

Annual Audit Letter

Stockton-on-Tees Borough Council

Year ended 31 March 2020





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1. EXECUTIVE SUMMARY

Purpose of the Annual Audit Letter

Our Annual Audit Letter summarises the work we have undertaken as the auditor for Stockton-on-Tees Borough Council (the Council) and the Stockton-on-Tees Borough Council Group (the Group) for the year ended 31 March 2020. Although this letter is addressed to the Council, it is designed to be read by a wider audience including members of the public and other external stakeholders.

Our responsibilities are defined by the Local Audit and Accountability Act 2014 (the 2014 Act) and the Code of Audit Practice issued by the National Audit Office (the NAO). The detailed sections of this letter provide details on those responsibilities, the work we have done to discharge them, and the key findings arising from our work. These are summarised below.

Area of responsibility	Summary
Audit of the financial statements	<p>Our auditor's report issued on 7 December 2020 included our opinion that the financial statements:</p> <ul style="list-style-type: none">• give a true and fair view of the Council's and Group's financial position as at 31 March 2020 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 2019/20.
Other information published alongside the audited financial statements	<p>Our auditor's report included our opinion that:</p> <ul style="list-style-type: none">• the other information in the Statement of Accounts is consistent with the audited financial statements.
Value for money conclusion	<p>Our auditor's report concluded that we are satisfied that in all significant respects, the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2020.</p>
Reporting to the group auditor	<p>In line with group audit instructions, issued by the NAO on 4th November, we reported to the group auditor in line with the requirements applicable to the Council's WGA return on 7 December 2020.</p>
Statutory reporting	<p>Our auditor's report confirmed that we did not use our powers under s24 of the 2014 Act to issue a report in the public interest or to make written recommendations to the Council.</p>



2. AUDIT OF THE FINANCIAL STATEMENTS

Opinion on the financial statements

Unqualified

The scope of our audit and the results of our work

The purpose of our audit is to provide reasonable assurance to users that the financial statements are free from material error. We do this by expressing an opinion on whether the statements are prepared, in all material respects, in line with the financial reporting framework applicable to the Council and Group and whether they give a true and fair view of the Council's and Group's financial position as at 31 March 2020 and of its financial performance for the year then ended.

Our audit was conducted in accordance with the requirements of the Code of Audit Practice issued by the NAO, and International Standards on Auditing (ISAs). These require us to consider whether:

- the accounting policies are appropriate to the Council's and Group's circumstances and have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management in the preparation of the financial statements are reasonable; and
- the overall presentation of the financial statements provides a true and fair view.

Our auditor's report, stated that in our view, the financial statements give a true and fair view of the Council's and Group's financial position as at 31 March 2020 and of its financial performance for the year then ended. We included an emphasis of matter paragraph in our report to highlight to readers the valuation uncertainty arising due to the COVID-19 pandemic, that was disclosed by the Council/Group in the financial statements. Our opinion was not modified in respect of this matter.

Our approach to materiality

We apply the concept of materiality when planning and performing our audit, and when evaluating the effect of misstatements identified as part of our work. We consider the concept of materiality at numerous stages throughout the audit process, in particular when determining the nature, timing and extent of our audit procedures, and when evaluating the effect of uncorrected misstatements. An item is considered material if its misstatement or omission could reasonably be expected to influence the economic decisions of users of the financial statements.

Judgements about materiality are made in the light of surrounding circumstances and are affected by both qualitative and quantitative factors. As a result we have set materiality for the financial statements as a whole (financial statement materiality) and a lower level of materiality for specific items of account (specific materiality) due to the nature of these items or because they attract public interest. We also set a threshold for reporting identified misstatements to the Audit and Governance Committee. We call this our trivial threshold.

The table below provides details of the materiality levels applied in the audit of the financial statements for the year ended 31 March 2020:

Financial statement materiality	Our financial statement materiality is based on 2% of Gross Operating Expenditure at the surplus or deficit on provision of services level.	Council: £9.614m Group: £9.650m
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	Council: £288k Group: £290k
Specific materiality	We have applied a lower level of materiality to the following areas of the accounts: - Members allowances - Senior manager remuneration - Exit packages	£175k £182k £359k



2. AUDIT OF THE FINANCIAL STATEMENTS

Our response to significant risks

As part of our continuous planning procedures we considered whether there were risks of material misstatement in the Council's and Group's financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Audit and Governance Committee within our Audit Strategy Memorandum and provided details of how we responded to those risks in our Audit Completion Report. The table below outlines the identified significant risks, the work we carried out on those risks and our conclusions.

Identified significant risk	Our response	Our findings and conclusions
<p>Management override of controls (Council and Group) In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Because of the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.</p>	<p>We addressed this risk through performing audit work over:</p> <ul style="list-style-type: none"> Accounting estimates impacting on amounts included in the financial statements; Consideration of identified significant transactions outside the normal course of business; and Journals recorded in the general ledger and other adjustments made in preparation of the financial statements. 	<p>Our audit work provided the assurance we sought and did not identify any material issues.</p>
<p>Property, Plant and Equipment Valuation (Council) The financial statements contain material entries on the Balance Sheet as well as material disclosure notes in relation to the Council's holding of PPE. Although the Council uses valuation experts to provide information on valuations, there remains a high degree of estimation uncertainty associated with the revaluation of PPE due to the significant judgements and number of variables involved in providing revaluations. We therefore identified the valuation of PPE to be an area of significant risk.</p>	<p>We addressed this risk by considering the Council's arrangements for ensuring that PPE values are reasonable and engaged our own expert to provide data to enable us to assess the reasonableness of the valuations provided by the Council's valuers. We also assessed the competence, skills and experience of the valuers.</p> <p>We discussed methods used with the valuers and examined supporting information. We used indices provided by our own expert to confirm the assets not revalued are unlikely to have materially changed in value. We tested a sample of revaluations in year to valuation reports and supporting information, and also undertook procedures to gain assurance over the source data used in the valuations.</p> <p>We also considered the impact of COVID-19 on the valuations to gain additional assurance on their reasonableness.</p>	<p>The Council's valuers followed guidance issued by the Royal Institute of Chartered Surveyors and their valuation reports disclosed a "material valuation uncertainty" in relation to the valuation of the Council's land and buildings. This has been disclosed in note 5 of the financial statements. We included reference to this disclosure as an 'emphasis of matter' in our audit report. The purpose of this paragraph is to draw attention to this disclosure, it is not a qualification and did not modify our unqualified opinion on the financial statements.</p> <p>Our work provided the assurance we sought and we did not identify any other material issues.</p>



2. AUDIT OF THE FINANCIAL STATEMENTS

Identified significant risk	Our response	Our findings and conclusions
<p>Defined benefit liability valuation (Council) The financial statements contain material pension entries in respect of retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. Moreover, in 2019/20 the local government pension fund assets and liabilities were subject to triennial revaluation. This resulted in an increased risk of material misstatement.</p>	<p>We discussed with key contacts any significant changes to the pension estimates. In addition to our standard programme of work in this area, we evaluated the management controls that you have in place to assess the reasonableness of the figures provided by the Actuary and considered the reasonableness of the Actuary's output, referring to our expert's report on all actuaries nationally.</p> <p>We reviewed the appropriateness of the key assumptions included within the valuations, compared them to expected ranges and reviewed the methodology applied in the valuation. We also considered the adequacy of disclosures in the financial statements.</p>	<p>The pension fund disclosed a "material valuation uncertainty" in relation to the valuation of the Pension Fund's property investments, arising from the potential impact of covid-19 on values. This has been disclosed in the final version of the financial statements. We, in line with normal practice, included reference to this disclosure as an 'emphasis of matter' in our audit report. The purpose of this paragraph is to draw attention to this disclosure, it is not a qualification and does not modify our proposed unqualified opinion on the financial statements.</p>

Internal control recommendations

As part of our audit we considered the internal controls in place that are relevant to the preparation of the financial statements. We did this to design audit procedures that allow us to express our opinion on the financial statements, but this did not extend to us expressing an opinion on the effectiveness of internal controls.

Our work did not identify any significant deficiencies to report, and there were none in the prior year to follow up.



3. VALUE FOR MONEY CONCLUSION

Value for money conclusion	Unqualified
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Our audit approach

We are required to consider whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out in order to form our conclusion, and sets out the criterion and sub-criteria that we are required to consider.

The overall criterion is that, ‘in all significant respects, the 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.’ To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:

- informed decision making;
- sustainable resource deployment; and
- working with partners and other third parties.

Our auditor’s report, stated that, in all significant respects, the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31st March 2020.

Sub-criteria	Commentary	Arrangements in place?
Informed decision making	<ul style="list-style-type: none"> • Constitution in place which is available on the Council's website. • Council plan in place for the period 2019 to 2022, and updated for period 2020 to 2023, on the Council’s website. • Leader's retrospective annual review undertaken. • Management team stable. • No data quality issues in respect of performance information we are aware of. • Regular reporting to TCWG of performance and financial information, including variances. • Medium term planning undertaken and plans in place; i.e. Council Plan 2019/2022 (updated for period 2020 to 2023) and 2019/2023 Medium Term Financial Plan (MTFP) (updated for period 2020-2023), and which are updated at least annually. Mid year report to Cabinet also sets out position on MTFP and impact for future years, including up to date risk assessment of the potential impact of COVID-19 pandemic. • Regular and timely reporting to members. • Risk register and risk management arrangements in place. Risks reported to Audit Committee and regular reporting by Internal Audit. • Annual governance statement prepared, reviewed and approved by Members. 	Yes



3. VALUE FOR MONEY CONCLUSION

Sub-criteria	Commentary	Arrangements in place?
Sustainable resource deployment	<ul style="list-style-type: none"> Financial and performance reports record achievement in meeting financial targets. Need to transform services to reduce costs recognised. MTFP updated at least annually as part of budget setting and progress monitoring undertaken including achieving savings targets. Mid year report to Cabinet also sets out position on MTFP and impact for future years, including up to date risk assessment of the potential impact of COVID-19 pandemic. Asset register in place and Capital Strategy in place. SWiS (Smarter working in Stockton) programme incorporates use of assets/estate. HR policies and procedures in place. Sickness information and reports are provided to Corporate Management Team, Human Resources Service Group and Heads of Service. 	Yes
Working with partners and other third parties	<ul style="list-style-type: none"> Examples of partnership working in place to reduce costs and improve service delivery. Better Care Fund in place with Health and Wellbeing Board having oversight and receiving quarterly updates. Council plan in place for the period 2019 to 2022 (updated for period 2020 to 2023), and on the Council's website. Council has written procedures for procuring products and services, which are within its Constitution (part 4). 	Yes



3. VALUE FOR MONEY CONCLUSION

Significant audit risks

The NAO’s guidance requires us to carry out work to identify whether or not a risk to our conclusion exists. Risk, in the context of our work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Council being inadequate. In our Audit Strategy Memorandum, we reported that we had identified one significant audit risk. The work we carried out in relation to significant risks is outlined below.

Risk	Work undertaken	Conclusion
<p>Risk heading</p> <p>Our audit work in previous years has concluded that the Council has robust arrangements in place for Medium Term Financial Planning.</p> <p>We need to ensure our knowledge of the Council’s MTFP arrangements remains up to date in order to ensure we give the correct VFM conclusion.</p>	<p>Building on our work in previous years, we:</p> <ul style="list-style-type: none"> reviewed the Council’s updated MTFP to ensure it reflects the latest funding position from central government and makes reasonable assumptions for future funding; reviewed and updated our knowledge of the arrangements the Council has in place to monitor and deliver any savings identified, any additional income generation and any measures to manage future cost pressures that underpin the MTFP. <p>We found that the MTFP, issued in February 2020 for the period 2020/2024, reports the known changes, but also reports the significant changes that could lead from national changes to future funding arrangements that are not yet finalised, and as such the funding position in the medium term remains uncertain. The overall planned position for the Council at that time, based on known factors, was a largely balanced position over the period to 2024. The Council has adequate reserves in the medium term, including £60m in useable revenue reserves at the end of March 2020.</p> <p>The arrival of COVID-19 in the UK has had a significant impact on the Council and its finances. Officers have reviewed and updated the position as the impact became clearer, and presented an update report to Cabinet/Council in July 2020. This reported a significant impact in 2020/21 and a net requirement, after available grants at that time of circa £6m. Clearly this will be subject to change as we continue to move through the crisis and its effects, but officers remain committed to ongoing updates to the Council’s plans as things become clearer. We also note that the Council retains adequate usable revenue reserves for the medium term.</p>	<p>We updated our knowledge of the arrangements the Council has in place, and our work mitigated the risk we identified at the planning stage. The MTFP reflected the latest Government announcements, and had been updated on a timely basis to reflect the potential impact of COVID-19.</p>



4. OTHER REPORTING RESPONSIBILITIES

Exercise of statutory reporting powers	No matters to report
Completion of group audit reporting requirements	Below testing threshold
Other information published alongside the audited financial statements	Consistent

The NAO's Code of Audit Practice and the 2014 Act place wider reporting responsibilities on us, as the Council's external auditor. We set out below, the context of these reporting responsibilities and our findings for each.

Matters on which we report by exception

The 2014 Act provides us with specific powers where matters come to our attention that, in our judgement, require reporting action to be taken. We have the power to:

- issue a report in the public interest;
- make statutory recommendations that must be considered and responded to publicly;
- apply to the court for a declaration that an item of account is contrary to law; and
- issue an advisory notice under schedule 8 of the 2014 Act.

We have not exercised any of these statutory reporting powers.

The 2014 Act also gives rights to local electors and other parties, such as the right to ask questions of the auditor and the right to make an objection to an item of account. We did not receive any such objections or questions.

Reporting to the NAO in respect of Whole of Government Accounts consolidation data

The NAO, as group auditor, requires us to complete the WGA Assurance Statement in respect of its consolidation data. We submitted this information to the NAO on 7 December 2020.

Other information published alongside the financial statements

The Code of Audit Practice requires us to consider whether information published alongside the financial statements is consistent with those statements and our knowledge and understanding of the Council. In our opinion, the other information in the Statement of Accounts is consistent with the audited financial statements.



5. OUR FEES

Fees for work as the Authority's auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum, presented to the Audit and Governance Committee in February 2020. This was based on the scale fee set by Public Sector Audit Appointments Limited. As noted throughout the year, we highlighted that there would be additional recurring audit fees as a result of increased regulatory pressures and requirements. We also mentioned that we would review the final position on fees when the audit was concluded.

Following completion of the audit, we have revisited the fees for 2019/20. In addition to the increase in the base audit fee, there have been some one-off increases in the audit fee for the 2019/20 audit year, and mainly relate to audit issues arising from the Covid-19 pandemic and other matters.

Any variations to the final fee will also require the approval of Public Sector Audit Appointments Limited, which manages the contracts for our work.

Area of work	2019/20 proposed fee / PSAA scale fee (£)	2019/20 final fee (£)
Delivery of audit work under the NAO Code of Audit Practice	97,604	97,604
Fee in respect of group consolidation (previously agreed)	3,220	3,228
Recurring increases in the base audit fee arising from regulatory pressures		15,128
One-off fee increases for 2019/20 specific issues		4,469
Total Audit Fees	100,824	120,429

All fees are subject to VAT

Analysis of Recurring increases in the base audit fee arising from regulatory pressures

Audit area for recurring additional work	Final fee 2019/20
Additional work on PPE and related valuations	£5,295
Additional work on pensions	£4,538
Additional work on review of journals	£3,026
Additional work in relation to the consideration of going concern	£2,269
Total additional fee for 2019/20 (recurring in future years)	£15,128



5. OUR FEES

Analysis of One-off fee increases for 2019/20 specific issues

Additional work relating to the 2019/20 audit	Final fee 2019/20
Additional procedures, including the impact of delays, in addressing the issues raised in the Pension Fund auditor assurance letter and the resolution of issues arising, including the overstatement of Pension Fund assets and the matters raised in relation to the Pension Fund category of 'undecideds'	£1,532
Additional procedures in relation to Material Valuation Uncertainty of the Council's property assets, including disclosures and the inclusion of an Emphasis of Matter paragraph in the audit report, which was subject to Consultant Partner Review	£1,236
Additional procedures in relation to Material Valuation Uncertainty of the Pension Fund's property assets, including disclosures and the inclusion of an Emphasis of Matter paragraph in the audit report, which was subject to Consultant Partner Review	£1,072
Additional procedures to consider the potential impact of the proposed remedy in the McCloud case against the pension liability disclosures, and consideration of the potential impact of the Goodwin case on pension liabilities	£629
Total additional fee for 2019/20 (not recurring)	£4,469

Fees for other work

We confirm that we have not undertaken any non-audit services for the Council or Group in the year.

We have undertaken or are engaged to undertake the following audit-related assurance services in relation to the 2019/20 financial year.

Area of work	2019/20 proposed fee	2019/20 final fee
Certification of Housing Benefit Subsidy Claim (work underway; this year's deadline has been extended due to the pandemic)	£10,900	£10,900 *
Teachers' Pensions (work completed)	4,150	4,150

* Subject to completion



6. FORWARD LOOK

Financial and operational challenges

The Council faces medium to long term uncertainty due to the impact of the COVID-19 pandemic, and how this will affect it in the longer term in terms of increased costs and lost revenue. In addition, the medium term position remains uncertain until a longer term spending review is announced, the outcome of the fair funding review is known, and the measures that will be taken in relation to the future operation of the business rates system take place.

The Council is relatively well placed financially with reserves available in the short term, however reserves are temporary or transitional and are not a long term solution.

Since the 2020 year end the Council has refreshed its medium term financial plan to respond to the COVID-19 pandemic, and we will consider this as part of our 2020/21 audit.

How we will work with the Council

We will focus our work on the risks that your challenges present to your financial statements and your ability to maintain proper arrangements for securing value for money.

In the coming year we will continue to support the Council by:

- continued liaison with the Council's Internal Auditors to minimise duplication of work;
- attending Audit and Governance Committee meetings and presenting an Audit Progress Report including updates on regional and national developments; and
- hosting events for staff, such as our Local Government Accounts workshop.

We will meet with key Council officers to identify any learning from the 2019/20 audit and will continue to share our insights from across local government and relevant knowledge from the wider public and private sector.

In terms of the technical challenges that officers face around the production of the statement of accounts, we will continue to work with them to share our knowledge of new accounting developments and we will be on hand to discuss any issues as and when they arise.

The Council has taken a positive and constructive approach to our audit and we wish to thank Members and officers for their support and co-operation during our audit.



6. FORWARD LOOK

Changes to the Code of Audit Practice

The Code of Audit Practice (the Audit Code), issued by the Comptroller and Auditor General, prescribes the way we carry out our responsibilities as your auditors. On 1st April 2020 a new Code came in to force and will apply to our work from 2020/21 onwards.

The new Audit Code continues to apply the requirements of International Standards on Auditing (ISAs) to our audit of the financial statements. While there are changes to the ISAs that are effective from 2020/21 the Audit Code has not introduced any changes to the scope of our audit of the financial statements. We will continue to give our opinion on the financial statements in our independent auditor's report.

There are however significant changes to the work on value for money arrangements, and the way we report the outcomes of our work to you.

The auditor's work on value for money arrangements

From 2020/21 we are still required to satisfy ourselves that you have made proper arrangements for securing the economy, efficiency and effectiveness in your use of resources, however unlike under the 2015 Audit Code, we will no longer report in the form of a conclusion on arrangements. Instead, where our work identifies significant weaknesses in arrangements, we are required to report those weaknesses to you, along with the actions that need to be taken to address those weaknesses.

Our work on value for money arrangements will focus on three criteria, specified in the revised Audit Code:

- Financial sustainability: how the body plans and manages its resources to ensure it can continue to deliver its services;
- Governance: how the body ensures that it makes informed decisions and properly manages its risks; and
- Improving economy, efficiency and effectiveness: how the body uses information about its costs and performance to improve the way it manages and delivers its services.

Under the new Audit Code we will be expected to report and make recommendations as soon as we identify a significant weakness in arrangements, as opposed to reporting our conclusion on arrangements at the end of the audit cycle as has previously been the case.

Reporting the results of the auditor's work

We currently issue you with an Annual Audit Letter which provides a summary of our work across all aspects of our audit. From 2020/21 the Annual Audit Letter will be replaced by the Auditor's Annual Report. This will continue to provide a summary of our work over the year of audit but will also include a detailed commentary on your arrangements in place to achieve economy, efficiency and effectiveness. This commentary replaces the conclusion on arrangements that was previously provided and will include details of any significant weakness identified and reported to you, follow up of any previous recommendations made, and the our view as to whether recommendations have been implemented satisfactorily.

The guidance supporting the new Audit Code is being developed by the National Audit Office and we will provide you with any further updates to our approach arising from this guidance when it is released.



6. FORWARD LOOK

Redmond Review

In September 2020, Sir Tony Redmond published the findings of his independent review into the oversight of local audit and the transparency of local authority financial reporting. The report makes several recommendations that, if implemented, could affect both the financial statements that local authorities are required to prepare and the work that we as auditors are required to do.

The report and recommendations are wide-ranging, and includes:

- the creation of the Office of Local Audit and Regulation (OLAR), be created to manage, oversee and regulate local audit;
- reviewing reporting deadlines;
- reviewing governance arrangements in local authorities, including the membership of the Audit Committee; and
- increasing transparency and reducing the complexity of local authority financial statements.

The recommendations and findings are being considered by the Ministry of Housing, Communities and Local Government and we look forward to working with all stakeholders to implement changes to ensure the development and sustainability of local audit.

The full report is available here: <https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-independent-review>



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