



**Derby City Council
Draft - Audit results
report**

Year ended 31 March 2019

26 July 2019



EY

Building a better
working world



Private and Confidential

23 July 2019

Derby City Council
Council House
Corporation Street
Derby
DE1 2FS

Dear Audit and Accounts Committee Members

We are pleased to attach our audit results report for the forthcoming meeting of the Audit and Accounts Committee. This report summarises our preliminary audit conclusion in relation to the audit of Derby City Council for 2018/19. We will issue our final report at the Audit Committee meeting scheduled for 30 July 2019.

We have substantially completed our audit of Derby City Council for the year ended 31st March 2019. Subject to concluding the outstanding matters listed in our report, we confirm that we expect to issue an unqualified audit opinion on the financial statements in the form at section 3 before the accounts publication date of 31 July 2019. We are reporting by exception about your arrangements to secure economy, efficiency and effectiveness in your use of resources.

This report is intended solely for the use of the Audit and Accounts Committee, other members of the Authority, and senior management. It should not be used for any other purpose or given to any other party without obtaining our written consent.

We would like to thank your staff for their help during the engagement.

We welcome the opportunity to discuss the contents of this report with you at the Audit and Accounts Committee meeting on 30 July 2019.

Yours faithfully

Stephen Clark

For and on behalf of Ernst & Young LLP

Encl

Contents



Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website (www.psa.co.uk). This Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The 'Terms of Appointment (updated April 2018)' issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Results Report is prepared in the context of the Statement of responsibilities / Terms and Conditions of Engagement. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure - If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.



01 Executive Summary

Executive Summary

Scope update

In our audit planning report tabled at the 27 March 2019 Audit and Accounts Committee meeting, we provided you with an overview of our audit scope and approach for the audit of the financial statements. We carried out our audit in accordance with this plan, with the following exception:

- ▶ Changes in materiality: We updated our planning materiality assessment using the draft financial statements and have also reconsidered our risk assessment. Based on our materiality measure of gross expenditure on provision of services, we have updated our overall materiality assessment to £6.55m (Audit Planning Report – £6.54m). This results in updated performance materiality, at 50% of overall materiality, of £3.27m, and an updated threshold for reporting misstatements of £0.33m.
- ▶ For clarity, we are reporting an extension to the scope of the work on one area of focus. We identified the Local Government Pension Scheme as an area of audit focus and listed the procedures we intended to perform. Due to the result of the McCloud judgement in relation to pensions, the Government Actuary Department (GAD) issuing guidance, and the result of the courts that the Government appeal to exclude the LGPS was denied, we extended the procedures to assess the adjustment made to the financial statements in respect of the judgement, the assumptions this adjustment was based on, and management's process for obtaining and considering the adjustment.
- ▶ Similarly, the impact of Guaranteed Minimum Pensions (GMP) case on LGPS has been further considered since the drafting of the financial statements. The actuary for the Derbyshire County Pension Scheme concluded that the impact would not be material. We have carried out further analysis on the range of the estimate.
- ▶ The effect of the amendment to the pension liability is reported under section 4 Audit Differences

Status of the audit

We have substantially completed our audit of Derby City Council's financial statements for the year ended 31 March 2019 and have performed the procedures outlined in our Audit planning report. Subject to satisfactory completion of the following outstanding items we expect to issue an unqualified opinion on the Authority's financial statements in the form which appears at Section 3. However until work is complete, further amendments may arise:

- ▶ Conclude on the pensions disclosures (IAS 19) including the review of assumptions used in making the adjustment to pension liabilities for McCloud
- ▶ Conclude on income, expenditure, receivables, payable procedures
- ▶ Conclude on property, plant and equipment procedures
- ▶ Conclude on other disclosures which include work on IFRS 15
- ▶ Completion of the PFI disclosures review
- ▶ Receipt of a signed letter of management representation and Annual Governance Statement
- ▶ Completion of Subsequent event review procedures
- ▶ Final review of the Narrative Report and financial statements
- ▶ Receipt of the Group Reporting pack from BDO
- ▶ Receipt of 3rd party confirmations for cash balances.
- ▶ Completion of procedures required by the National Audit Office (NAO) regarding the Whole of Government Accounts (WGA) submission. It should be noted that we cannot formally conclude the audit and issue an audit certificate until we have completed the work necessary to issue our assurance statement in respect of the Authority's WGA consolidation pack.

Executive Summary

Audit differences

Audit differences arising from our audit to date can be found in section 4.

Areas of audit focus

Our Audit Planning Report identified key areas of focus for our audit of Derby City Council's financial statements. This report sets out our observations and conclusions, including our views on areas which might be conservative, and where there is potential risk and exposure. We summarise our consideration of these matters, and any others identified, in the "Areas of Audit focus" section of this report.

We ask you to review these and any other matters in this report to ensure:

- ▶ There are no other considerations or matters that could have an impact on these issues
- ▶ You agree with the resolution of the issue
- ▶ There are no other significant issues to be considered.

There are no matters, apart from those reported by management or disclosed in this report, which we believe should be brought to the attention of the Audit and Accounts Committee.

Control observations

We have adopted a fully substantive approach, so have not tested the operation of controls.

In addition, during the audit we identified a number of observations and improvement recommendations in relation to management's financial processes and controls.

We have set out our observations at section 7 of the report.

Executive Summary

Value for money

We have considered your arrangements to take informed decisions; deploy resources in a sustainable manner; and work with partners and other third parties. In our Audit Planning Report we identified six significant risks to our value for money conclusion.

We performed the work set out in our audit plan in response to these risks and have concluded that the Authority's arrangements for 5 of the 6 significant risks are now in place and embedded.

We note that there is weakness in arrangements identified over the management of the A52 Junction improvement scheme. The original estimated total scheme cost within the Authority's capital programme was £14.906m. In March 2018, Cabinet approved £2.157m, within the Highways and Transport programme, to fund the delivery of ancillary works to the main A52 junction improvement scheme - taking the total planned spend to £17.063m.

In late March 2018 it became apparent that there were significant previously undisclosed overspends on the project. Internal audit were commissioned to carry out an investigation into the project, and highlighted significant issues with the processes around project management, monitoring, procurement and decision making by key senior members at the Authority. The scheme design was revisited and the project costs are now estimated to be £43.2m, an additional £28.3m over its original budget. This provides evidence of weaknesses in proper arrangements for informed decision making, sustainable resource deployment and working with partners and other third parties

We concluded a qualified 'except for' VFM conclusion to be appropriate for the 2018/19 financial year. Details of our findings can be found in section 5 of this report.

Other reporting issues

We have reviewed the information presented in the Annual Governance Statement for consistency with our knowledge of the Authority. Management has agreed to update the statement to clarify the current position on the A52 project and actions being taken.

We have not yet performed the procedures required by the National Audit Office (NAO) on the Whole of Government Accounts submission.

We have no other matters to report.

Independence

Please refer to Section 9 for our update on Independence.



02

Areas of Audit Focus



Areas of Audit Focus

Fraud risk

Risk of fraud in revenue and expenditure recognition for year end accruals and capitalisation of revenue expenditure.

What is the risk?

Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

Having considered the factors for expenditure recognition, we believe the risk is focused on the year-end balance sheet and in particular the completeness and valuation of creditors and the existence and valuation of debtors. We also believe the risk is linked to the existence of capital expenditure arising from the potential to incorrectly capitalise revenue expenditure. There is also the risk of incorrect cut-off in relation to revenue and/or expenditure leading to transactions being reported in the wrong period.

What did we do?

- ▶ Documented our understanding of the processes and controls in place to mitigate the risks identified, and walked through the processes and controls to confirm our understanding
- ▶ Review and tested expenditure recognition policies.
- ▶ Review and discussed with management any accounting estimates on expenditure recognition for evidence of bias.
- ▶ Sample tested material revenue streams and operating expenditure
- ▶ Sample tested additions to property, plant and equipment to test whether the Council has inappropriately capitalised revenue expenditure.
- ▶ Tested the cut-off of income and expenditure to ensure transactions are recorded within the correct period to which they relate
- ▶ Developed a testing strategy to test material receivables and payables; and
- ▶ Performed a search for unrecorded trade payables at period year.

What are our conclusions?

- ▶ Our testing has revealed one cut-off error (totalling £499k) where the Council had under-accrued for revenue expenditure that was invoiced post year-end.
- ▶ We are satisfied that the level of undetected misstatements is sufficiently low to enable us to conclude that no material misstatement has arisen as a result of fraud in revenue and expenditure recognition.



Areas of Audit Focus

Fraud risk

Misstatements due to fraud or error

What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

What did we do?

- ▶ Test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements;
- ▶ Review and discuss with management any changes the methodologies of existing and new accounting estimates for evidence of bias;
- ▶ Enquire of management about risks of fraud and the controls put in place to address those risks;
- ▶ Evaluate the business rationale for significant unusual transactions; and
- ▶ Understand the oversight given by those charged with governance of management's processes over fraud.

What are our conclusions?

We have not concluded our testing, however from the testing carried out to date:

- ▶ We have not identified any material weaknesses in controls or evidence of material management override.
- ▶ We have not identified any instances of inappropriate judgements being applied.
- ▶ We did not identify any other transactions during our audit which appeared unusual or outside the Authority's normal course of business



Areas of Audit Focus

Significant risk

Valuation of land and buildings

What is the risk?

Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

The fair value of other land and buildings represents a significant balance in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges.

The Council has rolling valuation process , which annually values 20% of the land and building assets, is subject to a number of assumptions and judgements, which if inappropriate could result in a material impact on the financial statements. There is also a potential risk of material misstatement that the remaining 80% of unvalued assets may have experienced a material change in value which has not been identified and accounted for correctly.

What judgements are we focused on?

We focused on the following:

- ▶ The adequacy of the scope of the work performed by the valuer including their professional capabilities
- ▶ The reasonableness of the underlying assumptions used by the Authority's expert valuer

What did we do?

- ▶ Document our understanding of the processes and controls in place to mitigate the risks identified, and walk through those processes and controls to confirm our understanding
- ▶ Evaluate the competence, capabilities and objectivity of management's specialist.
- ▶ Review any terms of engagement or instructions issued to the valuer to ensure these are consistent with accounting standards. And assess if the instruction includes a specific instruction from the council to the valuer relating to an assessment on the unvalued population;
- ▶ Engage our valuation specialists to support our testing strategy and help evaluate the work of the Council's valuer specifically to assess if the movement on the unvalued population has been addressed appropriately
- ▶ Engage our valuation specialists to support our testing strategy and help evaluate the work of the Council's valuer.
- ▶ Perform appropriate tests over the completeness and appropriateness of information provided to the valuer
- ▶ Review the classification of assets and ensure the correct valuation methodology has been applied.
- ▶ Ensure the valuer's conclusions have been appropriately recorded in the accounts

What are our conclusions?

- ▶ The Council's PPE is valued by the District Valuation Office (DVO).
- ▶ We have reviewed the instructions and data provided to the valuer by the Council. We identified no issues.
- ▶ Our review of accounting entries at period end and those journals made in processing valuation adjustments did not reveal any instances of management intention to misreport the financial position.
- ▶ We have obtained input from EY's own valuation experts to review the work of the DVO and their qualifications.
- ▶ Our valuation specialist has reviewed the valuation methods used by management's specialist and internal valuer.

We are in the process of completing the valuation method review before we can conclude our work.





Areas of Audit Focus

Other areas of audit focus

Pension Liability Valuation

What is the risk?

The Local Authority Accounting Code of Practice and IAS19 require the Authority to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Derbyshire County Council.

The Authority's pension fund deficit is a material estimated balance and the Code requires that the net liability be disclosed on the Authority's balance sheet. At 31 March 2018 this totalled £376.9 million.

The information disclosed is based on the IAS 19 report issued to the Authority by the actuary to the Pension Fund. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

In 2017/18, the Council's share of the pension scheme assets was £2.3m understated primarily as a result of the timing of the actuary's work. The Council is planning to obtain a second valuation as at 31 March 2019.

What judgements are we focused on?

We focused on the following:

- ▶ The reasonableness of the underlying assumptions used by Hymans Robertson
- ▶ Ensuring the information supplied to the actuary in relation to Derby City Council was complete and accurate
- ▶ Ensuring the accounting entries and disclosures made in the financial statements were consistent with the report from Hymans Robertson.

What did we do?

- ▶ Performed appropriate tests to obtain assurance over the information provided to the actuary.
- ▶ Wrote to the Pension Fund auditor to ascertain whether there are material concerns we need to be aware of for our audit.
- ▶ Ensured accounting entries and disclosures are consistent with the actuaries report.
- ▶ Assessed the work of the Pension Fund actuary (Hymans) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by Public Sector Auditor Appointments for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team.
- ▶ Reviewed the Actuary's report in conjunction with a review and testing of the accounting entries and disclosures made within the Authority's financial statements in relation to IAS19.

What are our conclusions?

Our work has not identified any material misstatements of the Authority's liability or related disclosures in this regard.

- ▶ We have assessed and are satisfied with the competency and objectivity of the Authority's actuaries: Hymans Robertson LLP.
- ▶ EY pensions team and PwC (Consulting Actuary to the NAO) have reviewed the work of the actuaries. We challenged the actuarial valuation and found no indication of management bias in this estimate.
- ▶ Our review of accounting entries at period end and those journals made in processing estimate did not reveal any instances of management intention to misreport the financial position.

See next page for adjustment made to the pension liability



Areas of Audit Focus

Other areas of audit focus



Pension liability valuation

There has been an ongoing national issue requiring late amendments to the pension fund accounts and IAS 26 fund liability disclosure, relating to legal rulings regarding age discrimination arising from public sector pension scheme transitional arrangements - commonly described as the McCloud ruling.

Since the year-end there had been increasing indications that the liability may need to be incorporated into the assessment of the scheme liabilities as at 31 March 2019 depending on the materiality of the issue. The Authority's initial disclosure for the pension scheme liability was based on the actuarial report dated 13 May 2019. An additional report was requested dated 4 July 2019. In the latter report the actuary reported that the liability had increased by £5.05m (past service costs £4.170m and £0.880m for the GMP equalisation). The Authority has agreed to make the required adjustments to the financial statements in respect of this matter.

We have included the adjusted mis-statement of a £5.05m increase in scheme liabilities in our summary of adjusted misstatements at Section 4.

The adjusted misstatement mis-statement does not impact cash nor the outturn for the year.



Areas of Audit Focus

Other areas of audit focus

IFRS 9 - financial instruments

What is the risk?

This new accounting standard is applicable for local authority accounts from the 2018/19 financial year and will change:

- How financial assets are classified and measured;
- How the impairment of financial assets are calculated; and
- The disclosure requirements for financial assets.

There are transitional arrangements within the standard; and the 2018/19 Cipfa Code of practice on local authority accounting provides guidance on the application of IFRS 9. However, until the Guidance Notes are issued and any statutory overrides are confirmed there remains some uncertainty on the accounting treatment.

What did we do?

- Assessed the authority's implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19;
- Considered the classification and valuation of financial instrument assets;
- Reviewed expected credit loss model impairment calculations for assets; and
- Checked additional disclosure requirements.

What are our conclusions?

- The disclosure within the accounts for financial instruments were updated in line with the disclosure requirements for IFRS 9.



Areas of Audit Focus

Other areas of audit focus

PFI Financing

What are our conclusions?

- ▶ We have confirmed that there have been no significant new PFI contracts or contract variations in the year.
- ▶ There were no material misstatements identified as a result of our procedures.

What is the risk?

The Council has a number of assets held under PFI arrangements. Four of these are recorded on the Council's balance sheet, one is not. Such arrangements are complex and substantial in value.

What did we do?

Our approach has focussed on:

- ▶ Obtaining and documenting an understanding of the schemes
- ▶ Considering whether the scheme falls within IFRIC 12 and should be accounted for on balance sheet
- ▶ Ensuring the outputs from the accounting model are correctly reflected in the financial statements, and relevant disclosures have been made.

Follow up of statutory written recommendations issued June 2017

What are our conclusions?

- ▶ We have confirmed that the Authority have satisfactory implemented the s24 recommendations.

What is the risk?

EY issued written recommendations to the Authority under s24 of the Local Audit and Accountability Act in June 2017.

The report presented to the audit committee in February 2019 by internal audit 18 months after we presented our statutory recommendations to the Authority shows majority of the recommendations have been addressed.

What did we do?

Our approach has focussed on:

- ▶ following up progress during our interim and final audit visits to assess whether the recommendations have been satisfactory concluded.



Areas of Audit Focus

Other areas of audit focus

IFRS 15 - Revenue contracts with customers

What is the risk?

This new accounting standard is applicable for local authority accounts from the 2018/19 financial year.

The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations.

The 2018/19 Cipfa Code of practice on local authority accounting provides guidance on the application of IFRS 15 and includes a useful flow diagram and commentary on the main sources of LG revenue and how they should be recognised. The impact on local authority accounting is likely to be limited as large revenue streams like council tax, non-domestic rates and government grants will be outside the scope of IFRS 15. If the Authority has not assessed if standard is relevant, there may be a risk of material misstatement if recognition of revenue is incorrect and new disclosure requirements are not included in the financial statements.

What did we do?

- Assessed the authority's implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19. This will include where relevant, any Local Authority Trading Companies consolidated into the Authority's Group Accounts
- Considered application to the Authority's revenue streams, and where the standard is relevant test to ensure revenue is recognised when (or as) it satisfies a performance obligation; and
- Checked additional disclosure requirements are correctly included.

What are our conclusions?

We are waiting on the assessment carried out by the Authority before we can conclude our work.



Areas of Audit Focus



Other matters

In 2018/19 Ministry for Housing, Local Government and Communities took the decision to defer the implementation of IFRS 16 (Accounting for leases) in 2019/20 to 2020/21. As a result we did not undertake a detailed review of the preparedness but recommended that the Authority continued to plan to implement the new standard commenced during 2019. We will discuss the Authority's progress to implement IFRS 16 as part of our audit planning for 2019/20.

In addition, changes have been made to the CIPFA/LAASAC Code for 2019/20, as noted below. These matters should be included where we have identified a potentially material impact arising in 2019/20;

- ▶ The revised IASB Conceptual Framework for Financial Reporting (Conceptual Framework), the main elements being (19/20 Code Cpt 2.1 refers):
 - new definitions of assets, liabilities, income and expenses
 - updates for the inclusion of the recognition process and criteria and new provisions on de-recognition
 - enhanced guidance on measurement bases
- ▶ Guidance in the treatment of the Apprenticeship Levy (19/20 Code Cpt 2.11 refers)
- ▶ Updated guidance on IFRS 9 Financial Instruments: Prepayment Features with Negative Compensation and LOBOs (19/20 Code Cpt 2.11 refers)
- ▶ Clarifications for the disclosure requirements with respect to interests in entities within the scope of IFRS 5 Non-current Assets Held for Sale and Discontinued Operations (19/20 Code Cpt 9 refers)



03 Audit Report



Audit Report

Draft audit report

Our opinion on the financial statements

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DERBY CITY COUNCIL

Opinion

We have audited the financial statements of Derby City Council for the year ended 31 March 2019 under the Local Audit and Accountability Act 2014. The financial statements comprise the:

- ▶ Movement in Reserves Statement,
- ▶ Comprehensive Income and Expenditure Statement,
- ▶ Balance Sheet,
- ▶ Cash Flow Statement
- ▶ Related notes 1 to 48,
- ▶ Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement and the related notes 1 to 9,
- ▶ Collection Fund and the related notes 1 and 2.

The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

In our opinion the financial statements:

- ▶ give a true and fair view of the financial position of Derby City Council as at 31 March 2019 and of its expenditure and income for the year then ended; and
- ▶ have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the authority in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard and the Comptroller and Auditor General's (C&AG) AGN01, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- ▶ the Interim Strategic Director of Corporate Resource's use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- ▶ the Interim Strategic Director of Corporate Resource has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Authority's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The other information comprises the information included in the Statement of Accounts, set out on pages 1 to 16, other than the financial statements and our auditor's report thereon. The Treasurer is responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.



Audit Report

Our opinion on the financial statements

Opinion on other matters prescribed by the Local Audit and Accountability Act 2014

Arrangements to secure economy, efficiency and effectiveness in the use of resources

Basis for Qualified Conclusion

Management of A52 Junction improvement scheme

The original estimated total scheme cost within the Authority's capital programme was £14.906m. In March 2018, Cabinet approved £2.157m, within the Highways and Transport programme, to fund the delivery of ancillary works to the main A52 junction improvement scheme - taking the total planned spend to £17.063m.

In late March 2018 it became apparent that there were significant previously undisclosed overspends on the project. Internal audit were commissioned to carry out an investigation into the project, and highlighted significant issues with the processes around project management, monitoring, procurement and decision making by key senior members at the Council. The scheme design was revisited and the project costs are now estimated to be £43.2m, an additional £28.3m over its original budget. This provides evidence of weaknesses in proper arrangements for informed decision making, sustainable resource deployment and Working with partners and other third parties.

Qualified conclusion [Except for]

In our opinion, based on the work undertaken in the course of the audit, having regard to the guidance issued by the Comptroller and Auditor General (C&AG) in November 2017, with the exception of the matter reported in the basis for qualified conclusion paragraph above, we are satisfied that, in all significant respects, Derby City Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

Matters on which we report by exception

We report to you if:

in our opinion the annual governance statement is misleading or inconsistent with other information forthcoming from the audit or our knowledge of the Council;
we issue a report in the public interest under section 24 of the Local Audit and Accountability Act 2014;
we make written recommendations to the audited body under Section 24 of the Local Audit and Accountability Act 2014;
we make an application to the court for a declaration that an item of account is contrary to law under Section 28 of the Local Audit and Accountability Act 2014;
we issue an advisory notice under Section 29 of the Local Audit and Accountability Act 2014; or
we make an application for judicial review under Section 31 of the Local Audit and Accountability Act 2014.

We have nothing to report in these respects

Responsibility of the Interim Strategic Director of Corporate Resource

As explained more fully in the Statement of the Interim Strategic Director of Corporate Resource's Responsibilities set out on page 17, the Interim Strategic Director of Corporate Resource is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19, and for being satisfied that they give a true and fair view.

In preparing the financial statements, the Interim Strategic Director of Corporate Resource is responsible for assessing the Authority's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Authority either intends to cease operations, or have no realistic alternative but to do so.

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.



Audit Report

Our opinion on the financial statements

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/auditorsresponsibilities>. This description forms part of our auditor's report.

Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

We have undertaken our review in accordance with the Code of Audit Practice, having regard to the guidance on the specified criterion issued by the Comptroller and Auditor General (C&AG) in November 2017, as to whether the Derby City Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. The Comptroller and Auditor General determined this criterion as that necessary for us to consider under the Code of Audit Practice in satisfying ourselves whether the Derby City Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

We planned our work in accordance with the Code of Audit Practice. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether, in all significant respects, the Derby City Council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We are required under Section 20(1)(c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the National Audit Office (NAO) requires us to report to you our conclusion relating to proper arrangements.

We report if significant matters have come to our attention which prevent us from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We are not required to consider, nor have we considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Delay in certification of completion of the audit

We cannot formally conclude the audit and issue an audit certificate until we have completed the work necessary to issue our assurance statement in respect of the Authority's Whole of Government Accounts consolidation pack. We are satisfied that this work does not have a material effect on the financial statements or on our value for money conclusion.

Use of our report

This report is made solely to the members of Derby City Council, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014 and for no other purpose, as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

Stephen Clark (Key Audit Partner)
Ernst & Young LLP (Local Auditor)
Birmingham
31 July 2019

The maintenance and integrity of the Derby City Council web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

A woman with long brown hair, wearing a dark sleeveless top, is pointing her right index finger at a large digital display wall. The wall is filled with various financial data visualizations, including line charts with green and red lines, and data tables. The background is dimly lit, emphasizing the bright screens.

04 Audit Differences



Audit Differences

In the normal course of any audit, we identify misstatements between amounts we believe should be recorded in the financial statements and the disclosures and amounts actually recorded. These differences are classified as “known” or “judgemental”. Known differences represent items that can be accurately quantified and relate to a definite set of facts or circumstances. Judgemental differences generally involve estimation and relate to facts or circumstances that are uncertain or open to interpretation.

Summary of adjusted differences

We highlight the following misstatements greater than £0.33m which have been corrected by management that were identified during the course of our audit;

- ▶ The pension liabilities were increased by £5.05m, due to the McCloud judgement and GMP equalisation.
- ▶ The Authority had accrued for £1.630m of Capital Grant Income which has been corrected by removing this amount from capital grant income and debtors.
- ▶ The Authority increased the income and expenditure internal recharges disclosed at Note 8 - expenditure and Income analysed by nature, by £5m, from £12m to £17m, there is no impact to the net income and expenditure disclosed on the comprehensive income and expenditure statement.
- ▶ £1.7m, re-classification of property to council dwellings, where the Authority incorrectly debited to the income and expenditure rather than to revaluation reserve.
- ▶ The authority had mis-calculated the Capital grants received in advance transferred to income and expenditure which caused the following errors in the cash flow disclosure:
 - ▶ Adjustments to net surplus or deficit on the provision of services for non-cash movements was understated by 10.977m.
 - ▶ Adjustments for items included in the net surplus or deficit on the provision of services that are investing and financing activities was understated by 10.977m.
 - ▶ Other non-cash items charged to the net Surplus or Deficit on the Provision of Services was understated by 10.977m
 - ▶ Capital grants credited to surplus or deficit on provision of services was understated by 10.977m.

We will also update Audit and Accounts Committee if there are any further issues arising from our incomplete audit procedures .

Disclosure amendments

In addition we identified a number of disclosure differences during the course of our audit procedures which were corrected by management in the final statement of accounts, as follows:

- ▶ A disclosure error was identified where the client had used the PFI schools carrying value figure of £6.4m in the narrative under the table, instead of the Voluntary Aided Schools figure of £4.8m.
- ▶ In the exit packages note, the number of “other departures” within the 20-60k banding is to be amended from 4 to 2 in line with audit procedures performed.
- ▶ An adjustment has been made to the fees, charges and income and other service expenses in Note 8 as both figures were both over-stated by 1.47m in the draft statement of accounts.

The are other minor disclosure amendments we noted were not corrected in the latest version of the statement of accounts



Audit Differences

Summary of unadjusted differences

In addition we highlight the following misstatements to the financial statements and/or disclosures which were not corrected by management. We request that these uncorrected misstatements be corrected or a rationale as to why they are not corrected be considered and approved by the Audit and Accounts Committee and provided within the Letter of Representation:

Uncorrected misstatements 31 March 2019	:	Balance Sheet (Decrease)/Increase				
		Comprehensive income and expenditure statement Debit/(Credit)	Assets current Debit/ (Credit)	Assets non current Debit/ (Credit)	Liabilities current Debit/ (Credit)	Liabilities non-current Debit/ (Credit)
Errors						
Known differences:						
<ul style="list-style-type: none"> Credit note not accrued for, received post year-end relating to 18/19. Increasing short term debtors and reducing expenditure by £499k 	£(499k)	£(499k)				
<ul style="list-style-type: none"> Understatement of PPE additions due to early close, £512k invoices relating to additions were received, of which £480k were paid and expensed. A prepayment was then made to defer the costs to 2019/20. The PPE additions relate to 2018/19 therefore the PPE figure increases by £512k, and prepayments reduced by £480k. As £32k of invoices were not paid these should be accrued for, increasing creditors by £32k. 			£512k £(480)	£(32k)		
The prior year audited figures were restated by the Authority, as follows:						
<ul style="list-style-type: none"> HRA statement - restated income, dwelling rents of £401k were miscoded to non dwelling rents 						
<ul style="list-style-type: none"> Note 30 - Earmarked reserves - restatement of the earmarked reserves to include additional analysis. 						
<ul style="list-style-type: none"> Note 25 - debtors - the note was restated to reclassify a previously misclassified long term loan bad debt provision to long term debtors. The restatement increased long term debtors and reduced short term debtors by £568k. 						

The restatements above do not meet the requirements of a prior period adjustments, changes for non material restatements are made in year.

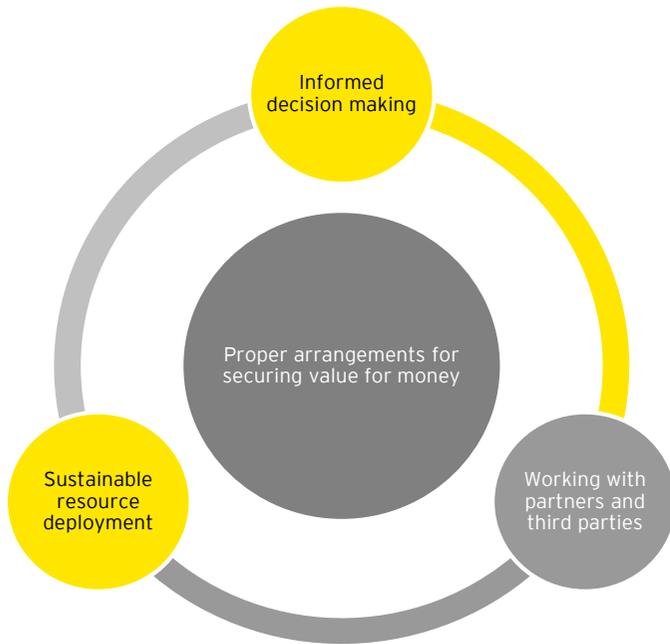


05

Value for Money Risks



Value for Money



Background

We are required to consider whether the Authority has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

For 2018/19 this is based on the overall evaluation criterion:

"In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people"

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.

In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

Overall conclusion

We identified 6 significant risks around these arrangements. The tables below present our findings in response to the risks in our Audit Planning Report and any other significant weaknesses or issues we want to bring to your attention. As a result of our procedures, we conclude that a qualified 'except-for' conclusion with respect to your arrangements to secure economy, efficiency and effectiveness in your use of resources is appropriate in relation to the management of the A52 Junction improvement scheme.



Value for Money Risks

We are only required to determine whether there are any risks that we consider significant within the Code of Audit Practice, where risk is defined as:

“A matter is significant if, in the auditor’s professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public”

Our risk assessment supports the planning of enough work to deliver a safe conclusion on your arrangements to secure value for money, and enables us to determine the nature and extent of any further work needed. If we do not identify a significant risk we do not need to carry out further work.

The table below presents the findings of our work in response to the risks areas in our Audit Planning Report [\[as well as any additional risks identified since then\]](#).

What is the significant value for money risk?	What arrangements did the risk affect?	What are our findings?
<p>Results of regulatory reviews and commentary</p> <p>The Council received various commentary throughout the prior year period from regulatory bodies, the tone of which was mixed. The findings in respect of education provision across the City from Ofsted and more broadly across the Council’s activities from the Local Government Association (LGA) Peer Review indicated a significant risk to our VFM conclusion. As a result of the findings and the recommendations made we will monitor the Council’s progress in these areas.</p>	<p><u>Working with partners and other third parties</u></p> <p>Working with third parties effectively to deliver strategic priorities</p>	<p>We considered the findings from regulatory bodies received during the year, in particularly the follow up to the LGA peer review and Ofsted report on children’s services:</p> <p>The 2017 LGA peer review report was, in the main, not a positive document. Issues were raised around the Council’s lack of planning and project management in many areas; weaknesses in decision making; poor internal control environment; Member/Officer relationships; and poor reputation with respect to the finance function and accounts delivery. The follow up visit, fed back that most of the areas have shown significant improvement, some improvement to Member Officer relations was recommended. We have discussed the Member/Officer relations with the Officers and conclude the relationships have improved to an acceptable level and is no longer a significant risk.</p> <p>Ofsted report - Inspection into children’s services in June 2017, gave a rating of Good, with children who need help and protection impacting the overall rating, as it required improvements. A follow up inspection during 18-22 March 2019 was reported on 8 May 2019, being a joint inspection of the multi-agency response to abuse and neglect in Derby City. The inspection included a ‘deep dive’ focus on the response to child sexual abuse in the family environment. The report shows improvements have been made, however there still remains areas for improvement and a written response by the council is to be made before 15 August 2019. Taking into consideration the draft written response and that children’s services are good overall, we are able to conclude the Authority has appropriate arrangements in place.</p> <p>We conclude there is no risk to our VFM conclusion from the regularity reviews and that it is no longer considered as a significant risk</p>



Value for Money Risks

We are only required to determine whether there are any risks that we consider significant within the Code of Audit Practice, where risk is defined as:

“A matter is significant if, in the auditor’s professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public”

Our risk assessment supports the planning of enough work to deliver a safe conclusion on your arrangements to secure value for money, and enables us to determine the nature and extent of any further work needed. If we do not identify a significant risk we do not need to carry out further work.

The table below presents the findings of our work in response to the risks areas in our Audit Planning Report [\[as well as any additional risks identified since then\]](#).

What is the significant value for money risk?	What arrangements did the risk affect?	What are our findings?
<p><u>Significant overspend on capital projects</u></p> <p>The A52 improvement project is a significant capital project, which is still ongoing. The project has been subject to substantial overspend, which highlighted reporting and control issues. At the time of writing, it is reported there is £40m of committed expenditure against a budget of £15m.</p>	<p><u>Informed Decision Making</u></p> <p>Managing and utilising assets effectively to support the delivery of strategic priorities</p>	<p>The original estimated total scheme cost within the Authority’s capital programme was £14.906m. In March 2018, Cabinet approved £2.157m, within the Highways and Transport programme, to fund the delivery of ancillary works to the main A52 junction improvement scheme - taking the total planned spend to £17.063m.</p> <p>In late March 2018 it became apparent that there were significant previously undisclosed overspends on the project. Internal audit were commissioned to carry out an investigation into the project, and highlighted significant issues with the processes around project management, monitoring, procurement and decision making by key senior Members at the Council. The scheme design was revisited and the project costs are now estimated to be £43.2m, an additional £28.3m over its original budget. This provides evidence of weaknesses in proper arrangements for informed decision making, sustainable resource deployment and working with partners and other third parties</p>



Value for Money Risks

What is the significant value for money risk?

June 2016 Public Interest Report

Grant Thornton issued a Report in the Public Interest in June 2016 which highlighted governance issues which remained present in the 2017/18 year of account. This report, and the Council's response to it therefore presents a significant risk to our VFM conclusion. Our work in 2017/18 confirmed the only remaining matter documented in the PIR which has an ongoing implication for DCC is the quality of member/officer relations. This matter was raised again in the Local Government Association report of July 2017.

July 2017 written recommendations under s24 of Local Audit and Accountability Act

In June 2017 EY exercised its powers under the Local Audit and Accountability Act 2014 and issued written recommendations to the Council. Although some progress had been made, it was our view that given the significance of the control weaknesses, insufficient progress has been made in the period following our report of 23 September 2016 to appropriately address the issues and strengthen the Council's control environment. The control issues identified across a significant number of areas of the Finance and associated supporting functions, most noticeably in respect of the Estates function, are pervasive and led to a significant number of errors identified in the 15/16 published draft Financial Statements relating to both the current and prior year accounting periods. This could undermine the Council's ability to effectively demonstrate it has proper arrangements to safeguard and make informed decisions in respect of public funds and assets.

The work of the internal audit work in respect to the follow-up of s24 recommendations was reported to the audit committee in February 2019, which shows the Council has clearly made progress against addressing many of the control issues communicated in our written recommendations, there are still recommendations to be concluded on, 18 months from when we presented our recommendations the council.

What arrangements did the risk affect?

Informed Decision Making

Acting in the public interest, through demonstrating and applying the principles and values of sound governance

Informed Decision Making

Managing risks effectively and maintaining a sound system of internal control'
And

Sustainable Resource Deployment

Managing and utilising assets effectively to support the delivery of strategic Priorities

What are our findings?

The only remaining matter documented in the PIR which has an ongoing implication for the Authority is the quality of Member/Officer relations. This matter was raised again in the LGA report of July 2017.
We have discussed the Member Officer relations with the officers and conclude the relationships have improved to an acceptable level and is no longer a significant risk.

The 2017-18 audit evidenced improvements and supported the findings of the internal audit report detailing follow up work carried out on EY S24 recommendations. The 2018-19 audit work confirms the controls are embedded.

We conclude the S24 recommendation have been implemented



Value for Money Risks

What is the significant value for money risk?	What arrangements did the risk affect?	What are our findings?
<p>Robustness of medium term financial planning The Council’s Medium Term Financial Plan and planning process have not previously been sufficiently robust. Savings targets were not accompanied by detailed plans on how the savings are to be achieved. There is no provision for scenario planning to identify financial sensitivities within the Medium Term Financial Plan. We have been informed of changes implemented in this area, but there is a risk present as we must ascertain whether the changes have been embedded within the Council. This therefore presents a significant risk to our Value For Money conclusion</p>	<p><u>Sustainable Resource Deployment</u> Planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions</p>	<p>We note that the MTFP and the process of identifying achievable savings and quantifiable pressures is sufficiently robust. Adequate plans and reporting is in place to deliver and monitor the identified savings.</p> <p>We conclude that the robustness of the MTFP has no impact on our VFM conclusion.</p>
<p><u>Provision of internal audit services</u> In the prior year, our view was that the reporting to the Committee by internal audit is superficial, and the challenge provided by the audit committee to the matters raised by internal audit was often weak. In early 2017 the Council initiated a review of the internal audit service offering, a transformation programme was initiated and improvements were made. We will continue to monitor progress in 2018-19</p>	<p><u>Working with partners and other third parties</u> Working with third parties effectively to deliver strategic priorities</p>	<p>Improvements have been made by the internal audit service.</p> <p>No significant weaknesses have been highlighted in internal audit reporting, there is improved communication with council Officers and audit and accounts committee.</p> <p>The council are now able to rely on internal audit and respect the services provided.</p>



06 Other reporting issues

Other reporting issues

Consistency of other information published with the financial statements, including the Annual Governance Statement

We must give an opinion on the consistency of the financial and non-financial information in the Statement of Accounts 2018/19 with the audited financial statements

We must also review the Annual Governance Statement for completeness of disclosures, consistency with other information from our work, and whether it complies with relevant guidance.

Financial information in the Statement of Accounts 2018/19 and published with the financial statements was consistent with the audited financial statements.

We have reviewed the information presented in the Annual Governance Statement for consistency with our knowledge of the Authority. Management has agreed to update the statement to clarify the current position on the A52 project and actions being taken.

Whole of Government Accounts

Alongside our work on the financial statements, we also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of our review, and the nature of our report, is specified by the National Audit Office.

We are yet to conclude our work in this area.

Other reporting issues

Other reporting issues

Other powers and duties

We have a duty under the Local Audit and Accountability Act 2014 to consider whether to report on any matter that comes to our attention in the course of the audit, either for the Authority to consider it or to bring it to the attention of the public (i.e. “a report in the public interest”). We did not identify any issues which required us to issue a report in the public interest.

We also have a duty to make written recommendations to the Authority, copied to the Secretary of State, and take action in accordance with our responsibilities under the Local Audit and Accountability Act 2014. We did not identify any issues.

Other matters

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we must tell you significant findings from the audit and other matters if they are significant to your oversight of the Authority’s financial reporting process.

Quality of the financial statement preparation process

We identified several audit differences during the course of our audit which are fully detailed in section 4. In our review some of the errors are a reflection of the financial statements preparation process that the Authority has in place together with the fact that 2018/19 is the second year of the faster close. These issues could be mitigated in the future by making improvements to the quality review arrangements before the financial statements are presented for audit.

We thank officers for their hard work in the preparation and supply of working papers requested in advance of and during our year-end audit visit.



07

Assessment of Control Environment



Assessment of Control Environment

Financial controls

It is the responsibility of the Authority to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Authority has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

As part of our audit of the financial statements, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. As we have adopted a fully substantive approach, we have therefore not tested the operation of controls. Although our audit was not designed to express an opinion on the effectiveness of internal control we are required to communicate to you significant deficiencies in internal control.

As a result of the work undertaken we have identified some deficiencies in internal control as follows:

- No reconciliation between HRA system and the General Ledger for the housing rents income at year-end which could result in the GL not agreeing to the HRA subledger
- The annual governance statement has not been made available alongside the draft accounts for the inspection period.



08 Data Analytics



Use of Data Analytics in the Audit

Analytics Driven Audit

Data analytics

We used our data analysers to enable us to capture entire populations of your financial data. These analysers:

- ▶ Help identify specific exceptions and anomalies which can then be the focus of our substantive audit tests; and
- ▶ Give greater likelihood of identifying errors than traditional, random sampling techniques.

In 2018/19, our use of these analysers in the authority's audit included testing journal entries to identify and focus our testing on those entries we deem to have the highest inherent risk to the audit.

We capture the data through our formal data requests and the data transfer takes place on a secured EY website. These are in line with our EY data protection policies which are designed to protect the confidentiality, integrity and availability of business and personal information.

Journal Entry Analysis

We obtain downloads of all financial ledger transactions posted in the year. We perform completeness analysis over the data, reconciling the sum of transactions to the movement in the trial balances and financial statements to ensure we have captured all data. Our analysers then review and sort transactions, allowing us to more effectively identify and test journals that we consider to be higher risk, as identified in our audit planning report.

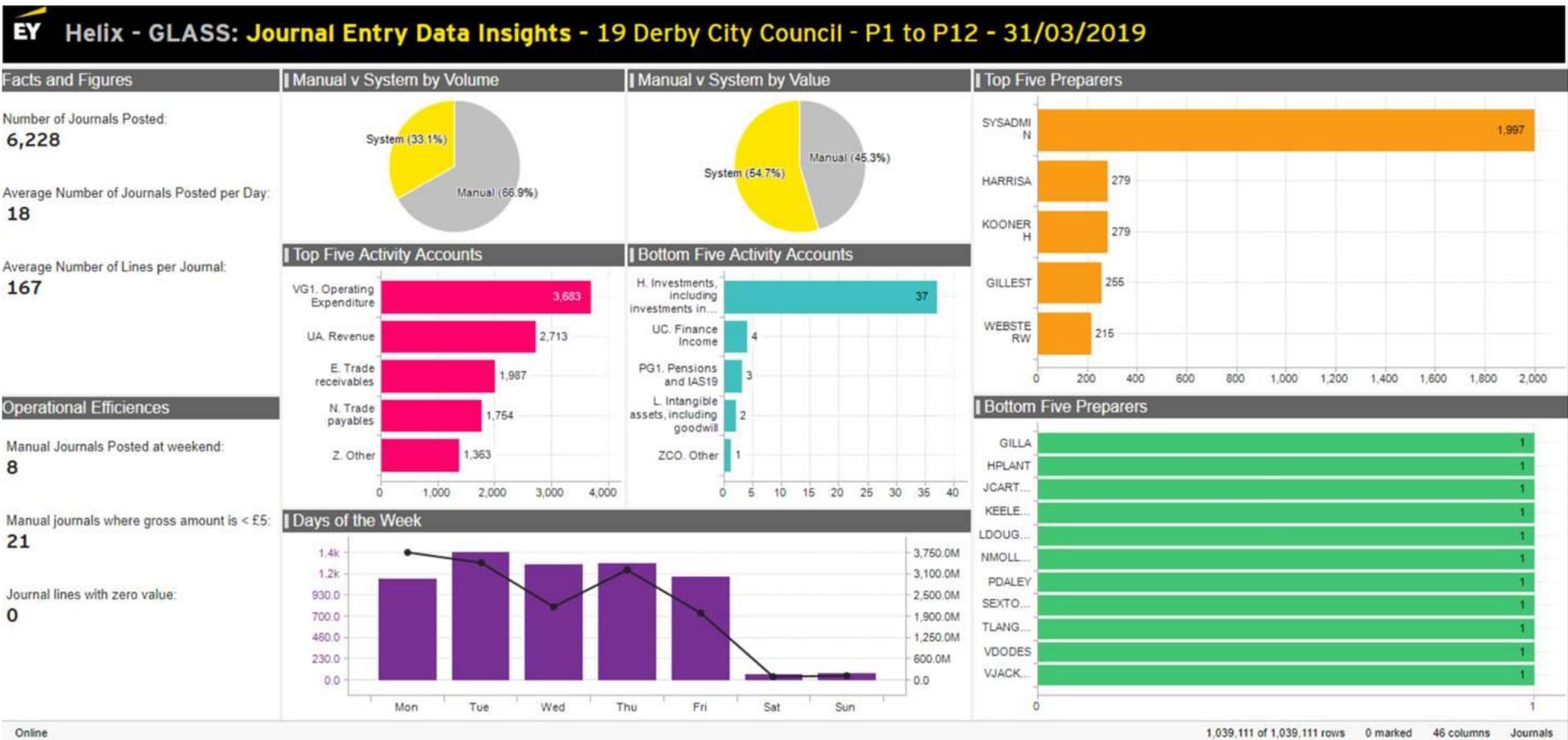


Data Analytics

Journal Entry Data Insights

The graphic outlined below summarises the journal population for 2018/19. We review journals by certain risk based criteria to focus on higher risk transactions, such as journals posted manually by management, those posted around the year-end, those with unusual debit and credit relationships, and those posted by individuals we would not expect to be entering transactions.

The purpose of this approach is to provide a more effective, risk focused approach to auditing journal entries, minimising the burden of compliance on management by minimising randomly selected samples.





Journal Entry Testing

What is the risk?

In line with ISA 240 we are required to test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements.

Journal entry data criteria – 31 March 2019

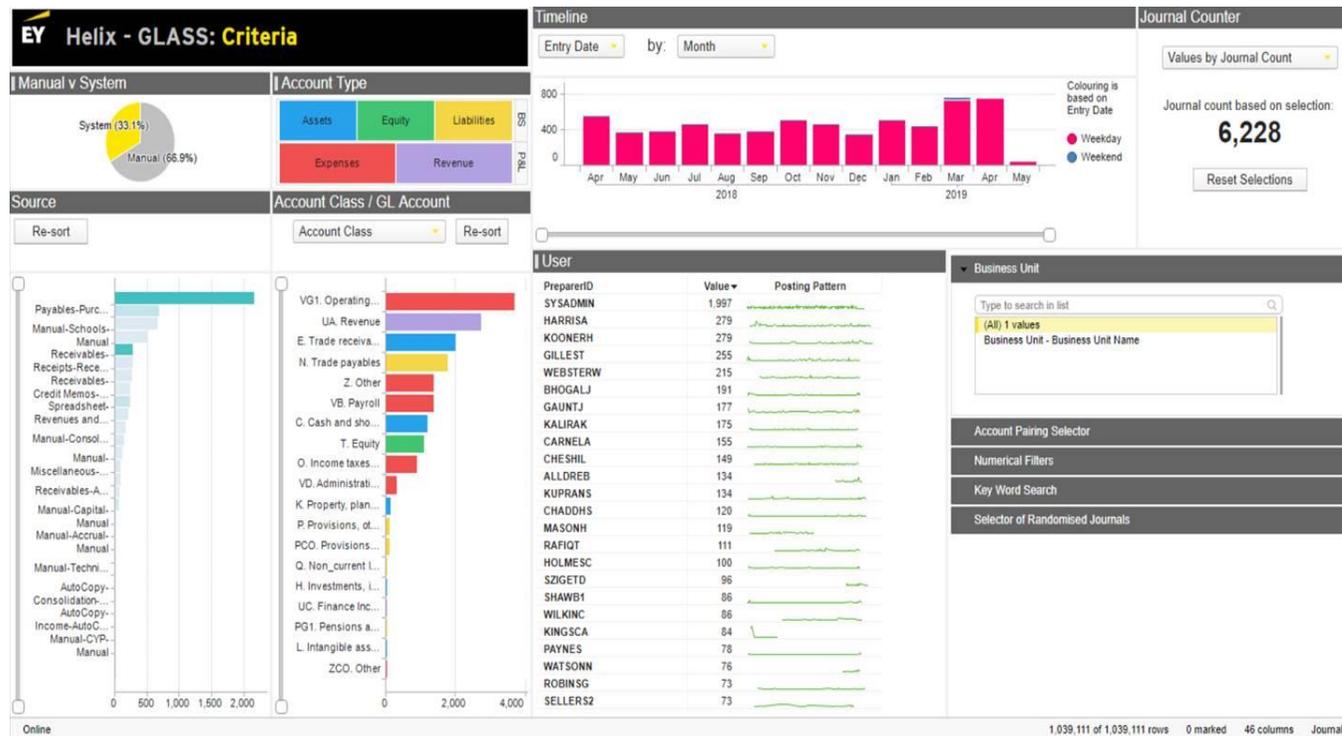
What judgements are we focused on?

Using our analysers we are able to take a risk based approach to identify journals with a higher risk of management override, as outlined in our audit planning report.

What did we do?

We obtained general ledger journal data for the period and have used our analysers to identify characteristics typically associated with inappropriate journal entries or adjustments, and journals entries that are subject to a higher risk of management override.

We then performed tests on the journals identified to determine if they were appropriate and reasonable.



What are our conclusions?

We isolated a sub set of journals for further investigation and obtained supporting evidence to verify the posting of these transactions and concluded that they were appropriately stated.



9

Independence

Confirmation



We confirm that there are no changes in our assessment of independence since our confirmation in our audit planning board report dated February 2019. We complied with the APB Ethical Standards and the requirements of the PSAA's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that you and your Audit and Accounts Committee consider the facts known to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the Audit and Accounts Committee on 30 July 2019.

We confirm we have not undertaken any non-audit work outside the PSAA Code requirements.

Independence

Relationships, services and related threats and safeguards



The FRC Ethical Standard requires that we provide details of all relationships between Ernst & Young (EY) and your Authority, and its directors and senior management and its affiliates, including all services provided by us and our network to your Authority, its directors and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on the our integrity or objectivity, including those that could compromise independence and the related safeguards that are in place and why they address the threats.

There are no relationships from 1 April 2018 to the date of this report, which we consider may reasonably be thought to bear on our independence and objectivity.

Services provided by Ernst & Young

Below includes a summary of the fees that you have paid to us in the year ended 31 March 2019 in line with the disclosures set out in FRC Ethical Standard and in statute.

We confirm that none of the services listed in the audit fee table on the next page has been provided on a contingent fee basis.

Independence

Fee analysis

As part of our reporting on our independence, we set out below a summary of the fees paid for the year ended 31 March 2019.

We confirm that we have not undertaken non-audit work outside the PSAA Code requirements.

	Final Fee 2018/19	Planned Fee 2018/19	Final Fee 2017/18
	£	£	£
Audit Fee - Code work*	151,766	147,766	182,553
Total Audit Fee - Code work	151,766	147,766	182,553
Non-audit services **	0	31,346	31,346
TOTAL	151,766	147,766	182,553

*an additional fee of £42,000 against the scale fee, for out of scope work being carried out during 2018-19, has agreed with management to address value for money risks, implementation of IFRS 9 / 15, use of EY real estates, group accounts and the McCloud issue.

** Planned non-audit work has not been started, our final fees will be reported within our annual certification report.

All fee variations are subject to approval by Public Sector Audit Appointments.

A close-up photograph of a person's hand reaching into a filing cabinet to touch a folder. The cabinet is filled with numerous folders of various colors (yellow, blue, white) and sizes, each containing stacks of papers. The background is a textured, light-colored wall.

10 Appendices

Appendix A

Audit approach update

Our audit procedures are designed to be responsive to our assessed risk of material misstatement at the relevant assertion level. Assertions relevant to the balance sheet include:

- Existence: An asset, liability and equity interest exists at a given date
- Rights and Obligations: An asset, liability and equity interest pertains to the entity at a given date
- Completeness: There are no unrecorded assets, liabilities, and equity interests, transactions or events, or undisclosed items
- Valuation: An asset, liability and equity interest is recorded at an appropriate amount and any resulting valuation or allocation adjustments are appropriately recorded
- Presentation and Disclosure: Assets, liabilities and equity interests are appropriately aggregated or disaggregated, and classified, described and disclosed in accordance with the applicable financial reporting framework. Disclosures are relevant and understandable in the context of the applicable financial reporting Framework
- As outlined in section 1, the valuation of pension liabilities is subject to significant estimation. For the 2018/19 financial statements an additional assessment of the impact of the McCloud judgement on pension liabilities is required and has resulted in adjustments to the balances recorded for pension liabilities. We have also considered the potential impact of the Guaranteed Minimum Pensions (GMP) ruling on the LGPS liabilities.

Our approach to the audit of the balance sheet has not change from the prior year audit.

Appendix B

Summary of communications

Date 	Nature 	Summary 
24 September 2018	Meeting	The Senior Manager met with the head of internal audit to discuss the results of their work in reviewing the actions taken in response to the s24 written recommendations and their work in respect of the A52 capital project overspend.
4 October 2018	Meeting	The partner in charge of the engagement, along with the senior manager, met with the s151 officer and the Head of Finance to discuss the matters identified as part of the first quarter review.
20 December 2018	Meeting	The partner in charge of the engagement, met with the newly appointed chief executive.
25 February 2019	Meeting	The partner in charge of the engagement, along with the senior manager, met with the s151 officer and the Head of Finance to discuss the matters identified.
27 March 2019	Report and meeting	The audit planning report, including confirmation of independence, was issued to the Audit and Accounts Committee.
29 April 2019	Meeting	The partner in charge of the engagement, along with the senior manager, met with the s151 officer and the Head of Finance to discuss the matters identified for 2018/19.
19 June 2019	Meeting	The senior manager, met with the Chair of Audit and Accounts Committee to discuss the audit.
26 July 2019	Meeting	Audit close meeting with the management team to discuss the preliminary findings of the audit.
26 July 2019	Report	The audit results report, including confirmation of independence, was issued to the Audit and Accounts Committee.
	Management letter	The management team and the Audit and Accounts Committee were provided details of internal control observations made in respect of the current year.
30 July 2019	Meeting	The partner in charge of the engagement, accompanied by other senior members of the audit team, will meet with the Audit and Accounts Committee and senior members of the management team to discuss the audit results report.

In addition to the above specific meetings and letters the audit team met with the management team multiple times throughout the audit to discuss audit findings.

Appendix C

Required communications with the Audit Committee

There are certain communications that we must provide to the Audit Committees of UK clients. We have detailed these here together with a reference of when and where they were covered:

		Our Reporting to you
Required communications	 What is reported?	  When and where
Terms of engagement	Confirmation by the Audit and Accounts Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter.	March 2019 - Audit planning report
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	March 2019 - Audit planning report
Significant findings from the audit	<ul style="list-style-type: none"> ▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▶ Significant difficulties, if any, encountered during the audit ▶ Significant matters, if any, arising from the audit that were discussed with management ▶ Written representations that we are seeking ▶ Expected modifications to the audit report ▶ Other matters if any, significant to the oversight of the financial reporting process 	July 2019 - Audit results report
Significant deficiencies in internal controls identified during the audit	<ul style="list-style-type: none"> ▶ Significant deficiencies in internal controls identified during the audit. 	July 2019 - Audit results report

Appendix C

		 Our Reporting to you
Required communications	 What is reported?	  When and where
Public Interest Entities	<p>For the audits of financial statements of public interest entities our written communications to the audit committee include:</p> <ul style="list-style-type: none"> ▶ A declaration of independence ▶ The identity of each key audit partner ▶ The use of non-member firms or external specialists and confirmation of their independence ▶ The nature and frequency of communications ▶ A description of the scope and timing of the audit ▶ Which categories of the balance sheet have been tested substantively or controls based and explanations for significant changes to the prior year, including first year audits ▶ Materiality ▶ Any going concern issues identified ▶ Any significant deficiencies in internal control identified and whether they have been resolved by management ▶ Subject to compliance with regulations, any actual or suspected non-compliance with laws and regulations identified relevant to the audit committee ▶ Subject to compliance with regulations, any suspicions that irregularities, including fraud with regard to the financial statements, may occur or have occurred, and the implications thereof ▶ The valuation methods used and any changes to these including first year audits ▶ The scope of consolidation and exclusion criteria if any and whether in accordance with the reporting framework ▶ The identification of any non-EY component teams used in the group audit ▶ The completeness of documentation and explanations received ▶ Any significant difficulties encountered in the course of the audit ▶ Any significant matters discussed with management ▶ Any other matters considered significant 	<p>March 2019 - Audit planning report July 2019 - Audit results report</p>

Appendix C

		 Our Reporting to you
Required communications	 What is reported?	 When and where
Going concern	<p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> ▶ Whether the events or conditions constitute a material uncertainty ▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▶ The adequacy of related disclosures in the financial statements 	No conditions or events were identified, either individually or together to raise any doubt about Derby City Council's ability to continue for the 12 months from the date of our report
Misstatements	<ul style="list-style-type: none"> ▶ Uncorrected misstatements and their effect on our audit opinion ▶ The effect of uncorrected misstatements related to prior periods ▶ A request that any uncorrected misstatement be corrected ▶ Material misstatements corrected by management 	July 2019 - Audit results report
Subsequent events	<ul style="list-style-type: none"> ▶ Enquiry of the audit committee where appropriate regarding whether any subsequent events have occurred that might affect the financial statements. 	July 2019 - Audit results report
Fraud	<ul style="list-style-type: none"> ▶ Enquiries of the Audit and Accounts Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the Authority ▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist ▶ Unless all of those charged with governance are involved in managing the Authority, any identified or suspected fraud involving: <ol style="list-style-type: none"> a. Management; b. Employees who have significant roles in internal control; or c. Others where the fraud results in a material misstatement in the financial statements. ▶ The nature, timing and extent of audit procedures necessary to complete the audit when fraud involving management is suspected ▶ Any other matters related to fraud, relevant to Audit and Accounts Committee responsibility. 	July 2019 - Audit results report Enquiries were made during the audit, and there are no issues to report to you.

Appendix C

		 Our Reporting to you
Required communications	 What is reported?	 When and where
Related parties	<p>Significant matters arising during the audit in connection with the Authority's related parties including, when applicable:</p> <ul style="list-style-type: none"> ▶ Non-disclosure by management ▶ Inappropriate authorisation and approval of transactions ▶ Disagreement over disclosures ▶ Non-compliance with laws and regulations ▶ Difficulty in identifying the party that ultimately controls the Authority 	<p>July 2019 - Audit results report No issues to report</p>
Independence	<p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence.</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> ▶ The principal threats ▶ Safeguards adopted and their effectiveness ▶ An overall assessment of threats and safeguards ▶ Information about the general policies and process within the firm to maintain objectivity and independence <p>Communications whenever significant judgments are made about threats to objectivity and independence and the appropriateness of safeguards put in place.</p>	<p>March 2019 - Audit planning report July 2019 - Audit results report</p>
External confirmations	<ul style="list-style-type: none"> ▶ Management's refusal for us to request confirmations ▶ Inability to obtain relevant and reliable audit evidence from other procedures. 	<p>July 2019 - Audit results report</p>
Consideration of laws and regulations	<ul style="list-style-type: none"> ▶ Subject to compliance with applicable regulations, matters involving identified or suspected non-compliance with laws and regulations, other than those which are clearly inconsequential and the implications thereof. Instances of suspected non-compliance may also include those that are brought to our attention that are expected to occur imminently or for which there is reason to believe that they may occur ▶ Enquiry of the audit committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the audit committee may be aware of 	<p>July 2019 - Audit results report</p>

Appendix C

		Our Reporting to you
Required communications	 What is reported?	  When and where
Group Audits	<ul style="list-style-type: none"> ▶ An overview of the type of work to be performed on the financial information of the components ▶ An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components ▶ Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work ▶ Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted ▶ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements. 	July 2019 - Audit results report
Written representations we are requesting from management and/or those charged with governance	<ul style="list-style-type: none"> ▶ Written representations we are requesting from management and/or those charged with governance 	July 2019 - Audit results report
Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	<ul style="list-style-type: none"> ▶ Material inconsistencies or misstatements of fact identified in other information which management has refused to revise 	July 2019 - Audit results report
Auditors report	<ul style="list-style-type: none"> ▶ Any circumstances identified that affect the form and content of our auditor's report 	July 2019 - Audit results report
Fee Reporting	<ul style="list-style-type: none"> ▶ Breakdown of fee information when the audit planning report is agreed ▶ Breakdown of fee information at the completion of the audit ▶ Any non-audit work 	March 2019 - Audit planning report July 2019 - Audit results report
Certification work	<ul style="list-style-type: none"> ▶ Summary of certification work 	No certification work carried out.

Draft Management representation letter

Management Rep Letter

To be prepared on the entity's letterhead]
[Date]

Ernst & Young LLP
1 Colmore Square
Birmingham B4 6HQ

This letter of representations is provided in connection with your audit of the financial statements of Derby City Council ("the Council") for the year ended 31 March 2019. We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the financial statements give a true and fair view of the Council financial position of Derby City Council as of 31 March 2018 and of its income and expenditure for the year then ended in accordance with CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

We understand that the purpose of your audit of our financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing (UK and Ireland), which involves an examination of the accounting system, internal control and related data to the extent you considered necessary in the circumstances, and is not designed to identify - nor necessarily be expected to disclose - all fraud, shortages, errors and other irregularities, should any exist.

Accordingly, we make the following representations, which are true to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

A. Financial Statements and Financial Records

1. We have fulfilled our responsibilities, under the relevant statutory authorities, for the preparation of the financial statements in accordance with the Accounts and Audit Regulations 2015 and CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.
2. We acknowledge, as members of management of the Council, our responsibility for the fair presentation of the financial statements. We believe the financial statements referred to above give a true and fair view of the financial position, financial performance (or results of operations) and cash flows of the Council in accordance with [the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19. We have approved the financial statements.
3. The significant accounting policies adopted in the preparation of the financial statements are appropriately described in the financial statements.
4. As members of management of the Council, we believe that the Council has a system of internal controls adequate to enable the preparation of accurate financial statements in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19, that are free from material misstatement, whether due to fraud or error.
5. We believe that the effects of any unadjusted audit differences, summarised in the accompanying schedule, accumulated by you during the current audit and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. We have not corrected these differences identified by and brought to our attention by the auditor because we do not believe that they are material.

Management representation letter

Management Rep Letter

B. Non-compliance with law and regulations, including fraud

1. We acknowledge that we are responsible to determine that the Council's activities are conducted in accordance with laws and regulations and that we are responsible to identify and address any non-compliance with applicable laws and regulations, including fraud.
2. We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.
3. We have disclosed to you the results of our assessment of the risk that the consolidated and Council financial statements may be materially misstated as a result of fraud.
4. We have no knowledge of any identified or suspected non-compliance with laws or regulations, including fraud that may have affected the Council (regardless of the source or form and including without limitation, any allegations by "whistleblowers"), including non-compliance matters:
 - involving financial statements;
 - related to laws and regulations that have a direct effect on the determination of material amounts and disclosures in the consolidated or Council's financial statements;
 - related to laws and regulations that have an indirect effect on amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operations of the Council's activities, its ability to continue to operate, or to avoid material penalties;
 - involving management, or employees who have significant roles in internal controls, or others; or
 - in relation to any allegations of fraud, suspected fraud or other non-compliance with laws and regulations communicated by employees, former employees, analysts, regulators or others.

C. Information Provided and Completeness of Information and Transactions

1. We have provided you with:
 - Access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - Additional information that you have requested from us for the purpose of the audit; and
 - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
2. All material transactions have been recorded in the accounting records and are reflected in the consolidated and council financial statements.
3. We have made available to you all minutes of the meetings of the County Council, Cabinet and Audit and Accounts Committee (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through the year to the most recent meeting on the following date: 30 July 2019.
4. We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the Council's related parties and all related party relationships and transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the year ended, as well as related balances due to or from such parties at the year end. These transactions have been appropriately accounted for and disclosed in the financial statements.
5. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.

Management representation letter

Management Rep Letter

6. We have disclosed to you, and the Council has complied with, all aspects of contractual agreements that could have a material effect on the consolidated and council financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.

D. Liabilities and Contingencies

1. All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the consolidated and council financial statements.
2. We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.
3. We have recorded and/or disclosed, as appropriate, all liabilities related litigation and claims, both actual and contingent, and have disclosed to you all guarantees that we have given to third parties.
4. No claims in connection with litigation have been or are expected to be received.

E. Subsequent Events

1. There have been no events subsequent to year end which require adjustment of or disclosure in the consolidated and council financial statements or notes thereto.

F. Other information

1. We acknowledge our responsibility for the preparation of the other information. The other information comprises the Annual Governance Statement and Narrative Statement.
2. We confirm that the content contained within the other information is consistent with the financial statements.

G. Comparative information - prior period adjustment

We represent, to the best of our knowledge and belief, the following:

1. The financial statements have been adjusted to reflect a change in the valuation of our long term investment in Entrust and to remove accumulated depreciation on assets revalued and disposed of in prior years.
2. The amounts involved are set out in Note 47 to the financial statements.
3. The comparative amounts have been correctly restated to reflect the above matter(s) and appropriate note disclosure of this (these) restatement(s) has (have) also been included in the current year's financial statements.

H. Retirement benefits

1. On the basis of the process established by us and having made appropriate enquiries, we are satisfied that the actuarial assumptions underlying the scheme liabilities are consistent with our knowledge of the business. All significant retirement benefits and all settlements and curtailments have been identified and properly accounted for

I. Use of the Work of a Specialist

1. We agree with the findings of the specialists that we engaged to evaluate the valuation of non-current assets and have adequately considered the qualifications of the specialists in determining the amounts and disclosures included in the consolidated and council financial statements and the underlying accounting records. We did not give or cause any instructions to be given to the specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an effect on the independence or objectivity of the specialists.

Management representation letter

Management Rep Letter

J. Accounting Estimates

Valuation of Pension Asset/Liabilities and Property, Plant and Equipment

1. We believe that the measurement processes, including related assumptions and models, used to determine the above accounting estimates have been consistently applied and are appropriate in the context of CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.
2. We confirm that the significant assumptions used in making the estimated valuations of Pension Asset/Liabilities and Property, Plant and Equipment appropriately reflect our intent and ability to carry out specific courses of action on behalf of the Council.
3. We confirm that the disclosures made in the council financial statements with respect to the accounting estimates are complete and made in accordance with CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.
4. We confirm that no adjustments are required to the accounting estimates and disclosures in the council financial statements due to subsequent events.

Yours faithfully,

Don McLure
s151 Officer

Cllr Willoughby
Chair of the Audit and Accounts Committee

EY | Assurance | Tax | Transactions | Advisory

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

© 2017 EYGM Limited.
All Rights Reserved.

ED None

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.

ey.com