



# The Interim Audit Findings for Herefordshire Council

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Year ended 31 March 2020

26 January 2021



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The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed for the purpose of expressing our opinion on the financial statements. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose all defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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# Headlines

This table summarises the key findings and other matters arising from the statutory audit of Herefordshire Council ('the Council') and the preparation of the group and Council's financial statements for the year ended 31 March 2020 for those charged with governance.

## Covid-19

The outbreak of the Covid-19 coronavirus pandemic has had a significant impact on the normal operations of the Council and group, including the delivery of front-line activities to the vulnerable, administration of grants to businesses and the closure of community facilities. These operation challenges have been coupled with uncertainty over future funding for the Council due to a loss of core income streams as well as additional costs introduced in delivering services in line with emerging government guidance.

The Finance team have also faced significant challenges in continuing their day to day operations, including remote access to systems and providing support to other service areas to prioritise support for the vulnerable and local businesses.

Authorities are still required to prepare financial statements in accordance with the relevant accounting standards and the CIPFA Code of Practice, albeit to an extended deadline for the preparation of the financial statements up to 31 August 2020 and the date for audited financial statements to 30 November 2020.

We updated our audit risk assessment to consider the impact of the pandemic on our audit and issued an audit plan addendum on 4 May 2020. In that addendum we reported an additional financial statement risk in respect of Covid -19 and highlighted the impact on our VfM approach. Further detail is set out on page 6.

Restrictions for non-essential travel has meant both Council and audit staff have had to develop new remote access working arrangements, including remote accessing financial systems, video calling and alternative procedures over the verification of completeness and accuracy of information produced by the entity. These have proved to allow the audit to progress but, somewhat inevitably, have extended the amount of time required for the audit.

# Headlines

This table summarises the key findings and other matters arising from the statutory audit of Herefordshire Council ('the Council') and the preparation of the group and Council's financial statements for the year ended 31 March 2020 for those charged with governance.

<b>Financial Statements</b>	<p>Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the group and Council's financial statements:</p> <ul style="list-style-type: none"> <li>• give a true and fair view of the financial position of the group and Council and the group and Council's income and expenditure for the year; and</li> <li>• have been properly prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014.</li> </ul> <p>We are also required to report whether other information published together with the audited financial statements (including the Annual Governance Statement (AGS) and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</p>	<p>Our audit work was completed remotely during July-January . Our findings are summarised on pages 5 to 15. We have identified disclose only adjustments to the financial statements. Audit adjustments are detailed in Appendix C. We have also raised recommendations for management as a result of our audit work in Appendix A. Our follow up of recommendations from the prior year's audit are detailed in Appendix B.</p> <p>Our work is substantially complete and there are no matters of which we are aware that would require material changes to the financial statements, subject to the following outstanding matters;</p> <ul style="list-style-type: none"> <li>• Going concern – receipt of extended cashflow forecast to support going concern</li> <li>• Pension liabilities – finalisation of our work</li> <li>• Covid-19 grant treatment – discussions on-going re grant treatment</li> <li>• PFI – agreement of payments disclosure</li> <li>• Expenditure and Funding Analysis – agreement to outturn</li> <li>• MRP – finalisation of treatment</li> <li>• Litigation and claims – review up to opinion sign off</li> <li>• Value for money – receipt of Council's final report</li> <li>• PBSE – consideration of events since balance sheet date</li> <li>• WGA</li> <li>• Final quality review</li> <li>• receipt of management representation letter; and</li> <li>• review of the final set of financial statements.</li> </ul> <p>We have concluded that the other information to be published with the financial statements is consistent with our knowledge of your organisation.</p>
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Our anticipated audit report opinion will be provided in the final Audit Findings Report.

## Headlines

# Headlines

This table summarises the key findings and other matters arising from the statutory audit of Herefordshire Council ('the Council') and the preparation of the group and Council's financial statements for the year ended 31 March 2020 for those charged with governance.

<b>Value for Money arrangements</b>	Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report if, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('the value for money (VFM) conclusion').	Our work in this area is currently on-going.
<b>Statutory duties</b>	<p>The Local Audit and Accountability Act 2014 ('the Act') also requires us to:</p> <ul style="list-style-type: none"> <li>• report to you if we have applied any of the additional powers and duties ascribed to us under the Act; and</li> <li>• To certify the closure of the audit.</li> </ul>	<p>We have not exercised any of our additional statutory powers or duties.</p> <p>We have completed the majority of work under the Code but are unable to issue our completion certificate until one particular confidential issue, arising from previous years has been brought to its conclusion. In addition, our value for money work is still on-going.</p>

## Acknowledgements

We would like to take this opportunity to record our appreciation for the assistance and timely collaboration provided by the finance team and other staff during these unprecedented times.

# Audit approach

## Overview of the scope of our audit

This Audit Findings Report presents the observations arising from the audit that are significant to the responsibility of those charged with governance to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Its contents have been discussed with management and will be discussed at Audit Committee.

As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK) and the Code, which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

## Audit approach

Our audit approach was based on a thorough understanding of the group's business and is risk based, and in particular included:

- An evaluation of the group's internal controls environment, including its IT systems and controls;
- An evaluation of the components of the group based on a measure of materiality considering each as a percentage of the group's expenditure to assess the significance of the component and to determine the planned audit response. From this evaluation we determined that a targeted approach was required for Hoople; and
- Substantive testing on significant transactions and material account balances, including the procedures outlined in this report in relation to the key audit risks

## Audit approach (continued)

We have had to alter our audit plan, as communicated to you on 4 May 2020, to reflect our response to the Covid-19 pandemic.

## Conclusion

We have substantially completed our audit of your financial statements and our anticipated audit report opinion will be provided in the final Audit Findings Report.

## Our approach to materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

Materiality levels remain the same as reported in our audit plan.

	Group Amount (£)	Council Amount (£)	Qualitative factors considered
Materiality for the financial statements	£6.71m	£6.7m	Materiality has been based on 1.8% of the Group and Authority's gross expenditure
Performance materiality	£4.7m	£4.7m	Our performance materiality has been set at 70% of our overall materiality.
Trivial matters	£0.3m	£0.3m	This is set a 5% of financial statements materiality and reflects a level below which stakeholders are unlikely to be concerned by uncertainties.

# Significant audit risks

## Risks identified in our Audit Plan

### Covid- 19

The global outbreak of the Covid-19 virus pandemic has led to unprecedented uncertainty for all organisations, requiring urgent business continuity arrangements to be implemented. We expect current circumstances will have an impact on the production and audit of the financial statements for the year ended 31 March 2020, including and not limited to;

- Remote working arrangements and redeployment of staff to critical front line duties may impact on the quality and timing of the production of the financial statements, and the evidence we can obtain through physical observation
- Volatility of financial and property markets will increase the uncertainty of assumptions applied by management to asset valuation and receivable recovery estimates, and the reliability of evidence we can obtain to corroborate management estimates
- Financial uncertainty will require management to reconsider financial forecasts supporting their going concern assessment and whether material uncertainties for a period of at least 12 months from the anticipated date of approval of the audited financial statements have arisen; and
- Disclosures within the financial statements will require significant revision to reflect the unprecedented situation and its impact on the preparation of the financial statements as at 31 March 2020 in accordance with IAS1, particularly in relation to material uncertainties.

We therefore identified the global outbreak of the Covid-19 virus as a significant risk, which was one of the most significant assessed risks of material misstatement.

### The revenue cycle includes fraudulent transactions

Under ISA240 (UK) there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.

## Auditor commentary

We:

- worked with management to understand the implications the response to the Covid-19 pandemic had on the organisation's ability to prepare the financial statements and update financial forecasts and assessed the implications for our materiality calculations. No changes were made to materiality levels previously reported. The draft financial statements were provided on 26 June 2020;
- liaised with other audit suppliers, regulators and government departments to co-ordinate practical cross-sector responses to issues as and when they arose. Examples include the material uncertainty disclosed by the Council's property valuation expert
- evaluated the adequacy of the disclosures in the financial statements that arose in light of the Covid-19 pandemic;
- evaluated whether sufficient audit evidence could be obtained through remote technology;
- evaluated whether sufficient audit evidence could be obtained to corroborate significant management estimates such as assets and the pension fund liability valuations ;
- evaluated management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment;
- discussed with management the implications for our audit report where we have been unable to obtain sufficient audit evidence.

This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.

We rebutted the risk at the planning stage of our audit. Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Authority, we determined that the risk of fraud arising from revenue recognition could be rebutted, because:

- there is little incentive to manipulate revenue recognition
- opportunities to manipulate revenue recognition are very limited
- the culture and ethical frameworks of local authorities, including Herefordshire Council, mean that all forms of fraud are seen as unacceptable

No circumstances arose that indicated we needed to reconsider this judgement.

# Significant audit risks

## Risks identified in our Audit Plan

### Management override of controls

Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities. The Authority faces external scrutiny of its spending and this could potentially place management under undue pressure in terms of how they report performance.

We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk, which was one of the most significant assessed risks of material misstatement.

## Auditor commentary

We:

- evaluated the design effectiveness of management controls over journals;
- analysed the journals listing and determine the criteria for selecting high risk unusual journals;
- tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration;
- gained an understanding of the accounting estimates and critical judgements applied made by management and consider their reasonableness with regard to corroborative evidence; and
- evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions.

Our work on journals, has identified that no there is no authorisation process in place over the journals posted. The systems put in place by the Council do restrict who can post journals, but there is no authorisation once these are posted. See action plan at appendix A for recommendation. This recommendation was also raised in the prior year.

### Valuation of property, plant and equipment

The Authority revalues its land and buildings on a rolling five-yearly basis. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved and the sensitivity of this estimate to changes in key assumptions.

Additionally, management will need to ensure the carrying value in the Authority and group financial statements is not materially different from the current value or the fair value (for surplus assets) at the financial statements date, where a rolling programme is used.

We therefore identified valuation of land and buildings, particularly revaluations and impairments, as a significant risk.

We:

- evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work;
- evaluated the competence, capabilities and objectivity of the valuation expert;
- wrote to the valuer to confirm the basis on which the valuation was carried out;
- challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding;
- we challenged management about their treatment of the waste plant;
- tested revaluations made during the year to see if they had been input correctly into the group's asset register; and
- 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.

No issues were identified from our audit work on the valuation of land and buildings.

We will be including an Emphasis of Matter paragraph into our audit opinion to draw the readers attention to the disclosures made around the estimation uncertainty in the valuation.



# Significant audit risks

## Risks identified in our Audit Plan

## Auditor commentary

### Valuation of pension fund net liability

The Council's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements and group accounts.

The pension fund net liability is considered a significant estimate due to the size of the numbers involved and the sensitivity of the estimate to changes in key assumptions.

We therefore identified valuation of the Council's pension fund net liability as a significant risk.

The Council is a statutory member of the Hereford and Worcestershire Local Government Pension Scheme administered by Worcestershire County Council. Herefordshire Council remain responsible for the accuracy of disclosures within the accounts and this will include having a clear understanding of key assumptions within the estimate.

We:

- updated our understanding of the processes and controls put in place by management to ensure that the Council's pension fund net liability is not materially misstated and evaluate the design of the associated controls;
- evaluated the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work;
- assessed the competence, capabilities and objectivity of the actuary who carried out the Authority's pension fund valuation;
- assessed the accuracy and completeness of the information provided by the Authority to the actuary to estimate the liability;
- tested the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary;
- undertook procedures to confirm the reasonableness of the actuarial assumptions, including the experience item, made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report;
- reviewed the McCloud position;
- challenged the Actuary on the experience item figures included in the IAS19 report;
- agreed the advance payment made to the pension fund during the year to the expected accounting treatment and relevant financial disclosures; and
- obtained assurances from the auditor of the Pension Fund as to the controls surrounding the validity and accuracy of membership data; contributions data and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements.

No issues have been identified from our audit work on the valuation of pension fund net liability to date. Our work is not yet complete in this area. We will be including an Emphasis of Matter paragraph into our audit opinion to draw the readers attention to the disclosures made around the estimation uncertainty in the valuation.

# Other audit risks

## Risks identified in our Audit Plan

### Employee remuneration

Payroll expenditure represents a significant percentage of the Council's operating expenses.

As the payroll expenditure comes from a significant number of individual transactions throughout the year, including transactions involving new-starters, grade changes and leavers, there is a risk that payroll expenditure in the accounts could be understated. We therefore identified occurrence of payroll expenses as a risk requiring particular audit attention.

## Auditor commentary

We have undertaken the following work in relation to this risk:

- evaluated the Council's accounting policy for recognition of payroll expenditure for appropriateness;
- documented our understanding of processes and key controls;
- undertaken walkthrough of key controls to assess whether those controls were in line with our documented understanding;
- obtained the year end payroll reconciliation and ensures that the amounts in the accounts reconcile to the ledger and through to payroll;
- agreed payroll related accruals (e.g. unpaid leave) to supporting documents and reviewed for reasonableness, and
- performed substantive analytical procedure for M1 to M12, disaggregated by month.

There are no issues to bring to your attention.

### Operating expenses

Non-pay expenses on other goods and services also represents a significant percentage of the Council's operating expenses. Management uses judgement to estimate accruals of non-invoiced costs.

We identified completeness of non-pay expenses as a risk requiring particular audit attention.

We have:

- evaluated the Council's accounting policy for recognition of non-pay expenditure for appropriateness;
- gained an understanding of the Council's system for accounting for non-pay expenditure and evaluated the design of the associated controls;
- documented the accruals process and the controls management has put in place, challenging key underlying assumptions, the appropriateness of the source data used and the basis of calculations; and
- obtained a listing from the cashbook of non pay payments made in April and tested to ensure that they have been charged to the correct year and to confirm accuracy, occurrence, classification and cut off.



There are no issues to bring to your attention.

## Significant findings – other issues





This section provides commentary on new issues and risks which were identified during the course of the audit that were not previously communicated in the Audit Plan and a summary of any significant control deficiencies identified during the year.

Issue	Commentary	Auditor view
<p><b>IFRS 16 implementation has been delayed by one year</b></p> <p>Although the implementation of IFRS 16 has been delayed to 1 April 2021, audited bodies still need to include disclosure in their 2019/2020 statements to comply with the requirement of IAS 8 para 31. As a minimum, we would expect audited bodies to disclose the title of the standard, the date of initial application and the nature of the changes in accounting policy for leases.</p>	<p>We have reviewed the accounting policies for the Council to gain assurance that unadopted accounting standards have been appropriately disclosed within the statement of accounts</p>	<p>We noted in the draft statement of accounts that the disclosure has been appropriately dated as per the amended timeline. We continue to review the disclosures in line with the guidance and will report any findings to management</p>


# Significant findings – key estimates and judgements

Accounting area	Summary of management's policy	Auditor commentary	Assessment
<b>Provisions for NNDR appeals</b> - £6.8m (£2.4m short-term, £4.4m long-term)	The Council is responsible for repaying a proportion of successful rateable value appeals. Management calculate the level of provision required based upon the latest information about outstanding rates appeals provided by the Valuation Office Agency (VOA) and previous success rates.	<p>We have:</p> <ul style="list-style-type: none"> <li>reviewed the appropriateness of the underlying information used to determine the estimate;</li> <li>considered the reasonableness of increase in estimate; and</li> <li>confirmed the adequacy of disclosure of estimate in the financial statements.</li> </ul>	 (green)
<b>Investment property valuation process</b>	In accordance with IFRS 13 investment property should be measured at fair value at the reporting date.	<ul style="list-style-type: none"> <li>investment property per the financial statements note 10 totals £33.8m;</li> <li>the Council formally revalued all of its investment property as at 31<sup>st</sup> March 2020;</li> <li>we performed coverage sampling on Investment assets by testing a total amount of £27.5m of assets. The valuations were agreed to the valuer's report. We also examined the type of the property and the rental income earned to gain assurance over the property's classification;</li> <li>evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work;</li> <li>evaluated the competence, capabilities and objectivity of the valuation expert;</li> <li>wrote to the valuer to confirm the basis on which the valuation was carried out;</li> <li>challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding; and</li> <li>we are satisfied that the Investment property value included within the financial statements is not materially misstated.</li> </ul>	 (green)

## Assessment

-  We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
-  We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
-  We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
-  We consider management's process is appropriate and key assumptions are neither optimistic or cautious

# Significant findings – key estimates and judgements

Accounting area	Summary of management's policy	Auditor commentary	Assessment
<b>Land and Buildings – Other - £339.2m</b>	<p>The Council revalues its land and buildings on a rolling basis to ensure that carrying value is not materially different from fair value. This represents a significant estimate by management in the financial statements.</p> <p>In line with RICS guidance, the Council's valuer disclosed a material uncertainty in the valuation of the Council's land and buildings at 31 March 2020 as a result of Covid-19. The Council has included disclosures on this issue in Note 1.48.</p> <p>The Council formally re-values its land and buildings on a rolling programme to ensure they are re-valued at least every 5 years, however in accordance with the Code all land and buildings values are reviewed annually for material changes and re-valued at 31<sup>st</sup> March if necessary. Valuations have been carried out externally by Wilks, Head and Eve. Valuations of land and buildings were carried out using the methodologies and bases of estimation set out in the professional standards of RICS.</p> <p>Surplus assets are valued at their "highest and best use". All other assets are valued at historical cost, including infrastructure and Vehicles, Plant and Equipment.</p>	<p>We have:</p> <ul style="list-style-type: none"> <li>made an assessment of the valuer;</li> <li>considered the completeness and accuracy of the underlying information used to determine the estimate;</li> <li>challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding;</li> <li>we challenged management about their treatment of the waste plant; and</li> <li>reviewed the adequacy of disclosure of estimates in the Financial Statements.</li> </ul>	 <b>green</b>

## Assessment

- We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
- We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
- We consider management's process is appropriate and key assumptions are neither optimistic or cautious

# Significant findings – key estimates and judgements

Accounting area	Summary of management’s policy	Auditor commentary	Assessment
Net pension liability	Work is on-going in this area		

Assessment

- We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- We consider the estimate is unlikely to be materially misstated however management’s estimation process contains assumptions we consider optimistic
- We consider the estimate is unlikely to be materially misstated however management’s estimation process contains assumptions we consider cautious
- We consider management’s process is appropriate and key assumptions are neither optimistic or cautious

# Significant findings – matters discussed with management

This section provides commentary on the significant matters we discussed with management during the course of the audit.

Significant matter	Commentary	Auditor view
<p><b>PPE Valuation material valuation uncertainty</b></p> <p>The Covid-19 pandemic commenced within the last two weeks of the 2019-20 financial year and created a large uncertainty in financial markets and the market for other assets.</p> <p>This led to the Royal Institute of Chartered Surveyors (RICS) issuing guidance identifying that all valuations will have a material valuation uncertainty as at 31 March 2020. The Council's draft statement of accounts did not include a material valuation uncertainty disclosure and it was our view, as external auditors, that such a disclosure should be included.</p>	<p>The Council formally revalues its land and buildings on a rolling five-year basis to ensure that the carrying value is not materially different from fair value.</p> <p>The Covid-19 pandemic outbreak commenced within the last two weeks of the 2019-20 financial year and created a large uncertainty in a number of markets. This led to RICS issuing guidance to its members that a material valuation uncertainty should be included within the valuer's report and subsequently in the statement of accounts. The Valuer's report and draft account reflected this material valuation uncertainty as expected.</p>	<p>It is the view of the auditor that a material valuation uncertainty for the PPE valuation should be included in the accounts to reflect the uncertainty that existed at the balance sheet date. This has been included within the Financial Statements as appropriate.</p>
<p><b>Pension Liability</b></p> <p>Experience gains included in the change in actuarial valuations.</p> <p>Experience items arise when the actuary's estimations are refined by the use of more up to date data and, consequently, are different to the previous estimates. Examples of experience items include:</p> <ul style="list-style-type: none"> <li>• actual pensionable salary increases being different to the estimate</li> <li>• actual pension increase being different to the estimate</li> <li>• actual leavers/retirements/deaths being different to the estimate</li> <li>• actual transfer values being different to the estimate</li> </ul> <p>Experience items can arise in any financial year but are expected to be greatest in the first set of financial statements produced following a triennial review.</p>	<p>The recorded gain arising from the actuary's use of roll forward annually gave a gain of £11.226m over the three years since the last triennial full valuation.</p>	<p>Work is on-going in this area</p>

# Significant findings – going concern

## Our responsibility

As auditors, we are required to “obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern” (ISA (UK) 570).

## Going concern commentary

### Management's assessment process

The Council's accounts have been prepared on the going concern basis. Public sector bodies are assumed to be going concerns where the continuation of the provision of a service in the future is anticipated, as evidenced by inclusion of financial provision for that service in published documents.

## Auditor commentary

We have subjected the 2020/21 budget, Medium Term Financial Strategy and cash flow forecast to December 2021 to detailed scrutiny and in our consideration of the appropriateness of management's use of the going concern assumption.

The Section 151 officer has produced an assessment of the Council's use of the going concern assumption. We have reviewed this and the underlying support and concur with his opinion that the going concern basis is appropriate.

In only exceptional circumstances would we expect a local authority not to prepare its accounts on a going concern, in line with the Code and the public sector adoption of the going concern assumption.

In 2020/21 the Council expects to achieve a balanced budget and the Council's usable reserves at 31 March 2020 stood at £134m.

The Covid-19 pandemic has resulted in a reduction of income in 2020/21, some of which has been covered through government support. The Council have set a balanced budget for 2020/21, although this will require savings to be made. This position is after taking into account the Government Grant that the Council has received for Covid-19.

The auditing standards require us to consider the cash flow forecast of the Council for a period at least twelve months after the reporting date. The cashflow forecast prepared by the Council is therefore being extended to meet this requirement.



# Other matters for communication

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

Issue	Auditor commentary
<b>Matters in relation to fraud</b>	We have previously discussed the risk of fraud with the Audit Committee. We have not been made aware of any incidents in the period and no other issues have been identified during the course of our audit procedures to date.
<b>Matters in relation to related parties</b>	We are not aware of any related parties or related party transactions which have not been disclosed.
<b>Matters in relation to laws and regulations</b>	You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work to date.
<b>Written representations</b>	A letter of representation has been requested from the Council, including specific representations in respect of the Group, which is included in the Audit and Governance Committee papers.
<b>Confirmation requests from third parties</b>	We requested from management permission to send confirmation requests for Bank and Investment balances.
<b>Disclosures</b>	Our review found no material omissions in the financial statements
<b>Audit evidence and explanations/significant difficulties</b>	All information and explanations requested from management was provided.

# Other responsibilities under the Code

Issue	Commentary
<b>Other information</b>	<p>We are required to give an opinion on whether the other information published together with the audited financial statements (including the Annual Governance Statement and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</p> <p>No inconsistencies have been identified. We plan to issue an unmodified opinion in this respect – refer to Appendix E.</p>
<b>Matters on which we report by exception</b>	<p>We are required to report on a number of matters by exception in a numbers of areas:</p> <ul style="list-style-type: none"> <li>• If the Annual Governance Statement does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the other information of which we are aware from our audit</li> <li>• If we have applied any of our statutory powers or duties</li> </ul> <p>We have nothing to report on these matters.</p>
<b>Certification of the closure of the audit</b>	<p>We will be unable to certify the completion of the 2019/20 audit of Herefordshire Council in our auditor's report, as detailed in Appendix E as there remain unresolved matters from the prior years and out value for money work is still in progress. We have been updated by officers of progress on the prior year matter during the year.</p>
<b>Other information</b>	<p>We are required to give an opinion on whether the other information published together with the audited financial statements (including the Annual Governance Statement and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</p> <p>No inconsistencies have been identified. We plan to issue our opinion in the final Audit Findings Report.</p>

# Value for Money

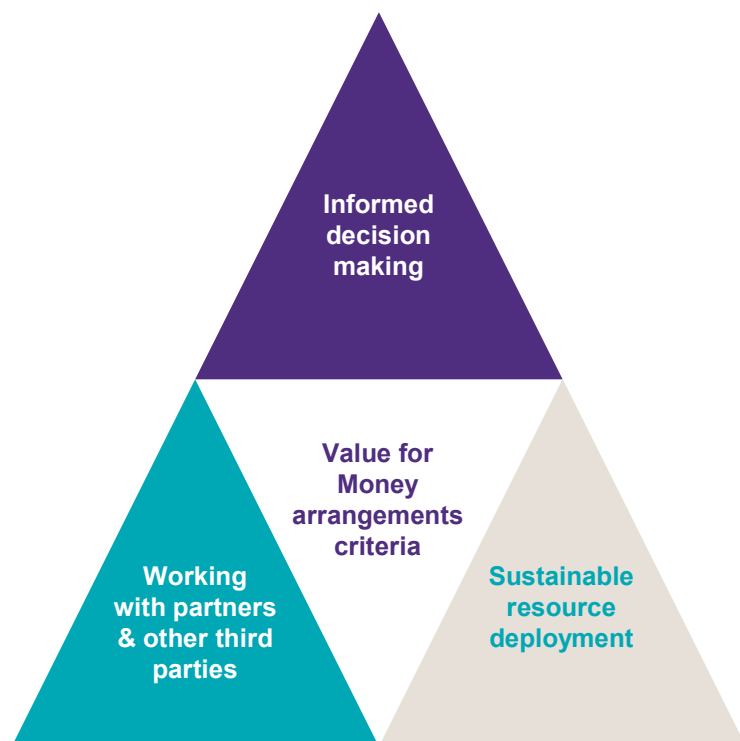
## Background to our VFM approach

We are required to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the Value for Money (VFM) conclusion.

We are required to carry out sufficient work to satisfy ourselves that proper arrangements are in place at the Council. In carrying out this work, we are required to follow the NAO's Auditor Guidance Note 3 (AGN 03) issued in April 2020. AGN 03 identifies one single 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."*

This is supported by three sub-criteria, as set out below:



## Risk assessment

We carried out an initial risk assessment in January 2020 and identified a number of significant risks in respect of specific areas of proper arrangements using the guidance contained in AGN03. We communicated these risks to you in our Audit Plan dated 28 January 2020.

We have continued our review of relevant documents up to the date of giving our report, and have not identified any further significant risks where we need to perform further work.

We carried out further work only in respect of the significant risks we identified from our initial and ongoing risk assessment.

# Value for Money

## Our work

AGN 03 requires us to disclose our views on significant qualitative aspects of the Council's arrangements for delivering economy, efficiency and effectiveness.

We have focused our work on the significant risks that we identified in the Council's arrangements. In arriving at our conclusion, our main considerations were:

- Financial sustainability
- Capital programme
- Governance arrangements

We have set out more detail on the risks we identified, the results of the work we performed, and the conclusions we drew from this work on pages 21 to 23.

## Overall conclusion

To be confirmed – our work is currently on-going.

# Value for Money

## Key findings

We set out below our key findings against the significant risks we identified through our initial risk assessment and further risks identified through our ongoing review of documents.

Significant risk	Findings
<p>The significant risk identified was financial sustainability. If the key assumptions within the Medium-Term Financial Strategy are not reasonably based, then the future financial position of the Council could be at risk.</p> <p>Audit work proposed to address this risk: we will discuss with Officers the key assumptions in the Medium-Term Financial Strategy and consider supporting evidence, particularly around looked after children as this appears to be an area where there has been consistent pressures against the budget.</p>	<p>The MTFS for 2019/20 -2021/22 was presented to Council on 15 February 2019 and a revenue budget of £151,092 was approved for the 2019/20 financial year. This MTFS included savings for 2019/20 of £3.6m which was achieved during the year.</p> <p>In June 2020, the Council reported an outturn position of £150.5m which agreed to the draft financial statements. This resulted in a small underspend against budget and the General Fund Balance increased by £5.9m to £81.4m.</p> <p>On 26 November 2020, Cabinet received a paper showing the impact that Covid-19 has had on the financial position as at September 2020. This shows that the Council are forecasting an outturn of £172m against a budget of £157m meaning a forecast year end position of an overspend of £15m, £10.8m being directly attributable to Covid-19. Officers are currently updating the MTFS and are exploring savings schemes to mitigate this overspend.</p> <p>The original budget for the Children &amp; Families Directorate was £30.8m and £18.6m specifically in relation to looked after children. The reported outturn for 2019/20 was £32.3m and £20.6m for looked after children. The overall overspend for the Directorate was £1.4m, however £1.9m was the overspend on looked after children.</p> <p>The reason for the increase is both the increase in numbers and costs associated with each case as the cases are becoming more complex.</p> <p>Ofsted undertook a focused visit in December 2019 and as a result of this, the service will require additional support to address the findings raised.</p> <p><b>Whilst the Council continues to operate under significant financial pressures, in particular due to the impact of Covid-19, it has effective arrangements in place to routinely monitor its budget and has a good track record of delivering the required savings. We therefore conclude that overall the Council has appropriate arrangements in place to manage its financial sustainability. However, the impact of Covid-19 is not yet fully known. Consequently, the Council will need to maintain and strengthen its financial monitoring arrangements to ensure that funding and spending pressures are identified and acted upon swiftly.</b></p>

# Value for Money

## Key findings

We set out below our key findings against the significant risks we identified through our initial risk assessment and further risks identified through our ongoing review of documents.

### Significant risk

### Findings

The significant risk identified related to the Council's capital programme. There has been a number of issues identified in recent years around the capital programme. Whilst the Council is responding to the issues, we consider that this represents a significant on-going risk to our vfm conclusion.

The audit work proposed to address this risk is that we will consider the actions that the Council is taking to respond to concerns raised around the governance of the capital programme. We will also consider the governance of capital projects in support of NMiTE.

To address the issues highlighted in previous years, the Council employed a Consultant to undertake a review of the governance arrangements around the capital programme. The brief provided to the Consultant was reviewed and found to be comprehensive.

The consultant provided the S151 Officer with a series of findings and where these could be implemented immediately, were done so. Other longer term recommendations are currently being worked through by the Management team.

In our 2018/19 Audit Findings Report, we reported that there was a delay in procurement around the by-pass however we issued an unqualified opinion based on the fact that as no contract had actually been awarded, there was no loss to the Council. A 'pause and review' process was undertaken and a review of the options surrounding the by-pass were examined. In December 2020, Cabinet agreed to formally stop the by-pass and in the Council meeting on 20 January the financial implications of this will be discussed.

Our work in this area is currently on-going.

# Value for Money

## Key findings

We set out below our key findings against the significant risks we identified through our initial risk assessment and further risks identified through our ongoing review of documents.

Significant risk	Findings
<p>The significant risk identified was governance arrangements. Following the Authority's political change, new policies will be considered and implemented. It is likely that significant political decisions will be taken and there is a consequent need to ensure that the governance arrangements supporting such decisions remains sound.</p> <p>Audit work proposed to address this risk: we will discuss with Officers the impact that the political change has had and consider how this has been reflected in the governance arrangements in place.</p>	<p>Following the 2019 elections, a three-way coalition between 'Herefordshire Independents', 'It's our County' and the Green Party were formed. This resulted in new Cabinet positions and new members now holding senior positions.</p> <p>Discussions were held with the Chief Executive, S151 Officer and Monitoring Officer to discuss the impact of the political change. The Council had procedures in place to provide training to the new Administration as this is a typical change in local government.</p> <p>Officers agreed that the new Administration appears to be working as a collective and the Cabinet Officers like the support of the full Cabinet so have been sharing information through the Cabinet briefing more than has been happening in the past.</p> <p>An on-going training programme is being developed to address training needs as they arise.</p> <p><b>Overall we would conclude that the new Administration has settled into a coalition and is accepting Officers' guidance and advice when needed.</b></p>

# Independence and ethics

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 Financial Reporting Council's Ethical Standard and confirm that we, as a firm, and each covered person, 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 and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements.

Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in May 2020 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

Details of fees charged are detailed in Appendix D



# Independence and ethics


## Audit and Non-audit services

For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The following non-audit services were identified, as well as the threats to our independence and safeguards that have been applied to mitigate these threats.

	Fees £	Threats identified	Safeguards
<b>Audit related</b>			
Certification of Education Skills Funding Agency	3,000	Self-Interest (because this is a recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is approx. £3,000 in comparison to the total fee for the audit of £95,792 and in particular relative to Grant Thornton UK LLP's turnover overall.
Certification of Teachers Pension Return	5,500	Self-Interest (because this is a recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is approx. £5,500 in comparison to the total fee for the audit of £95,792 and in particular relative to Grant Thornton UK LLP's turnover overall.
Certification of Housing Benefit Claim	7,000	Self-Interest (because this is a tbc recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is approx. £7,000 in comparison to the total fee for the audit of £95,792 and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. We do not prepare the return, and do not expect material changes to arise from the work that would affect information in the financial system. We report factually, based on the instructions and any decisions on amendments to returns are for the Council to make, in discussion with the relevant government body. These factors all mitigate the perceived self-interest, self-review and management threats to acceptable levels.

# Action plan

We have identified one recommendations for the Council as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2020/21 audit. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

Assessment	Issue and risk	Recommendations
 <b>Medium</b>	<p><b>Journals authorisation</b></p> <p>We reported in the 2018/19 Audit Findings Report that the journals process did not have appropriate authorisation. Management confirmed that this was to be implemented in Business World. This has not occurred during 2019/20. We would therefore repeat our previous recommendation that the Council consider its authorisation of journals.</p>	<p>We therefore recommend that management look to increase the priority of the authorisation process or put in place mitigating controls until this process can be implemented.</p> <p><b>Management response</b></p> <p>We will reconsider this recommendation. Currently posting restrictions and authorisation outside the general ledger controls are in place.</p>

- Controls**
- High – Significant effect on control system
  - Medium – Effect on control system
  - Low – Best practice

# Follow up of prior year recommendations

We identified the following issues in the audit of Herefordshire Council's 2018/19 financial statements, which resulted in two recommendations being reported in our 2018/19 Audit Findings report.

Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
X	<p>Journals authorisation – During the course of our testing we noted that none of the journals posted to the financial system were subject to an authorisation process. The risk is that this could result in a material misstatement in the financial statements. From discussions with management we note that the financial system has restrictions in place so that only appropriate staff can post journals. We understand that management are looking to introduce an authorisation process in the future.</p> <p>We therefore recommend that management look to increase the priority of the authorisation process or put in place mitigating controls until this process can be implemented.</p>	<p>Management confirmed that this was to be implemented in Business World. This has not occurred during 2019/20. We would therefore repeat our previous recommendation that the Council consider its authorisation of journals.</p>
✓	<p>The Council now prepares group financial statements however the Annual Governance Statement appears to be focussed on the Council with limited reference to the subsidiary company, Hoople. The CIPFA accounting Code confirms that where there is a group relationship, the review of the internal control systems shall include group activities.</p> <p>We therefore recommend that management look to expand the Annual Governance Statement in future years to cover the group activities.</p>	<p>The Annual Governance Statement has been expanded to cover the group financial statements.</p>

## Assessment

✓ Action completed

X Not yet addressed

## Appendix C

# Audit adjustments

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

## Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the key statements and the reported net expenditure for the year ending 31 March 2020.

Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000
None			

## Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Disclosure omission	Detail	Auditor recommendations	Adjusted?
PPE - Disposals	Disposal amount of St Weonard's primary school was incorrectly recorded by £500k in the fixed asset register as net book value less an amount in the revaluation reserve	Adjustment required	✓
Officers' Remuneration	One Officer incorrectly banded as £145-£150k instead of £150-£155k. Also, 2018/19 bandings not consistent with the published 2018/19 financial statements.	Adjustment required	✓
Exit packages	Exit packages in the financial statements did not agree to the underlying supporting workpapers. Agreed working papers show correct figures.	Adjustment required	✓
Capital Financing and Expenditure	PPE Additions of £554k was overstated in the Capital Financing and Expenditure note due to loan repayments being misclassified. An additional line was needed in the note.	Adjustment required	✓
Grant Income / Dedicated Schools Grant	Two miscodings were identified which had overstated grant income and children's expenditure by £554k (one caused overstatement by £873k and the other an understatement of £283k). The net impact on the note was nil. In addition, figures did not cast due to rounding's.	Adjustment required	✓
Audit fees	Audit fees incorrectly stated as fees for non-statutory work should be separately disclosed.	Adjustment required	✓

## Appendix C

# Audit adjustments

Disclosure omission	Detail	Auditor recommendations	Adjusted?
Related parties	Disclosure within the significant long term contracts section is incorrectly stated for Balfour Beatty	Adjustment required	✓
Remuneration notes	Difference in one Officer between payroll evidence and the financial statements	Adjustment required	✓
Accounting policies	Removal of policies which are no longer relevant	Adjustment required	✓
Presentation	Wording throughout the financial statements to be updated to ensure correctly and appropriately reflects Council's background and processes.	Adjustment required	✓

# Audit adjustments

## Impact of unadjusted misstatements

The table below provides details of adjustments identified during the 2019/20 audit which have not been made within the final set of financial statements. The Audit and Governance Committee is required to approve management's proposed treatment of all items recorded within the table below:

Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000	Reason for not adjusting
None				

## Impact of prior year unadjusted misstatements

The table below provides details of adjustments identified during the prior year audit which had not been made within the final set of 2018/19 financial statements.

Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000	Reason for not adjusting
Our testing of expenditure cut off discovered an accrual for Housing Benefits expenditure for 2018/19 that was paid out 2019/20 has not been made. From the items we tested this identified an error of £23,588, which when extrapolated across the population is £570,927.	(571)	(571)	(571)	As this is an extrapolated error we would not expect an adjustment
During our grants testing we identified a £25k credit to the fees and charges grants section was miscoded and should have been a credit to expenditure. Expenditure and income have therefore been overstated. The extrapolated error is £554,026.	(554)	(554)	(554)	As this is an extrapolated error we would not expect an adjustment
<b>Overall impact</b>	<b>1,125</b>	<b>1,125</b>	<b>1,125</b>	

## Appendix D

# Fees

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

Audit fees	Proposed fee	Final fee
Council audit	95,792	95,792
Fee Variation	11,000	tbc
Covid-19 fee	tbc	tbc
<b>Total fee – excluding certification</b>	<b>106,792</b>	<b>tbc</b>
Grant certification	15,500	tbc
<b>Total audit fees (excluding VAT)</b>	<b>£122,292</b>	<b>tbc</b>

The fees reconcile to the draft financial statements.

Non-audit fees for other services	Proposed fee	Final fee
Certification of Education Skills Funding Agency	3,000	3,000
Certification of Teachers Pension Return	5,500	5,500
Housing Benefit Grant Claim	7,000	tbc
<b>Total non- audit fees (excluding VAT)</b>	<b>£15,500</b>	<b>tbc</b>

