and to review how services should be provided, including decommissioning services where necessary.</p> <p data-bbox="526 529 1970 611">In Quarter One of 2019/20, the Council is reporting recurrent savings of £581,000 against the target of £740,000 from phase 1 of the programme, which was largely completed during May 2019. Phase 2 will be completed by the end of December 2019 and is expected to deliver the balance of the savings for 2019/20 and the recurring savings for 2020/21 onwards.</p> <p data-bbox="526 625 617 649"><b>Savings</b></p> <p data-bbox="526 654 1980 792">The Council has a good track record of delivering against its savings target. However, the forecast increasing budget gaps means that there needs to be continued focus on delivery of efficiencies. As well as using the commissioning framework to prioritise resources the Council is preparing a Commercial Strategy to ensure income is optimised and will explore further opportunities for joint working. The updated MTFP in February 2019, indicated that unless there are relevant earmarked resources, no revenue budget growth bids (including reductions in income) should be accepted for 2020/21, until all budget pressures are funded and the budget deficit is met.</p> <p data-bbox="526 835 658 859"><b>Conclusion</b></p> <p data-bbox="526 863 1991 945"><b>Based on the review of the arrangements in place during 2018/19 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. The Council can further enhance arrangements by continuing to closely monitor:</b></p> <ul data-bbox="526 978 1943 1059" style="list-style-type: none"><li>• and report on the run rate on the use of its usable reserves.</li><li>• the capital works with third parties so that better profiling of spend can be achieved and/or corrective action can be taken sooner to prevent slippage.</li></ul>

## A. Reports issued and fees

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

### Reports issued

Report	Date issued
Audit Plan	February 2019
Audit Findings Report	July 2019
Annual Audit Letter	August 2019

### Fees

	PSAA Scale fee £	Actual fees £	2017/18 fees £
Statutory audit	43,005	44,505	55,851
<b>Total fees</b>	<b>43,005</b>	<b>44,505</b>	<b>55,851</b>

### Audit fee variation

As outlined in our audit plan, the 2018-19 scale fee published by PSAA of £43,005 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. When the fee variation is taken into account the Council has still achieved a 20% reduction in audit fee from the 2017/18 audit.

Area	Reason	Fee proposed
Assessing the impact of the McCloud ruling	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.	£1,500
<b>Total</b>		<b>£1,500</b>

Fee variations are still subject to final PSAA approval.

## B. Action plan

We have identified one recommendation for the Council as a result of issues identified during the course of our audit. We have agreed our recommendation with management and we will report on progress on this recommendation during the course of the 2019/20 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	●	<p>The final valuation report for all assets provided by Lambert Smith Hampton was received in May 2019. Prior to receipt of this final report, the various valuations had been communicated to the Council via email. The valuation of the lake assets was not communicated in this manner but included on the final valuation report.</p> <p>As no comparison of the final report was made with the valuation changes made on the asset register/ledger the revaluation of the lake assets had not been processed. This resulted in the overall asset value being understated in the draft accounts.</p>	<p>Carry out a formal review of the final valuation report on an annual basis to ensure that all asset revaluations are accurately captured in the financial statements.</p> <p><b>Management response</b> Agreed, to include a reconciliation of the values provided by the Valuer with those required by the Council in its appointment letter and between the values received in year and the valuers final report.</p>

### Controls

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



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