

The Annual Audit Letter for London Borough of Croydon

Year ended 31 March 2017

October 2017

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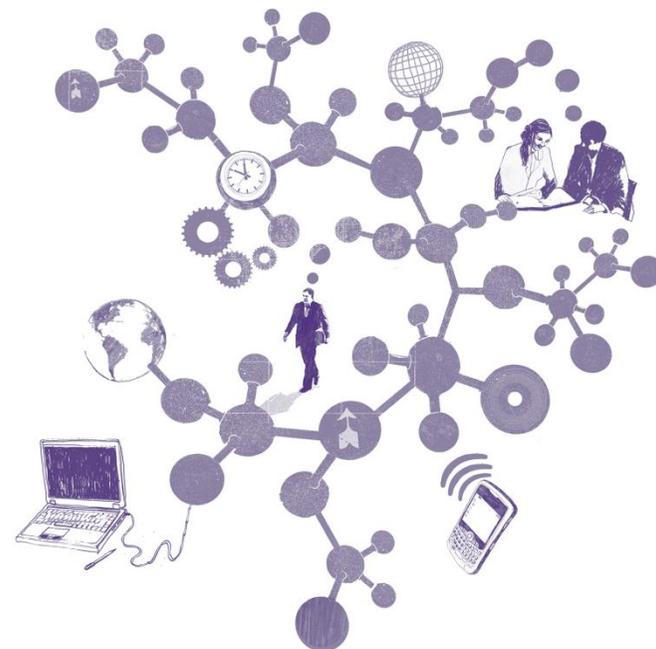
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Executive summary

Purpose of this letter

Our Annual Audit Letter (Letter) summarises the key findings arising from the work we have carried out at London Borough of Croydon ('you' or 'the Council') for the year ended 31 March 2017.

This Letter provides a commentary on the results of our work to you and your external stakeholders, and highlights issues we wish to draw to the attention of the public. In preparing this letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice (the Code) and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'.

We reported the detailed findings from our audit work to your General Purposes and Audit Committee (as those charged with governance) in our Audit Findings Report on 20 September.

Our responsibilities

We have carried out our audit in accordance with the NAO's Code of Audit Practice, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

- give an opinion on your financial statements, including the pension fund (section two)
- assess your arrangements for securing economy, efficiency and effectiveness in your use of resources (the value for money conclusion) (section three).

In our audit of your financial statements, we comply with International Standards on Auditing (UK and Ireland) (ISAs) and other guidance issued by the NAO.

Our work

Financial statements opinion

We gave an unqualified opinion on your financial statements on 29 September 2017. The quality of your financial statements was good as in previous years. We did not identify any errors affecting your overall financial position. On the same day we also issued an unqualified opinion on your pension fund accounts.

Value for money conclusion

We were satisfied that you put in place proper arrangements to ensure economy, efficiency and effectiveness in your use of resources during the year ended 31 March 2017, except for the issue noted below.

On 4 September 2017, Ofsted published a report on their findings from their inspection of your services for children in need of help and protection, children looked after and care leavers, and their review of the effectiveness of the Local Safeguarding Children Board. Ofsted rated your children's services as "inadequate". The report highlighted that there has been a significant deterioration in the quality of service provision in relation to children's services since the previous inspection in 2012. Ofsted highlighted that there was weak management oversight of social care practice and that the failings identified left some children at risk of severe harm.

In response to the outcome of the Ofsted inspection, you have issued a Transitional Action Plan setting out key actions to be taken over the three months following the inspection.

As a result of the above matter, we therefore qualified our value for money conclusion in our audit opinion on 29 September 2017.

This qualification relates only to the issues noted within the September 2017 Ofsted report on children's services. In all other respects we are satisfied that you have demonstrated that you have in place appropriate arrangements for securing economy, efficiency and effectiveness.

We have reviewed your budget position and medium term financial planning and note that you have forecast the attainment of a balanced budget over the period to 2019/20. We are satisfied that this is based upon reasonable assumptions but note that, in common with other local authorities nationally, you face challenging savings requirements over the next few years as a result of increasing demand pressures, incurred at a time of reductions in central government funding for local government.

Whole of government accounts

We completed our work on your consolidation return following guidance issued by the NAO and we issued an unqualified assurance statement on 29 September 2017.

Use of additional powers and duties

We are required under the Act to give electors the opportunity to raise questions about your accounts and we consider and decide upon objections received in relation to the accounts.

We received an objection relating to your Private Finance Initiative (PFI) programme of street lighting. We are considering the matters laid out in this objection and your response to these matters.

Certificate

We are unable to certify that we have completed the audit of your accounts until we have completed our work in respect of the objection we received.

Certification of grants

We also carry out work to certify your Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. Our work on this claim is not yet complete and will be finalised by 30 November 2017. We will report the results of this work to the General Purposes and Audit Committee on a subsequent date.

Other work completed

During 2016/17 we carried out a number of other services for you.

- We carried out the audit of your subsidiary housing company, Brick by Brick Croydon Limited.
- Members of your finance team attended our financial resilience capacity building programme.
- You subscribed to our CFO Insights service, which provides you with detailed performance information and benchmarking data with other councils.

Working with you

From 2017/18, the statutory deadlines for the preparation and audit of the financial statements will be brought forward. You will be required to produce draft statements by 31 May and secure an audit opinion by 31 July 2018.

Moving towards an earlier deadline, particularly within the more complex environment within which you now operate, will require an element of redesign of some of your closedown processes, arrangements and internal business processes. We have worked with many large clients to successfully implement faster close and will continue to work with you during the coming year to support you in identifying opportunities for efficiencies in the financial reporting processes and to help improve controls around closedown in preparation for the earlier timetable.

We would like to record our appreciation for the assistance and co-operation provided to us during our audit.

Audit of the accounts

Our audit approach

Materiality

In our audit of your accounts, we applied the concept of materiality to determine the nature, timing and extent of our work, and to evaluate the results of our work. We define materiality as the size of the misstatement in the financial statements that would lead a reasonably knowledgeable person to change or influence their economic decisions.

We determined materiality for our audit of your accounts to be £22.3 million, which is 1.95% of your gross revenue expenditure. We used this benchmark as, in our view, users of your accounts are most interested in how you have spent the income raised from taxation and grants during the year. We did not identify any areas of the accounts where a separate materiality would apply.

We set a lower threshold, of £1 million, above which we reported errors to the General Purposes and Audit Committee in our Audit Findings Report.

Pension Fund

For the audit of the Croydon Pension Fund accounts, we determined materiality to be £10.9 million, which is 1% of the Fund's net assets. We used this benchmark as, in our view, users of the Pension Fund accounts are most interested in the value of assets available to fund pension benefits.

We set a lower level of specific materiality of £547,000 for management expenses. We set the same threshold, of £547,000, as the level above which we reported errors to the General Purposes and Audit Committee.

The scope of our audit

Our audit involves obtaining enough evidence about the amounts and disclosures in the financial statements to give reasonable assurance they are free from material misstatement, whether caused by fraud or error. This includes assessing whether:

- Your accounting policies are appropriate, have been consistently applied and adequately disclosed;
- significant accounting estimates made by the Executive Director of Resources are reasonable; and
- the overall presentation of the financial statements gives a true and fair view.

We also read the narrative report and annual governance statement to check they are consistent with our understanding of you and with the accounts included in the Statement of Accounts on which we gave our opinion.

We carry out our audit in line with ISAs (UK and Ireland) and the NAO Code of Audit Practice. We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach was based on a thorough understanding of your business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks and the results of this work.

Audit of the accounts – Council

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Valuation of property, plant and equipment</p> <p>You revalue your land and building assets on a rolling basis over a five year period. The Code requires that councils ensure that the carrying value at the balance sheet date is not materially different from the current value. This represents a significant estimate by management in the financial statements.</p>	<p>We completed the following work in respect of this risk.</p> <ul style="list-style-type: none"> • We reviewed the competence, expertise and objectivity of management experts used. • We tested revaluations made during the year to ensure they were consistent with underlying valuer information and were input correctly into your asset register. • We reviewed your processes and assumptions for the calculation of the estimate. • We reviewed the instructions issued to valuation experts and the scope of their work. • We discussed with the valuer the basis on which the valuation is carried out and we challenged the key assumptions. • We evaluated the assumptions made by management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value. 	<p>Our audit did not identify any significant issues in relation to the valuation of Property, Plant and Equipment</p>
<p>First year accounting and consolidation of Brick by Brick Croydon Ltd</p> <p>This is the first year that you have prepared consolidated accounts to include Brick by Brick, and it is expected to be a material subsidiary undertaking. There is the risk of inappropriate accounting treatment.</p>	<p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> • We reviewed the outputs from the statutory audit of Brick by Brick performed by Grant Thornton in respect of the year ended 31 December 2016. • We reviewed accounting estimates, judgments and decisions made by management during the preparation of the financial statements. • We reviewed unusual significant transactions. • We reviewed your accounts disclosures compared with Code requirements. 	<p>Our audit did not identify any significant issues in relation to the risk identified</p>

Audit of the accounts – Pension Fund

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work on the audit of the pension fund.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Valuation of level 3 investments Significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.</p>	<p>We undertook the following work in relation to this risk.</p> <ul style="list-style-type: none"> • We updated our understanding of the processes and control in place to estimate the valuation of these assets. • For a sample of investments we tested valuations by obtaining and reviewing the audited accounts at latest date for individual investments and agreeing these to fund manager reports at that date. Reconciliation of those values to the values at 31st March with reference to known movements in the intervening period. • We reviewed the nature and basis of estimated values and consider what assurance management has over the year end valuation provided for these type of investments. • We reviewed the competence, expertise and objectivity of management experts used. • We reviewed the qualifications of the fund managers as experts to value the level 3 investments at year end and gain an understanding of how the valuation of these investments has been reached. 	<p>Our audit testing of the figures in the accounts identified that infrastructure and private equity investments were understated in the financial statements by £9,155k. This is due to the audited final valuation data not being available at the time of compiling the draft financial statements This is purely a timing issue for the finance team receiving the information.</p> <p>No other significant issues were identified in our work.</p>

Audit of the accounts

Audit opinion

We gave an unqualified opinion on your accounts on 29 September 2017, in advance of the 30 September 2017 national deadline.

You originally intended to deliver draft accounts and working papers to us by the end of May 2017, in line with the forthcoming earlier close timetables, but were not able to achieve this. Your draft financial statements for the year ended 31 March 2017 were approved and issued for audit on 20 June 2017, and working papers were provided shortly after this. The absence of a successful 'trial run' increases the risk of missing the earlier statutory deadlines next year.

The challenge you face is to reduce the time taken to close the accounts by almost a third, without any reduction or deterioration in the quality and accuracy of the draft accounts submitted for audit. Achieving this may require fundamental change in some of your internal processes for preparing the accounts and supporting the audit process. You should consider the mitigating steps that can be taken to release capacity into the finance team, reduce potential bottlenecks, and reduce the time taken to facilitate the audit and respond to queries.

It will be vital to the success of achieving early close to ensure that all officers involved in the process for preparation are aware of their responsibilities for supporting the earlier closure of the audit. Capacity of the finance team to respond to the audit on top of their existing, significant, workload remains an issue, and will be compounded during a more intense early close audit cycle. Achieving such a significant earlier signoff of the audit is not something that can be achieved by the finance team alone and will require full engagement from the wider organisation.

Issues arising from the audit of the accounts

We reported the key issues from our audit of your accounts to the General Purposes and Audit Committee on 20 September 2017.

The draft financial statements and supporting working papers were prepared to a good standard of quality as in previous years, with few issues arising during the audit process. The volume of error in the accounts was reduced compared to previous years, demonstrating improvements in the accuracy and quality of the accounts submitted for audit.

We did not identify any errors affecting your overall financial position. We identified one material adjustment, being a reclassification of borrowing between long term and short term on the balance sheet. We also identified a small number of disclosure amendments and improvements to the presentation of the accounts.

Pension fund accounts

We also reported the key issues from our audit of accounts of the Pension Fund hosted by the Council to the General Purposes and Audit Committee on 20 September 2017.

The Pension Fund accounts were also prepared to a high standard. There was one adjustment required of £9.1 million, affecting the Fund's reported financial position. This was an understatement of infrastructure and private equity investments, which officers made us aware of before submitting the draft financial statements for audit. The level 3 investment year end final valuation figures were not made available to officers until after the draft financial statements were completed. For 2018 officers expect to receive the valuation information by the end of June and do not envisage this being a problem for the early opinion deadline of 31 July 2018. Officers will continue to liaise with the fund managers to ensure information is received in line with the earlier deadlines.

We have also recommended a small number of adjustments to improve the presentation of the financial statements.

Audit of the accounts

Annual Governance Statement and Narrative Report

We are required to review your Annual Governance Statement and Narrative Report. You published these documents on your website with the draft accounts in line with the national deadlines.

Both documents were prepared in line with the relevant guidance and were consistent with the supporting evidence provided. Following the publication of the Ofsted report into children's services you updated your Annual Governance Statement to highlight the steps you are taking to address governance failings in this service area.

Whole of Government Accounts (WGA)

We carried out work on your consolidation schedule in line with instructions provided by the NAO . We issued a group assurance certificate which did not identify any issues for the group auditor to consider on 29 September 2017.

Other statutory duties

We also have additional powers and duties under the Act, including powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about your accounts and to raise objections received in relation to the accounts.

You advertised the statutory inspection period for your accounts as required by the Act. We received one objection to the accounts during the statutory inspection period. The objection relates to your PFI scheme for street lighting in the Borough.

We concluded that the objection was not material to the financial statements and did not prevent us from issuing an unqualified opinion. We have discussed the objection with management and we are considering management's responses to the matters raised.

We are currently unable to certify that we have completed the audit of your accounts until we have completed our work in respect of the objection.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice (the Code), following the guidance issued by the NAO in November 2016 which specified the criterion for auditors to evaluate:

In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.

Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the key risks where we concentrated our work. We continued our review and risk assessment up to the date of giving our report. We identified a further significant risk against which we carried out further work, relating to the Ofsted inspection of children's services.

The key risks we identified and the work we performed are set out in table 2 below and overleaf.

Table 2: Value for money risks

Risk identified	Work carried out	Findings and conclusions
Budget position and medium term financial planning	We reviewed your arrangements in setting and controlling the budget position.	For 2016/17 your outturn position was a £0.05 million underspend. This consisted of a significant departmental overspend of £10.4 million (largely in demand led services), offset by non-departmental underspends. It is not certain that non-departmental underspends will continue, so vigilance over future positions is critical. Failure to deliver departmental budgets could have a significant impact on your financial health.
	We reviewed your processes to control and challenge budget overspends where they materialise.	
	We reviewed the adequacy of your underlying budget assumptions and your plans to address the budget gaps to 2019/20.	
		For 2017/18, you have set a balanced budget, with generally robust underlying assumptions. In doing so you have increased Croydon's share of council tax by 4.99 per cent.

continued.....

Overall VfM conclusion

In seeking to satisfy ourselves that you have made proper arrangements for securing economy, efficiency and effectiveness in your use of resources, we have considered reports issued by regulators. During the year of audit, in September 2017 a report on the inspection of services for children in need of help and protection, looked after children and care leavers, and review of effectiveness of the Local Safeguarding Children Board concluded that, overall, children's services in the London Borough of Croydon were inadequate.

Based on the work we performed to address the significant risks, we concluded that with the exception of the matter set out above in relation to arrangements for management of children's services, we are satisfied that in all significant respects you have put in place proper arrangements to secure economy, efficiency and effectiveness in your use of resources for the year ended 31 March 2017.

Value for Money

Table 2: Value for money risks

Risk identified	Work carried out	Findings and conclusions
<p>Budget position and medium term financial planning</p> <p>.....(continued)</p>		<p>As service pressures are expected to grow, substantial efficiency and transformation savings will continue to be required across the organisation.</p> <p>Medium term financial plans show that your budget is balanced for three years, which is an impressive achievement. The budget incorporates assumptions around growth in the council tax base.</p> <p>Vigilance over the position and risks is still required to address future uncertainties. Longer term growth assumptions are lower than that experienced to date, so the forecast may need to be revised should growth exceed expectations.</p>
<p>Health and Social Care Integration</p>	<p>We reviewed your progress to date in implementing the planned integration and considered your arrangements to monitor and manage risks and ensure benefits from the project are realised.</p>	<p>Both health and social care face enormous pressure and greater integration is needed to relieve financial pressures and deliver a more effective service. The position in Croydon is particularly challenging.</p> <p>You are working with the NHS and other providers through the STP and the Outcomes Based Commissioning model to foster greater integration and improve outcomes. Plans are in early stages, however, arrangements appear reasonable. There are a number of risks that you have identified and are appropriately monitoring, which will be critical to ensuring future success.</p>
<p>Ofsted inspection of children's services</p>	<p>We reviewed the report of Ofsted and considered the response of the Council to the report.</p>	<p>On 4 September 2017, Ofsted published a report on their findings from inspection of your services for children in need of help and protection, children looked after and care leavers and review of the effectiveness of the Local Safeguarding Children Board that rated you as "inadequate". We issued a qualified Value for Money conclusion as a result of the issues set out within the report.</p> <p>In response to the outcome of the Ofsted inspection, you have issued a Transitional Action Plan setting out key actions to be taken over the three months following the inspection to improve child safety and the quality of service provided. A formal Improvement Plan is currently being developed for submission to Ofsted in December 2017.</p>

Appendix A: Reports issued and fees

We confirm below our final fees charged for the audit and provision of non-audit services.

Fees

	Proposed fee £	Actual fees £	2015/16 fees £
Statutory audit of Council	172,860	TBC***	172,860
Statutory audit of Pension Fund	21,000	21,000	21,000
Audit of subsidiary company Brick by Brick Croydon Limited	30,000	TBC *	N/A
Housing Benefit Grant Certification	25,755	TBC **	24,894
Total fees (excluding VAT)	249,615	TBC	218,754

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA).

* The audit of Brick By Brick Croydon Ltd is now complete and the final fee will be discussed with management.

** This work is on-going and the final fee will be determined once this work has been concluded.

***We are unable to determine the final fee until we have concluded our work on the objections to the accounts raised during the statutory inspection period.

Reports issued

Report	Date issued
Audit Plans	March 2017
Audit Findings Reports	September 2017
Annual Audit Letter	October 2017

Fees for other services

Service	Fees £
Audit related services:	
• none	none
Non-audit services:	
• Subscription to CFO Insights	10,000
• Finance capacity building	3,500

Independence and ethics

- Ethical Standards and ISA (UK&I) 260 require us to give you timely disclosure of matters relating to our independence.
- We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and confirm that we are independent and are able to express an objective opinion on the financial statements.
- We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard
- We have received confirmation that the external experts whose work we have relied upon during the course of our audit, PricewaterhouseCoopers LLP and Gerald Eve LLP, are independent
- For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The table below summarises all other services which were identified:

Non- audit services

- We have considered whether other services might be perceived as a threat to our independence as your auditor and have ensured that appropriate safeguards are put in place, as reported overleaf.

Reports issued and fees (continued)

We have considered whether other services might be perceived as a threat to our independence as the group's auditor and have ensured that appropriate safeguards are put in place

	Service provided to	Fees £	Threat?	Safeguard
Non-audit services				
<p><u>Financial resilience capacity building programme</u></p> <p>A series of workshops were held to help finance officers to develop by learning new leadership skills, listening to guest speakers and networking with their peers.</p>	London Borough of Croydon	3,500	<ul style="list-style-type: none"> No threats noted 	The facilitators for the programme were separate to the audit team. The work was structured so as not to make any recommendations in relation to strategic decision making or partnership working or on the deployment of resources.
<p><u>CFO Insights subscription</u></p> <p>CFO Insights is an online software service offering that enables users to rapidly analyse, segment and visualise all the key data relating to the financial performance of a local authority.</p>	London Borough of Croydon	10,000	<ul style="list-style-type: none"> Self interest threat 	<p>The fee is a recurrent subscription and thus gives high self-interest threat. However, the fee for this work is negligible in comparison to the total fee for the audit and in particular Grant Thornton UK LLP's turnover overall. It is also a fixed fee with no contingent element. We consider that these factors all mitigate the perceived self-interest threat to an acceptable level.</p> <p>CFO Insights does not provide any advice; the tool provides only information and insight that to help inform decision making by officers. It is the responsibility of your officers who use this service to undertake informed interpretation of the information provided. The team that operates this service is separate to the audit team.</p>
	TOTAL	13,500		

- The above non-audit services are consistent with the Council's policy on the allotment of non-audit work to your auditor.
- None of the above services were provided on a contingent fee basis.
- For the purposes of our audit we have made enquiries of all Grant Thornton teams within the Grant Thornton International Limited network member firms providing services to the London Borough of Croydon The table summarises all non-audit services which were identified.
- The fees set out above agree to those reported in Note 29 'External Audit Costs' in the financial statements.



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