

# Annual Audit Letter

## Lincolnshire County Council

Year ending 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 Lincolnshire County Council (the Council) 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	Outcome	Summary
Audit of the financial statements	[Green]	<p>Our auditor's report issued on 30 April 2021 included our opinion that the financial statements:</p> <ul style="list-style-type: none"><li>• give a true and fair view of the Council's financial position as at 31 March 2020 and of its expenditure and income for the year then ended; and</li><li>• have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20</li></ul>
Other information published alongside the audited financial statements	[Green]	<p>Our auditor's report included our opinion that:</p> <ul style="list-style-type: none"><li>• the other information in the Statement of Accounts is consistent with the audited financial statements.</li></ul>
Value for money conclusion	[Green]	<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	[Green]	<p>In line with group audit instructions, issued by the NAO on 4<sup>th</sup> November, we reported to the group auditor in line with the requirements applicable to the Council's Whole of Government Accounts return on 30 April 2021.</p>
Statutory reporting	[Green]	<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 whether they give a true and fair view of the Council'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 National Audit Office and International Standards on Auditing. These require us to consider whether:

- the accounting policies are appropriate to the Council'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 financial position as at 31 March 2020 and of its financial performance for the year then ended.

Our auditor's report was modified to include an emphasis of matters paragraph. This drew attention to the financial statement disclosure explaining that COVID-19 had contributed to 'material valuation uncertainty' in the valuation of the Council's land and buildings and investment properties, and in the Council's share of Lincolnshire Pension Fund's property assets included in the estimated net Pension Liability.



## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our approach to materiality

We apply the concept of materiality when planning and performing our audit. 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. We set materiality for the financial statements as a whole (financial statement materiality) and set 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 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.	£22.8m
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	£0.7m
Specific materiality	We have applied a lower level of materiality to the following areas of the accounts: <ul style="list-style-type: none"><li>• Senior Officer Remuneration</li><li>• Members Allowances</li><li>• External Audit Fee</li></ul>	£5k £258k £17k



## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our response to significant audit risks

As part of our continuous planning procedures, we considered whether there were risks of material misstatement in the Council's financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Audit 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><b>Management override of controls</b></p> <p>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 testing over accounting estimates and financial journal entries and considering any significant transactions outside the normal course of business.</p>	<p>Our audit procedures did not identify any material errors or uncertainties in the financial statements, or other matters that we wish to bring to Members' attention.</p>
<p><b>Valuation of Land and Buildings and Investment Properties</b></p> <p>The Council's accounts contain material balances relating to its Land and Buildings and Investment Properties with the majority of these assets required to be carried at valuation.</p>	<p>We performed a range of audit tests, including, but not limited to:</p> <ul style="list-style-type: none"> <li>• Reviewing the valuer's qualifications, objectivity and independence to carry out the required programme of revaluations.</li> <li>• Testing a sample of valuations to ensure the correct methodology had been applied and were supported by appropriate evidence.</li> <li>• Considering the impact of assets not revalued in 2019/20 to ensure these remained materially correct at the balance sheet date.</li> <li>• engaging a valuation expert to specifically review the Council's original and updated valuation of the Energy from Waste (EFW) assets.</li> </ul>	<p>Our audit procedures did not identify any material errors or uncertainties in the financial statements. The updated EFW valuation report was received by the Council in March 2021. The difference in valuation (£6.674m) was not material and the draft financial statements were not adjusted.</p> <p>The Council's valuer declared that the valuation of the Council's property assets were subject to 'material valuation uncertainty' as a result of COVID-19 and this was disclosed in Note 3 of the financial statements and referred to in the 'emphasis of matter' paragraph in our audit report.</p> <p>A 'material valuation uncertainty' declaration does not mean that the valuation cannot be relied upon, only that, because of the extraordinary circumstances arising from COVID-19, less certainty can be attached to the valuation.</p>



## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our response to significant audit risks (continued)

Identified significant risk	Our response	Our findings and conclusions
<p><b>Valuation of the Net Pension Liability</b></p> <p>The Council's accounts contain material liabilities relating to the local government pension scheme. The Council uses an actuary to provide an annual valuation of these liabilities in line with the requirements of <i>International Accounting Standard 19 Employee Benefits</i>.</p>	<p>We performed a range of audit tests, including, but not limited to:</p> <ul style="list-style-type: none"> <li>• Liaising with the auditor of the Lincolnshire Pension Fund to obtain direct assurance over the controls surrounding membership, contributions and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements.</li> <li>• Reviewing the appropriateness of the Pension Asset and Liability valuation methodologies applied by the Pension Fund Actuary, and the key assumptions included within the valuation.</li> <li>• Considered the impact of the remedy solution for the McCloud legal judgement on the net pension liability.</li> </ul>	<p>'Material valuation uncertainty' was disclosed on the Pension Fund's property investment assets as a result of COVID-19. As the Council's share of those assets in the net Pension Liability in its own balance sheet is material, the Council has disclosed this in Note 3 of the financial statements and we have reflected this in the 'emphasis of matters' paragraph in our Audit Report.</p>
<p><b>Revenue Recognition</b></p> <p>Under <i>International Standards on Auditing 240</i>, there is a presumed risk that revenue may be misstated due to improper revenue recognition.</p>	<p>We evaluated the design and implementation of controls to mitigate the risk of material debtors being recognised in the wrong period. We tested debtors to ensure that they are supported by sufficient and appropriate evidence and were accounted for correctly.</p> <p>Our audit approach also incorporated a range of other substantive procedures, including, but not limited to the testing of receipts around the year-end to provide assurance that any material items of income had been recorded in the correct financial year</p>	<p>Our audit procedures in relation to this risk did not identify any material errors or uncertainties in the financial statements, or other matters that we wish to bring to your attention.</p>



## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our response to significant audit risks (continued)

Identified management judgement	Our response	Our findings and conclusions
<p><b>Expenditure Recognition</b></p> <p>Under <i>International Standards on Auditing 240</i>, there is similarly a presumed risk that material misstatement may occur due to improper expenditure recognition.</p>	<p>We evaluated the design and implementation of controls to mitigate the risk of material creditors being recognised in the wrong period. We tested creditors to ensure that they are supported by sufficient and appropriate evidence and were accounted for correctly.</p> <p>Our audit approach also incorporated a range of other substantive procedures, including, but not limited to the testing of payments around the year-end to provide assurance that any material items of expenditure had been recorded in the correct financial year</p>	<p>Our audit procedures in relation to this risk did not identify any material errors or uncertainties in the financial statements, or other matters that we wish to bring to your attention.</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. The matters we report are limited to those deficiencies and other control recommendations that we have identified during our normal audit procedures and that we consider to be of sufficient importance to merit being reported.

We reported a small number of minor control deficiencies in our Audit Completion Report presented to the Audit Committee in November 2020 and there are none that we need to highlight in this report.



### 3. VALUE FOR MONEY CONCLUSION

Value for money conclusion

Unqualified

#### 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.

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.

When we perform our work, we consider whether there are any areas requiring additional audit attention as a “Significant Audit Risk”, which we report to the Audit Committee prior to finalising our conclusion. As set out in our Audit Strategy Memorandum we identified no significant audit risks. We did though identify the Council’s medium term financial sustainability as a matter which we needed to keep under close review during our audit. Before drawing our conclusion we, amongst other things:

- Reviewed the 2019/20 financial performance and forecasts during the year and considered the Council’s financial outturn position as presented in the financial statements.
- Reviewed the 2020/21 Revenue and Capital budgets and Medium Term Financial Plan, Treasury Management Strategy, incorporating the Minimum Revenue Provision Policy and Capital and Investment Strategies
- Considered the Council’s latest financial monitoring information and its updated medium term outlook.

From the work performed, no new significant VFM risks were identified.

In April 2020 NAO issued an update to its VFM guidance to auditors which set out how local auditors should approach considering the impact of COVID-19 on their 2019/20 VFM arrangements conclusion risk assessment. We did not identify in considering this guidance any significant failures in the Council’s arrangements during 2019/20 and are satisfied that no additional significant VFM risks have been identified in relation to these matters.

#### Overall Conclusion

Our auditor’s report stated that 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 31<sup>st</sup> March 2020.



## 4. OTHER REPORTING RESPONSIBILITIES

Exercise of statutory reporting powers	<b>No matters to report</b>
Completion of group audit reporting requirements	<b>No matters to report</b>
Other information published alongside the audited financial statements	<b>Consistent</b>

The 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 National Audit Office, as group auditor, requires us to complete a Whole of Government Accounts Assurance Statement in respect of financial consolidation data produced by the Council. We have completed the work required for this assurance return and submitted the information requested to the NAO on 30 April 2021.

### 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 Council's auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum in June 2020. Having completed our work for the 2019/20 financial year, we can confirm that our final proposed fees are as follows. These fees are subject to agreement with management and approval by PSAA:

Area of work	2019/20 proposed fee	2019/20 Final fee
Scale fee for delivery of audit work under the NAO Code of Audit Practice	£82,630	£82,640
Fee Variations*		
Scope changes caused by increased audit quality expectations:		£12,273
<ul style="list-style-type: none"> <li>• Additional Testing on Property, Plant &amp; Equipment and Defined Benefit Pensions Schemes</li> <li>• Additional Costs associated with being a 'Major Local Audit' and requiring additional level of audit procedures and quality control</li> </ul>		
Scope changes caused by Covid-19:		£4,899
<ul style="list-style-type: none"> <li>• Impact of 'Material Valuation Uncertainty' in Council's Property Assets and its share of Pension Fund Assets</li> <li>• Updating audit risk assessments, including the value for money conclusion</li> <li>• Additional considerations of estimation uncertainty and the Going Concern assertion</li> </ul>		
One-off matters for 2019/20:		£2,122
<ul style="list-style-type: none"> <li>• Changes impacting pension liabilities through McCloud and Goodwin</li> <li>• Additional testing on the valuation of the Energy from Waste assets, including engaging an auditor's valuation expert.</li> </ul>		
<b>Final audit fee</b>	<b>£82,630</b>	<b>£101,934</b>
Assurance related services		
<ul style="list-style-type: none"> <li>• Assurance on the 2019/20 Teachers Pensions Return</li> <li>• Assurance on the subcontracting arrangements for the Education and Skills Funding Agency</li> </ul>		£5,700 £5,250

\*Fee variations subject to confirmation from PSAA.

### Fees for other work

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



## 6. FORWARD LOOK: AUDIT CHANGES 2020/21

### 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 1<sup>st</sup> April 2020 a new Code came in to force and applies 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 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 our view as to whether recommendations have been implemented satisfactorily.

The new Audit Code will result in additional officer time and auditor time and therefore audit fees.



## 6. FORWARD LOOK: AUDIT CHANGES 2020/21

### 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 made 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 recommendations and findings have been considered by the Ministry of Housing, Communities and Local Government (MHCLG) and we look forward to working with all stakeholders to implement the agreed changes. The main agreed outcomes are:

- a recognition by MCHLG that audit fees are not sufficient to meet the work required, with £15m additional central funding support to be provided in 2021/22.
- Confirmation by MCHLG that the date for publication of audited accounts will be 30th September for the 2020/21 and 2021/22 financial years, with a commitment to review whether it is realistic to return to a 31st July date in future years.

MHCLG has also proposed that a new audited 'standardised statement of service information and costs' is produced by Local Government bodies to help simplify financial reporting. CIPFA has been asked to work on this for introduction in 2021/22.



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