

Northumberland County
Council
Audit results report

Year ended 31 March 2017

Private and Confidential

23 November 2017

Dear Audit Committee members

We have completed our audit of Northumberland County Council (the Council) for the year ended 31 March 2017.

Following the Audit Committee meeting on 27 September 2017, we have received all of the information that we require to complete our audit. We have reviewed this information and considered the implications for our audit. We propose to issue a modified value for money conclusion; further details on the proposed modification are included within this report.

This report is intended solely for the use of the Audit Committee, other members of the Council, 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 look forward to discussing with you any aspects of this report or any other issues arising from our work.

Yours faithfully

Stephen Reid
Partner

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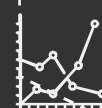
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In April 2015, Public Sector Audit Appointments Ltd ("PSAA") issued the "Statement of responsibilities of auditors and audited bodies". It is available via the PSAA website (www.PSAA.co.uk).

The 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 February 2017)" issued by the 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 in legislation, and covers matters of practice and procedure which are of a recurring nature.

This report is made solely to the Audit Committee, other members of the Council and the management of Northumberland County Council in accordance with the Statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee, other members of the Council and the management of Northumberland County Council those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit Committee, other members of the Authority and the management of Northumberland County Council for this report or for the opinions we have formed. It should not be provided to any third-party without obtaining our written consent.



01

Executive Summary



Executive summary

Overview of the audit

Scope and materiality

In our audit plan, presented to the Audit Committee on 29 March 2017, we provided an overview of how we intended to carry out our responsibilities as your auditor. We carried out our audit in accordance with that plan.

We planned our procedures using a materiality of £16,968,820 for the Council and £17,291,260 for the Group, based on the prior year's gross expenditure. We reassessed this using your actual year-end gross expenditure, which increased our materiality to £17,665,780 for the Council and £18,072,640 for the Group. The threshold for reporting audit differences also increased from £848,441 to £883,289.

Status of the audit

We have completed our audit of the Council's financial statements for the year ended 31 March 2017 and have performed the procedures outlined in our audit plan. We will issue an unqualified opinion on the Council's financial statements and a modified value for money conclusion in the form which appears in section 3.

We expect to issue our audit certificate at the same time as the audit opinion.



Executive Summary

Executive summary (continued)

Audit differences

There is one unadjusted audit difference in relation to the valuation of land and buildings at Ashington Football Club which is owned by the Arch Group, and held within investment property in the Council's group financial statements. The land and buildings have been valued using a depreciated replacement cost basis by the Arch Group; however consultation with our EY estates team has suggested that a market valuation would be a more appropriate basis which could lead to a reduction in valuation of approximately £1.5 million. Further detail is included in sections 2 and 4 of this report.

There have been some amendments to the financial statements; we have listed the adjusted audit differences in section 4 of this report. In summary, they relate to:

- Correction of collection fund debtor and creditor balances identified by management as part of their quality review process on the unaudited draft financial statements; and
- Reversal of a revenue to capital contribution of £15.7 million, following a request from the leader of the Council following the publication of the unaudited draft financial statements.

Areas of audit focus

Our Audit Plan identified key areas of focus for our audit of the Council's financial statements. This report sets out our observations and conclusions, including our views on areas which might be prudent, and where there is potential risk and exposure. We summarise our consideration of these matters, and any others identified, in the "Key Audit Issues" 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; and
- 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 Committee.



Executive Summary

Executive summary (continued)

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 Plan we identified a significant risk in respect of financial planning, with a particular focus on the phasing of required savings. Following completion of our work in this area, we were satisfied that there was no impact on our value for money conclusion and we have summarised the findings arising from our work in section 5 of this report.

Following presentation of our Audit Plan we were made aware of allegations of impropriety at the Arch Group; a group of wholly owned subsidiary companies. The Council's internal auditors were commissioned to undertake a review of arrangements. We requested a copy of the draft report in relation to the review, together with details of the emergent findings in early August. In October 2017 management provided access to the information and met with us to discuss the findings. We have concluded that, as the review identified that the principles and values of sound governance were not always in place for some decisions taken during 2016/17, a modification to our value for money opinion was required.

In August 2017 the Council commissioned an independent review of financial arrangements to ensure that decision making going forward would be based on complete and transparent financial information and that the baseline position was accurate. The review focused on the accuracy and completeness of the base budget, together with the veracity of the underpinning processes and systems and the Council's longer term financial plans. The overall conclusion from the review was that, whilst areas for improvement to the process of preparing the budget were identified, there were no indications of significant errors or omissions and that there was an adequate base to take forward future financial plans. We are satisfied that there were no findings from this review that are material to our value for money conclusion.

Other reporting matters

We have reviewed the information presented in the Annual Governance Statement for consistency with our knowledge of the Council. We have no matters to report as a result of this work. We revisited the statement, following the decision to issue a modified value for money conclusion and noted that reviewing the Council's governance arrangements in relation to the activities of the Arch Group was already identified as an area for improvement and therefore we are satisfied that no amendment to the statement is required.

Control observations

Based on the audit work completed during 2016/17, we have not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in your financial statements and which is unknown to you.

Independence

We provide an update to confirm our independence in Appendix B.



02

Areas of Audit Focus

Audit issues and approach:

Revenue and Expenditure Recognition

What are our conclusions?


Our testing has not identified any material misstatements with respect to revenue and expenditure recognition.

Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the Council's financial position.

What is the risk?

Risk of fraud in revenue and expenditure recognition

Under International Standard on Auditing (UK & Ireland) 240, there is a presumed risk that revenue may be misstated due to improper 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 manipulating expenditure recognition.

 Significant Risk

What did we do?

We completed the following work in this area:

- We reviewed and tested revenue and expenditure recognition policies;
- We reviewed and substantively tested year-end income debtors and accrued income by agreeing to post year-end cash receipts;
- We reviewed and substantively tested year-end expenditure accruals and provisions by corroborating the assumptions used to third party evidence;
- We tested completeness of expenditure by selecting a sample of invoices posted to the ledger and cash payments made from the bank post year-end to confirm that they were recorded in the correct period; and
- We tested the assumptions used in calculating the repairs and maintenance provision, the most significant provision held by the Council.

The repairs and maintenance provision recorded at 31 March 2017 has been based on an independent assessment by the Council's advisers. The lease on this property has ended and the Council is required to undertake some restoration work under the terms of the lease. The Council's adviser has calculated the lease on a worst case scenario rather than a most likely case scenario; management has not undertaken a separate assessment. As the total provision is not material to the financial statements, we concur with management's view that any over-provision will not be material.

No other significant issues have been identified as part of this work.

Audit issues and approach:

Management override

What are our conclusions?

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.

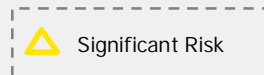
We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business.

What is the risk?

Risk of management override

As identified in ISA (UK and Ireland) 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.

We consider that for the Council the risk of management override of controls manifests itself through manipulation of accounting estimates (i.e. non-routine income and expenditure accruals and provisions).



What did we do?

We have completed the following work in this area:

- We tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements;
- We reviewed accounting estimates for evidence of management bias (as noted above relating to revenue and expenditure recognition); and
- We evaluated the business rationale for any potential significant unusual transactions and concluded that there were none.

No significant issues have been identified as part of this work.

Audit issues and approach:

Valuation of land, buildings and investment properties

We have not identified any material misstatement in our testing of the Council's valuation of land and buildings and investment properties.

What is the risk?

Land and buildings is the most significant balance in the Council's balance sheet. The valuation of land and buildings is subject to a number of assumptions and judgements. A small movement in these assumptions can have a material impact on the financial statements.

In addition, there is judgement applied in determining the classification of assets between property, plant and equipment and investment properties, and hence the basis of valuation could be incorrectly applied.

What did we do?

We have:

- Reviewed the output of the Council's valuation experts;
- Performed procedures to satisfy ourselves that the Council's expert were reliable to carry out the valuations;
- Challenged the assumptions used by reference to external evidence and the CIPFA Code of Practice on Local Authority Accounting; and
- Tested the journals for the valuation adjustments to ensure that they were accurately processed.

When valuing the Council dwelling stock, standard practice is to apply an adjustment known as the Existing Use Value - Social Housing (EUV-SH) factor, recognising that stock is used for social housing. The Department for Communities and Local Government (DCLG) updated the EUV-SH factor for Northumberland to 44% in 2016/17; however the Council's valuers applied a factor of 41% in their valuation.

The rationale provided was that this revised factor reflects the government policy for an annual social housing rent decrease of 1% per annum. We consulted with our internal valuation experts who confirmed that their understanding was that the 1% rent decrease was built into the EUV-SH factor issued by DCLG; however they pointed to guidance confirming that there is a 5% tolerance on the EUV-SH factor used before it is deemed to be an unreasonable assumption. Given that the factor used falls within this range we are satisfied that there is no impact on our audit opinion.

Audit issues and approach:

What did we do?

The value of investment property in the Council's Group financial statements is approximately £286 million, reflecting the value of investment property held by the Arch Group. As part of our audit, we identified that land and buildings leased to Ashington Football Club, owned by Arch, has been valued at approximately £1.9 million, on a depreciated replacement cost basis. We consulted with our EY valuation team who consider that a more appropriate basis of valuation would be market value. There is some judgement required in determining the valuation basis; however the EY valuation team estimate that a valuation at market value would be in the region of between £0.25 million and £0.5 million. We have recommended that management at the Arch Group commission a valuation of this asset using market value; however as the difference in valuation is not material to the Council's Group financial statements we have included a judgemental unadjusted difference of £1.5 million in the summary of unadjusted differences in section 4.

No further material issues were identified as part of this work.

Audit issues and approach:

Accounting for group pension obligations

What are our conclusions?

We have not identified any material misstatement in our testing of the Council's pension obligation and IAS19 accounting.

What is the risk?

Funding of the Council's participation in the local government pension scheme will continue to have an impact on both Council cash flows and balance sheet liabilities.

Pension liabilities are summarised in the table below:

	31 March 2017 £m	31 March 2016 £m	31 March 2015 £m
Net assets excluding pension liability	£1,018m	£923m	£864m
Pension liability	£678m	£652m	£678m

The pension liability is the most significant liability on the Council's balance sheet and is calculated through use of a number of actuarial assumptions. A small movement in these assumptions can have a material impact on the balance sheet.

Over the last three years the Council's net liability has fluctuated and continues to be a pressure on the Council's finances.

What did we do?

We have:

- Reviewed the output from the Council's actuary;
- Obtained assurances over the completeness of information provided to the actuary from the Northumberland Pension Fund audit team;
- Reviewed the assumptions used by the actuary to determine whether they are in our expected range, through liaison with internal actuarial specialists; and
- Tested the journal entries used to post the journal entries.

No significant issues have been identified as part of this work.

Audit issues and approach:

Changes to the Code of Practice

What are our conclusions?

The Council has correctly applied the changes to the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 ("the Code"), including changes in financial statement presentation, to reflect new reporting requirements.

What is the risk?

Amendments have been made to the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 ("the Code") including changes in financial statement presentation to reflect new reporting requirements.

The new reporting requirements impact the Comprehensive Income and Expenditure Statement ("CIES") and the Movement in Reserves Statement ("MiRS"), and include the introduction of the new 'Expenditure and Funding Analysis' note as a result of the 'Telling the Story' review of the presentation of local authority financial statements.

The Code no longer requires statements or notes to be prepared in accordance with the Service Reporting Code of Practice ("SeRCOP"). Instead the Code requires that the service analysis is based on the organisational structure under which the Council operates.

This change in the Code required a new structure for the primary statements, new notes and a full retrospective restatement of impacted primary statements.

What did we do?

We have:

- Reviewed the Expenditure and Funding Analysis, CIES and associated notes to ensure the disclosures are in line with the Code;
- Reviewed the analysis of how these figures are derived, how the ledger system has been re-mapped to reflect the Council's organisational structure and how overheads are apportioned across the service areas reported; and
- Agreed the restated comparative figures back to the Council's segmental analysis and supporting working papers.

No significant issues have been identified as part of this work.

Audit issues and approach:

Loans to third parties

What are our conclusions?

Loans to third parties have been approved in line with agreed Council procedures.

What is the risk?

The Council has made loans to third parties in the year, including a significant loan in the region of £90 million to the Arch Group to fund the purchase of the Manor Walks retail park.

Loans to third parties can have a significant impact on the Council's treasury strategy and there is also specific guidance on when a local authority can make loans to other bodies.

What did we do?

We have:

- Agreed approvals of loans to supporting documentation, including minutes of meetings and signed statements from the s151 officer;
- Agreed the transfer of cash to third party was within the approved limits; and
- Performed procedures to assess the recoverability of the loans.

We noted that the level of loans to third parties exceeded the level planned for 2016/17; however this was reported appropriately in the treasury management outturn report.

No significant issues have been identified as part of this work.



03 Audit Report

Draft audit report

Our draft opinion on the financial statements

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF NORTHUMBERLAND COUNTY COUNCIL

Opinion on the Authority and firefighters' pension fund financial statements

We have audited the financial statements and the firefighters' pension fund financial statements of Northumberland County Council (Authority or Council) for the year ended 31 March 2017 under the Local Audit and Accountability Act 2014. The financial statements comprise the:

- Authority and Group Movement in Reserves Statement,
- Authority and Group Comprehensive Income and Expenditure Statement,
- Authority and Group Balance Sheet,
- Authority and Group Cash Flow Statement,
- Notes to the Authority Financial Statements 1 to 54,
- Notes to the Group Financial Statement 1 to 21
- Housing Revenue Account Income and Expenditure Statement and related notes 1 to 13,
- Collection Fund and the related notes 1 to 4,
- and include the firefighters' pension fund financial statements comprising the Fund Account, the Net Assets Statement and the related notes 1 to 3.

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 2016/17.

This report is made solely to the members of Northumberland County 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 Northumberland County Council and the Northumberland County Council's members as a body, for our audit work, for this report, or for the opinions we have formed.



Audit Report

Draft audit report (continued)

Our draft opinion on the financial statements (continued)

Respective responsibilities of the Director of Corporate Resources and auditor

As explained more fully in the Director of Corporate Resources Responsibilities set out on page 236, the Director of Corporate Resources is responsible for the preparation of the Statement of Accounts, which includes the Authority and Group financial statements and the firefighters pension fund 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 2016/17, and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

This includes an assessment of: whether the accounting policies are appropriate to the Authority and Group and the firefighters pension fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Corporate Resources; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Statement of Accounts 2016/17 to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the financial position of Northumberland County Council and Group as at 31 March 2017 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 2016/17.

Opinion on other matters

In our opinion, the information given in the Statement of Accounts 2016/17 for the financial year for which the financial statements are prepared is consistent with the financial statements.



Audit Report

Draft audit report (continued)

Our draft opinion on the financial statements (continued)

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

Conclusion on Northumberland County Council's arrangements for securing economy, efficiency and effectiveness in the use of resources

Authority's responsibilities

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.

Auditor's responsibilities

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.



Audit Report

Draft audit report (continued)

Our draft opinion on the financial statements (continued)

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 2016, as to whether Northumberland County 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 Northumberland County Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2017.

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, Northumberland County Council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Basis for Qualified Conclusion

- **Informed decision making**

A review of the Arch Group (a wholly owned subsidiary) by the Council's internal auditors identified that there were some significant weaknesses in proper arrangements for acting in the public interest and that there was evidence that the principles and values of sound governance were not appropriately applied for decisions taken for the year ended 31 March 2017.

Qualified conclusion

On the basis of our work, having regard to the guidance issued by the C&AG in November 2016, with the exception of the matter reported in the basis for qualified conclusion paragraph above, we are satisfied that, in all significant respects, Northumberland County Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2017.

Certificate

We certify that we have completed the audit of the accounts of Northumberland County Council in accordance with the requirements of the Local Audit and Accountability Act 2014 and the Code of Audit Practice issued by the National Audit Office.

Stephen Reid (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Appointed Auditor
Edinburgh
23 November 2017



04

Audit Differences



Audit differences

In any audit, we may identify misstatements between amounts we believe should be recorded in the financial statements and 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

Uncorrected misstatements

We highlight the following judgemental misstatement identified during the audit process:

- Investment properties in the Group financial statements are overstated by approximately £1.5 million due to land and buildings at Ashington Football Club, owned by the Arch Group, being valued on a depreciated replacement cost basis rather than a market value basis.

Corrected misstatements

We highlight the following misstatements identified during the audit process. These have been corrected by management:

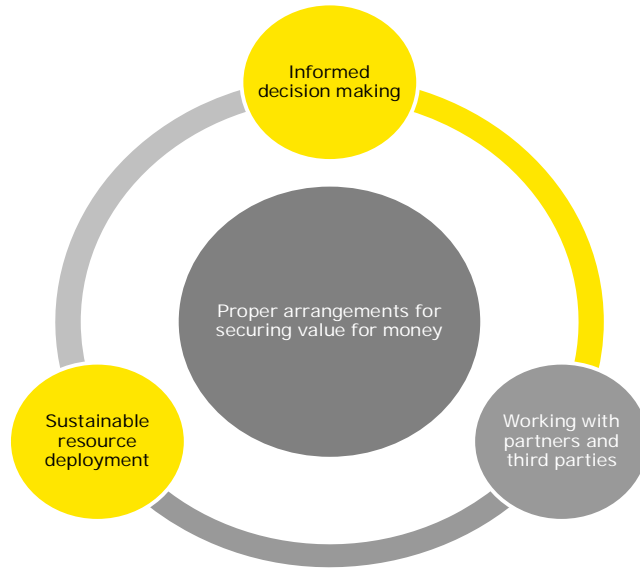
- As part of their quality review of the unaudited draft financial statements management identified that the journal for netting debtors and creditors with central government in relation to payments had not been posted. This has been amended in the final financial statements and short term debtors and creditors with central government have been reduced by £36,929,458; and
- At the request of the leader of the Council, a revenue to capital contribution of £15.7 million posted in the unaudited draft financial statements has been reversed.



05 Value for Money



Value for Money



Economy, efficiency and effectiveness

We must consider whether you have 'proper arrangements' to secure economy, efficiency and effectiveness in your use of resources. This is known as our value for money conclusion.

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 use the CIPFA/SOLACE framework for local government to ensure that our assessment is made against an already existing mandatory framework which you use in documents such as your Annual Governance Statement.

Overall conclusion

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 Plan we identified a significant risk in respect of financial planning, with a particular focus on the phasing of required savings. Our findings in respect of this risk are summarised over the page.

Following presentation of our Audit Plan we were made aware of allegations of impropriety at the Arch Group, a group of wholly owned subsidiary companies. The Council's internal auditors were commissioned to undertake a review of arrangements. We requested a copy of the draft report in relation to the review, together with details of the emergent findings in early August. In October 2017 management provided access to the information and met with us to discuss the findings. We have concluded that, as the review identified that the principles and values of sound governance were not always in place for some decisions taken during 2016/17, a modification to our value for money opinion was required.

Value for Money

Overall conclusion

In August 2017 the Council commissioned an independent review of financial arrangements to ensure that decision making going forward would be based on complete and transparent financial information and that the baseline position was accurate. The review focused on the accuracy and completeness of the base budget, together with the veracity of the underpinning processes and systems and the Council's longer term financial plans. The overall conclusion from the review was that, whilst areas for improvement to the process of preparing the budget were identified, there were no indications of significant errors or omissions and that there was an adequate base to take forward future financial plans. We are satisfied that there were no findings from this review that are material to our value for money conclusion.

As part of our consideration of the Council's value for money arrangements, we also considered the impact of the change in administration on the risks to our conclusion and factored this into our work on the medium-term financial plan. Following the change in administration a number of significant decisions were taken subsequent to the financial year end. Given the timing of these decisions, we are satisfied that there is no impact on our 2016/17 value for money conclusion. Decisions taken since 1 April 2017, including reversal of plans to move Council Headquarters from the existing County Hall to Ashington and the termination of employment of the former Chief Executive and section 151 officer, together with the broader senior team restructuring will be factored into our planning for 2017/18 audit.

Value for Money (continued)

What is the significant VFM risk?	What arrangements did this affect?	What are our findings?
<p>The most recent medium financial plan shows that the Council is required to make savings in the region of £36 million over the period 2017/18 – 2019/20. Of the total savings requirement, £30 million is planned for delivery in the final two years of the plan.</p> <p>Given that the Council has been operating in a challenging environment for a number of years now, savings will typically be required to be delivered through more challenging transformational schemes.</p>	<p>Deploying resources in a sustainable manner</p>	<p>We reviewed the assumptions used to develop the medium term financial plan (MTFP) and have no matters to raise over the assumptions used.</p> <p>Our significant risk was attached to the phasing of savings and that £30 million of savings were required in the final two years of the financial plan. Through discussion with management we noted that there are currently no firm plans in place for achieving this £30 million as, following the change in administration, all existing savings plans are being reviewed.</p> <p>We considered the financial position of the Council to determine the impact of not having fully developed savings plans and noted that total useable reserves at 31 March 2017 are £137.9 million. This demonstrates that even if the Council was to make no savings in the final two years of the MTFP there would still be useable reserves available greater than £100 million.</p> <p>We also benchmarked the level of reserves held by the Council based on data held by the PSAA for the Council's nearest statistical neighbours and noted that levels of reserves are in the highest 20% of similar authorities.</p> <p>We concluded that we are satisfied that there is no impact on our value for money conclusion.</p>



06

Other reporting matters



Other reporting matters

Other reporting matters

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 audited financial statements.

Financial information in the Narrative Report and published with the financial statements was consistent with the audited financial statements.

We have reviewed the Annual Governance Statement for completeness of disclosures, consistency with other information from our work, and whether it complies with relevant guidance. No matters have been noted.

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.

No matters have been noted.

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.



07

Assessment of Control Environment



Assessment of control environment

Financial controls

It is the responsibility of the Council 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 Council 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.

We did not identify any issues to report to you that have not already been identified by management.



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Appendices



Appendix A

Required communications with the Audit Committee

There are certain communications that we must provide to the Audit Committee. We have done this by:

		 Our Reporting to you
Required communications	 What is reported?	  When and where
Terms of engagement	Confirmation by the Audit 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.
Planning and audit approach	Communication of the planned scope and timing of the audit, including any limitations.	March 2017 Audit Plan
Significant findings from the audit	<ul style="list-style-type: none"> ▶ Our view of the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▶ Any significant difficulties encountered during the audit ▶ Any significant matters arising from the audit that were discussed with management ▶ Written representations we have requested ▶ Expected modifications to the audit report ▶ Any other matters significant to overseeing the financial reporting process 	September 2017 November 2017 Audit Results Report
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 the 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 ▶ Significant corrected misstatements, in writing 	September 2017 Audit Results Report







Appendix A

		Our Reporting to you
Required communications	What is reported?	When and where
Fraud	<ul style="list-style-type: none"> ▶ Asking the Audit Committee whether they have knowledge of any actual, suspected or alleged fraud affecting the Council ▶ Unless all those charged with governance are involved in managing the entity, any fraud identified or information obtained indicating that a fraud may exist involving: <ul style="list-style-type: none"> (a) management; (b) employees with significant roles in internal control; or (c) others where the fraud results in a material misstatement in the financial statements. ▶ A discussion of any other matters related to fraud, relevant to Audit Committee responsibility. 	<p>We have asked management and those charged with governance about arrangements to prevent or detect fraud.</p> <p>Management informed us of some potential allegations of fraud. We have concluded that it is not material to our financial statement audit opinion.</p>
Related parties	<p>Significant matters arising during the audit in connection with the Council's related parties including, where 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/or regulations ▶ Difficulty in identifying the party that ultimately controls the entity 	We have no matters to report.
Subsequent events	<ul style="list-style-type: none"> ▶ Where appropriate, asking the Audit Committee whether any subsequent events have occurred that might affect the financial statements. 	We have asked management and those charged with governance. We have no matters to report.
Other information	<ul style="list-style-type: none"> ▶ Where material inconsistencies are identified in other information included in the document containing the financial statements, but management refuses to make the revision. 	We have no matters to report.
External confirmations	<ul style="list-style-type: none"> ▶ Management's refusal for us to request confirmations ▶ We were unable to obtain relevant and reliable audit evidence from other procedures. 	We have no matters to report.



Appendix A

		 Our Reporting to you
Required communications	 What is reported?	  When and where
Consideration of laws and/or regulations	<ul style="list-style-type: none"> ▶ Audit findings of non-compliance where it is material and believed to be intentional. This communication is subject to compliance with legislation on “tipping off” ▶ Asking the Audit Committee about possible instances of non-compliance with laws and/or regulations that may have a material effect on the financial statements, and known to the Audit Committee. 	We have not identified any material instances or non-compliance with laws and regulations.
Significant deficiencies in internal controls identified during the audit	<ul style="list-style-type: none"> ▶ Significant deficiencies in internal controls identified during the audit. 	September 2017 Audit Results Report
Independence	<p>Communication of all significant facts and matters that have a bearing on EY’s objectivity and independence.</p> <p>Communicating 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 on the firm’s general policies and processes for maintaining objectivity and independence <p>Communications whenever significant judgments are made about threats to objectivity or independence and the appropriateness of safeguards,</p>	March 2017 Audit Plan September 2017 Audit Results Report
Fee Reporting	<p>Breakdown of fee information when the audit plan is agreed</p> <p>Breakdown of fee information at the completion of the audit</p> <p>Any non-audit work</p>	March 2017 Audit Plan September 2017 Audit Results Report
Certification work	Summary of certification work	January 2018



Independence

We confirm that there are no changes in our assessment of independence since our confirmation in our Audit Plan dated 31 March 2017.

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 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 Committee 22 September 2017.

As part of our reporting on our independence, we set out below a summary of the fees paid for the year ended 31 March 2017.

We confirm that we have undertaken non-audit work outside the PSAA Code requirements in relation to tax advice.

We have adopted the necessary *safeguards* in completing this work and complied with Auditor Guidance Note 1 issued by the NAO in December 2016.

	Final Fee 2015/16 £	Planned Fee 2016/17 £	Scale Fee 2016/17 £	Final Fee 2016/17 £
Total Audit Fee – Code Work	195,596	197,796*	190,596	TBC
Non –audit work – Housing Benefit Subsidy Claim	9,341	9,900	9,900	
Other certification work	16,600	**		
Non –audit work – Tax Services (Council)	40,350	-	-	40,350

* We agreed a scale fee variation in the region of £7,200 to reflect additional work undertaken



**We are currently liaising with funding bodies and the Council about the completion of the Teachers' Pension and Housing Pooling Return. The fees for these returns have not yet been agreed.



Appendix C



Accounting and regulatory update

Since the date of our last report to the Audit Committee, new accounting standards and interpretations have been issued. The following table provides a high level summary of those that have the potential to have the most significant impact on you:

Name	Summary of key measures 	Impact on Northumberland County Council 
<i>IFRS 9 Financial Instruments</i>	<p>Applicable for local authority accounts from the 2018/19 financial year and will change:</p> <ul style="list-style-type: none"> • How financial assets are classified and measured • How the impairment of financial assets are calculated • Financial hedge accounting • The disclosure requirements for financial assets. • Transitional arrangements are included within the accounting standard, however as the 2018/19 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be and whether any accounting statutory overrides will be introduced to mitigate any impact. 	<p>Although some initial thoughts on the approach to adopting IFRS 9 have been issued by CIPFA, until the Code is issued and any statutory overrides are confirmed there remains some uncertainty. However, what is clear is that the Council will have to:</p> <ul style="list-style-type: none"> • Reclassify existing financial instrument assets • Re-measure and recalculate potential impairments of those assets; and • Prepare additional disclosure notes for material items.
<i>IFRS 15 Revenue from Contracts with Customers</i>	<p>Applicable for local authority accounts from the 2018/19 financial year. This new standard deals with accounting for all contracts with customers except:</p> <ul style="list-style-type: none"> • Leases; • Financial instruments; • Insurance contracts; and • for local authorities; Council Tax and NDR income. <p>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.</p> <p>There are transitional arrangements within the standard; however as the 2018/19 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be.</p>	<p>As with IFRS 9, some initial thoughts on the approach to adopting IFRS 15 have been issued by CIPFA. However, until the Code is issued there remains some uncertainty. However, what is clear is that for all material income sources from customers the Council will have to:</p> <ul style="list-style-type: none"> • Disaggregate revenue into appropriate categories; • Identify relevant performance obligations and allocate income to each; and • Summarise significant judgements.



Appendix C

Name	Summary of key measures 	Impact on Northumberland County Council 
<i>IFRS 16 Leases</i>	<p>IFRS 16 will be applicable for local authority accounts from the 2019/20 financial year.</p> <p>Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease in a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet.</p> <p>There are transitional arrangements within the standard, although as the 2019/20 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be or whether any statutory overrides will be introduced.</p>	<p>Until the 2019/20 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area.</p> <p>However, what is clear is that the Council will need to undertake a detailed exercise to classify all of its leases and therefore must ensure that all lease arrangements are fully documented.</p>
<i>Earlier deadline for production and audit of the financial statements from 2017/18</i>	<p>The Accounts and Audit Regulations 2015 introduced a significant change in statutory deadlines from the 2017/18 financial year. From that year the timetable for the preparation and approval of accounts will be brought forward with draft accounts needing to be prepared by 31 May and the publication of the audited accounts by 31 July.</p>	<p>These changes provide challenges for both the preparers and the auditors of the financial statements.</p> <p>As auditors, nationally we have:</p> <ul style="list-style-type: none"> • Issued a thought piece on early closedown; • As part of the strategic Alliance with CIPFA jointly presented accounts closedown workshops across England, Scotland and Wales; and • Presented at CIPFA early closedown events and on the subject at the Local Government Accounting Conferences in July 2017.



Appendix D

Management representation letter

Management Representation Letter

[To be prepared on the entity's letterhead]

[Date]

Ernst & Young LLP
Citygate
St James' Boulevard
Newcastle upon Tyne
NE1 4JD

This letter of representations is provided in connection with your audit of the consolidated and council financial statements of Northumberland County Council ("the Group and Council") for the year ended 31 March 2017. 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 consolidated and council financial statements give a true and fair view of the Group and Council financial position of Northumberland County Council as of 31 March 2017 and of its financial performance (or operations) and its cash flows for the year then ended in accordance with, for the Group and Council, CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.

We understand that the purpose of your audit of our consolidated and council financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing, 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, for the Group and Council, the Accounts and Audit Regulations 2015 and CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.



Appendix D

Management Representation Letter (continued)

2. We acknowledge, as members of management of the Group and Council, our responsibility for the fair presentation of the consolidated and council financial statements. We believe the consolidated and council 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 Group and Council in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 and are free of material misstatements, including omissions. We have approved the consolidated and council financial statements.
3. The significant accounting policies adopted in the preparation of the Group and Council financial statements are appropriately described in the Group and Council financial statements.
4. As members of management of the Group and Council, we believe that the Group and Council have 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 2016/17 for the Group and Council that are free from material misstatement, whether due to fraud or error.
5. We confirm that the unadjusted difference of £1.5 million in the Group financial statements in relation to the over-valuation of land and buildings at Ashington Football Club, owned by the Arch Group, is not material to the Group financial statements.

B. Fraud

1. We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.
2. 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.
3. We have disclosed to you all significant facts relating to any frauds, suspected frauds or allegations of fraud known to us that may have affected the Group or Council (regardless of the source or form and including, without limitation, allegations by “whistle-blowers”), whether involving management or employees who have significant roles in internal control. Similarly, we have disclosed to you our knowledge of frauds or suspected frauds affecting the entity involving others where the fraud could have a material effect on the consolidated or council financial statements. We have also disclosed to you all information in relation to any allegations of fraud or suspected fraud communicated by employees, former employees, analysts, regulators or others, that could affect the consolidated or council financial statements

C. Compliance with Laws and Regulations

1. We have disclosed to you all identified or suspected non-compliance with laws and regulations whose effects should be considered when preparing the consolidated and council financial statements.



Appendix D

Management Representation Letter (continued)

D. 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 Council and Cabinet (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: [list date].
4. We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the Group and 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 consolidated and council financial statements.
5. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.
6. We have disclosed to you, and the Group and 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.

E. 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 in the consolidated and council financial statements all guarantees that we have given to third parties.



Appendix D

Management Representation Letter (continued)

F. 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.

G. Group audits

1. Necessary adjustments have been made to eliminate all material intra-group unrealised profits on transactions amongst council, subsidiary undertakings and associated undertakings.

H. Other information

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

I. Comparative information – corresponding financial information

1. There have been changes to the structure of the financial statements for 2016/17 with the introduction of the Expenditure and Funding Analysis and related notes. The comparative information for 2015/16 has been restated to incorporate these changes.
2. The comparative amounts have been correctly restated to reflect the above matter and appropriate note disclosure of this restatement has also been included in the current year's consolidated and council financial statements.

J. Ownership of Assets

1. Except for assets capitalised under finance leases, the Group and Council has satisfactory title to all assets appearing in the balance sheet and there are no liens or encumbrances on the Group and Council's assets, nor has any asset been pledged as collateral. All assets to which the Group and Council has satisfactory title appear in the balance sheet.



Appendix D

Management Representation Letter (continued)

K. Reserves

1. We have properly recorded or disclosed in the consolidated and council financial statements the useable and unusable reserves.

L. Use of the Work of a Specialist

1. We agree with the findings of the specialists that we engaged to evaluate the actuarial assumptions used in calculating the value of liability for the local government pension scheme 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.
2. We agree with the findings of the specialist that we engaged to value our land and buildings 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.

Yours faithfully,

(Interim Director of Finance, s151 officer)

(Interim Chief Executive)

(Chair of the Audit Committee)

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