

The Audit Findings for Surrey County Council

DRAFT

This version of the report is a draft. Its contents and subject matter remain under review and its contents may change and be expanded as part of the finalisation of the report.

Year ended 31 March 2015

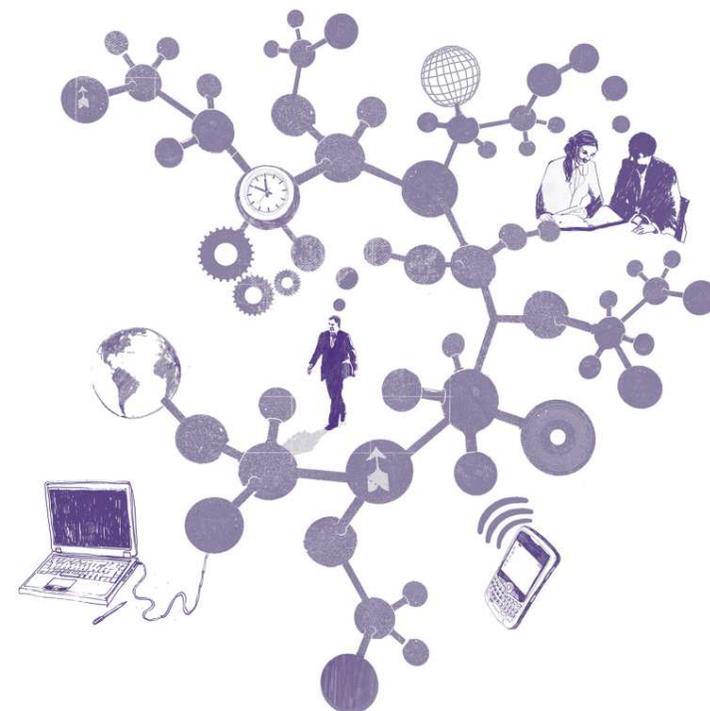
Page 215
July 2015

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July 2015

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Page 216
Audit Findings for Surrey County Council for the year ending 31 March 2015

This Audit Findings report highlights the significant findings arising from the audit for the benefit of those charged with governance (in the case of Surrey County Council, the Audit and Governance Committee), as required by International Standard on Auditing (UK & Ireland) 260. Its contents have been discussed with management.

As auditors we are responsible for performing the audit, in accordance with International Standards on Auditing (UK & Ireland), 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.

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 primarily 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 any control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. 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.

We would like to take this opportunity to record our appreciation for the kind assistance provided by the finance team and other staff during our audit.

Yours faithfully

Chartered Accountants

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Andy Mack, for and on behalf of Grant Thornton UK LLP

Contents

Section	Page
1. Executive summary	4
2. Audit findings	8
3. Value for Money	24
4. Fees, non-audit services and independence	30
5. Communication of audit matters	32
Appendices	
A Action plan	35
B Audit opinion	36

Section 1: Executive summary

- 01. Executive summary
- 02. Audit findings
- 03. Value for Money
- 04. Fees, non-audit services and independence
- 05. Communication of audit matters

Executive summary

Purpose of this report

This report highlights the key matters arising from our audit of Surrey County Council's (the Council) group and Council financial statements for the year ended 31 March 2015. It is also used to report our audit findings to management and those charged with governance in accordance with the requirements of International Standard on Auditing 260 (ISA UK&I).

Under the Audit Commission's Code of Audit Practice we are required to report whether, in our opinion, the group and Council's financial statements present a true and fair view of the financial position and expenditure and income for the year and whether they have been properly prepared in accordance with the CIPFA Code of Practice on Local Authority Accounting. We are also required to reach a formal conclusion on whether the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources (the Value for Money conclusion).

Introduction

In the conduct of our audit we have had to alter our planned audit approach, which we communicated to you in our Audit Plan dated 9 April 2015. Specifically, we have had to undertake additional procedures for our value for money conclusion in respect of the publication of the Ofsted report on Children's Services in June 2015.

As at 16 July our audit is nearing completion although we are finalising our procedures in a small number of areas:

Audit testing still to complete:

- Related party transactions

Procedures to be performed as part of audit closing procedures once above matters resolved:

- review of the final version of the financial statements
- obtaining and reviewing the final management letter of representation once it has been signed at the Audit and Governance Committee meeting
- updating our post balance sheet events review, to the date of signing the opinion
- testing of the Whole of Government Accounts return.

We received draft financial statements and accompanying working papers at the start of our audit, in accordance with the agreed timetable.

Key issues arising from our audit

Financial statements opinion

We anticipate providing an unqualified opinion in respect of the financial statements.

The key messages arising from our audit of the group and Council's financial statements are that the Council:

- produced draft financial statements and working papers to a good standard , bringing forward the timetable for working paper preparation
- successfully prepared group accounts for the first time in respect of S. E. Business Services Limited and Surrey Choices.
- the timeliness of response to audit queries could be improved. This will be important in enabling the Council to close down its accounts more efficiently ahead of the statutory deadline for audited accounts moving forward in 2017/18.

During the course of our audit management identified two adjustments affecting the group's and Council's reported financial position (details are recorded in section two of this report). The draft financial statements for the year ended 31 March 2015 recorded net expenditure of £1,021m. The equivalent figure per the audited financial statements is £1,043m. The adjustments relate to:

An amendment in respect of the collection fund required on receipt of the council tax and business rate returns from Surrey District and Borough Councils.

The accounting treatment in respect of three foundation schools that gained academy status during the year.

Management have also made additional disclosure in the financial statements regarding a critical judgement re the derecognition of the three schools mentioned above. The impairment charge in respect of these schools would be £23.3m. Rather than make a charge to the general fund in respect of the derecognition, management have applied a statutory override. It is currently unclear as to whether the application of the override is permitted by the regulations. CIPFA's view is that the applicable statutory adjustment is for the authority to determine and the Council should obtain its own advice as to the statutory basis for the reversal of the loss. We are satisfied that the impact is not material on the 2014/15 financial statements. However we recommend that the Council obtains legal advice to determine if the approach it has taken is appropriate. Further details are provided on page 18 of this report.

Value for Money conclusion

The Council continues to have good arrangements in place to secure financial resilience. In determining our conclusion on the Council's arrangements for challenging economy, efficiency and effectiveness, we have had regard to Ofsted's findings from its new style multi-agency inspection of services for children in need of help and protection, children looked after and care leavers. The inspection took place in October and November 2014 at the Council's request and concluded that children's services were inadequate. Immediately following the inspection the Council established an Improvement Board to action Ofsted's recommendations.

We propose to issue a value for money conclusion which is qualified on an 'except for' basis in respect of this one matter. This is based on the outcome of Ofsted's inspection and not on any further inspection work performed by Grant Thornton in respect of children's services. We have not identified any weaknesses in other arrangements. Further detail of our work on Value for Money is set out in section three of this report.

Whole of Government Accounts (WGA)

As at 16 July we have not completed our work in respect of the Whole of Government Accounts in accordance with the national timetable.

We will update Audit and Governance Committee members with the findings of our work.

Controls

Roles and responsibilities

The Council's management is responsible for the identification, assessment, management and monitoring of risk, and for developing, operating and monitoring the system of internal control.

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 any control weaknesses, we report these to the Council.

Findings

Our work has not identified any control weaknesses which we wish to highlight for your attention.

Further details are provided within section two of this report.

The way forward

Matters arising from the financial statements audit and review of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources have been discussed with the Director of Finance.

We have made a small number of recommendations, which are set out in the action plan in Appendix A. Recommendations have been discussed and agreed with the Director of Finance and the finance team.

Acknowledgment

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

Grant Thornton UK LLP
July 2015

Section 2: Audit findings

- 01. Executive summary
- 02. Audit findings**
- 03. Value for Money
- 04. Fees, non-audit services and independence
- 05. Communication of audit matters

Audit findings

In this section we present our findings in respect of matters and risks identified at the planning stage of the audit and additional matters that arose during the course of our work. We set out on the following pages the work we have performed and the findings arising from our work in respect of the audit risks we identified in our audit plan, presented to the Audit and Governance Committee on 9 April 2015. We also set out the adjustments to the financial statements arising from our audit work and our findings in respect of internal controls.

Changes to Audit Plan

We have made one change to our Audit Plan as previously communicated to you on 9 April 2015. Further details are provided on page 5.

Audit opinion

Our proposed audit opinion is set out in Appendix B.

Audit findings against significant risks

"Significant risks often relate to significant non-routine transactions and judgmental matters. Non-routine transactions are transactions that are unusual, either due to size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty" (ISA (UK&I) 315).

In this section we detail our response to the significant risks of material misstatement which we identified in the Audit Plan. As we noted in our plan, there are two presumed significant risks which are applicable to all audits under auditing standards.

	Risks identified in our audit plan	Work completed	Assurance gained and issues arising
1.	<p>Improper revenue recognition</p> <p>Under ISA (UK&I) 240 there is a presumed risk that revenue may be misstated due to improper recognition</p>	<ul style="list-style-type: none"> • review and testing of revenue recognition policies • testing of material revenue streams • review of unusual significant transactions 	Our audit work has not identified any issues in respect of the risk identified.
2.	<p>Management override of controls</p> <p>Under ISA (UK&I) 240 there is a presumed risk of management over-ride of controls</p>	<ul style="list-style-type: none"> • testing of journal entries • review of unusual significant transactions • review of accounting estimates, judgements and decisions made by management 	Our audit work has not identified any issues in respect of the risk identified.

Page 224

Audit findings against significant risks (continued)

	Risks identified in our audit plan	Work completed	Assurance gained and issues arising
3.	<p>Valuation of property, plant and equipment</p> <p>The Council undertakes a rolling programme of revaluations of its land and buildings. This represents a significant estimate by management in the financial statements.</p>	<ul style="list-style-type: none"> • Identification of the controls put in place by management to ensure that the carrying value of property, plant & equipment is not materially different from fair value at year end. An assessment of whether these controls were implemented as expected and whether they are sufficient to mitigate the risk of material misstatement. • Review of the consistency of the financial statements with the valuation report from your valuers • Performing procedures to confirm the reasonableness of the proposed revaluations, including reference to national trends. 	<p>Our audit work has not identified any issues in respect of the risk identified.</p>
4.	<p>Valuation of property, plant and equipment – schools</p> <p>Guidance issued during 2014 has confirmed that maintained schools (but not free schools or academies) are separate entities, and that under IFRS 10 they meet the definition of entities controlled by local authorities which should be consolidated in group accounts. The 2014/15 CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom (the Code) requires local authorities to account for maintained schools within their single entity accounts. Identifying and accounting for school land and buildings not already included in the Council's accounts is a significant exercise.</p>	<ul style="list-style-type: none"> • We have discussed the guidance with finance team and agreed an approach for the accounting of the authority's voluntary-aided, voluntary-controlled and foundation schools. • Identification of the controls put in place by management to ensure the schools to be included in the authority's accounts are correctly identified and accounted for. An assessment of whether these controls were implemented as expected and whether they are sufficient to mitigate the risk of material misstatement. • Review of the judgements made by management for each school reviewed and agree the land and buildings included to supporting working papers. 	<p>Our audit work has not identified any issues in respect of the risk identified.</p>

Page 225

Audit findings against significant risks (continued)

	Risks identified in our audit plan	Work completed	Assurance gained and issues arising
5.	<p>Consolidation – schools</p> <p>Guidance issued during 2014 has confirmed that maintained schools (but not free schools or academies) are separate entities, and that under IFRS 10 they meet the definition of entities controlled by local authorities which should be consolidated in group accounts. The 2014/15 CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom (the Code) requires local authorities to account for maintained schools within their single entity accounts. This includes school income and expenditure as well as assets and liabilities. Identifying and accounting for schools not already included in the Council's accounts is a significant exercise.</p>	<ul style="list-style-type: none"> We have discussed the guidance with the finance team and agreed an approach for the accounting of the authority's voluntary-aided, voluntary-controlled and foundation schools Identification of the controls put in place by management to ensure the schools to be included in the authority's accounts are correctly identified and accounted for. Assessment of whether these controls were implemented as expected and whether they are sufficient to mitigate the risk of material misstatement. Review of the judgements made by management for each school assessed. <p>As at 16 July, the following procedures are in progress:</p> <ul style="list-style-type: none"> Testing of assets and liabilities, income and expenditure for those schools included to supporting working papers. 	<p>Subject to resolution of the outstanding issues as detailed on page 5 of this report, our audit work has not identified any issues in respect of revenue recognition.</p> <p>We will update Audit and Governance Committee members with the findings from our work.</p>
6.	<p>Valuation of pension fund liability</p> <p>The Council's pension fund liability represents a significant estimate in the financial statements.</p>	<ul style="list-style-type: none"> We have identified the controls put in place by management to ensure that the pension fund liability is not materially misstated. We have concluded these controls were implemented as expected and are sufficient to mitigate the risk of material misstatement. Review of the consistency of the financial statements with the actuarial report from your actuary Procedures to confirm the reasonableness of the actuarial assumptions made. 	<p>Our audit work has not identified any issues in respect of the risk identified.</p>

Page 226

Audit findings against significant risks (continued)

	Risks identified in our audit plan	Work completed	Assurance gained and issues arising
7.	<p>Consolidation – S.E. Business Services Limited and Surrey Choices Limited.</p> <p>The Council will be preparing consolidated accounts for the first time this year. Although its subsidiaries' accounts are not expected to be quantitatively material to the group, they are qualitatively material.</p>	<ul style="list-style-type: none"> • Identification of the controls put in place by management over the consolidation process. Assessment of whether these controls were implemented as expected and whether they are sufficient to mitigate the risk of misstatement and ensure that all required disclosures are made. • Review and testing of the consolidation working papers and agreement to supporting evidence. 	<p>Our audit work has not identified any issues in respect of the risk identified.</p>



Audit findings against other risks

In this section we detail our response to the other risks of material misstatement which we identified in the Audit Plan. Recommendations, together with management responses, are attached at Appendix A.

Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
Operating expenses	Creditors understated or not recorded in the correct period	<ul style="list-style-type: none"> Walkthrough of your controls in place over operating expenditure Review of the year-end reconciliation of your accounts payable system to the general ledger Testing of year-end creditors and accruals Testing of post-year end payments 	Our audit work has not identified any issues in respect of the risk identified.
Employee remuneration	Employee remuneration accruals understated	<ul style="list-style-type: none"> Walkthrough of your controls in place over payroll expenditure Review of the year-end reconciliation of your payroll system to the general ledger Trend analysis of the monthly payroll runs from during the year Testing of employee contracts to provide sufficient assurance over existence and occurrence. 	Our audit work has not identified any issues in respect of the risk identified.
Property, plant and equipment	Property, plant and equipment activity not valid	<ul style="list-style-type: none"> Walkthrough of your controls in place over property, plant and equipment Review of the reconciliation of your fixed assets register to the general ledger Testing of a sample of disposals Testing of a sample of additions Testing of the depreciation charge for the year 	Our audit work has not identified any issues in respect of the risk identified.

Group audit scope and risk assessment

ISA (UK&I) 600 requires that as Group auditors we obtain sufficient appropriate audit evidence regarding the financial information of the components and the consolidation process to express an opinion on whether the group financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Component	Significant?	Level of response required under ISA 600	Risks identified	Work completed	Assurance gained & issues raised
S. E. Business Services Limited	No	Targeted	None	Agreement of amounts to underlying financial records and performance of a high level analytical review.	Our audit work has not identified any issues in respect of the risk identified.
Surrey Choices Limited	No	Targeted	None	Agreement of amounts to underlying financial records and performance of a high level analytical review.	Our audit work has not identified any issues in respect of the risk identified.

Accounting policies, estimates & judgements

In this section we report on our consideration of accounting policies, in particular revenue recognition policies, and key estimates and judgements made and included with the Council's financial statements.

Accounting area	Summary of policy	Comments	Assessment
Revenue recognition	<ul style="list-style-type: none"> • Revenue (income) from the sale of goods and provision of services is recognised when the Council transfers the goods or completes delivery of a service • Whether paid on account, by instalments or in arrears, government grants and third party contributions and donations are recognised as due to the Council when there is reasonable assurance that: <ul style="list-style-type: none"> (i) The Council will comply with the conditions attached to the payments; and (ii) The grants or contributions will be received. 	<ul style="list-style-type: none"> • The accounting policies are adequately disclosed in line with the requirements of the Code • Our testing of government grants and contributions has not identified any instances of improper revenue recognition. 	 Green
Estimates and judgements	<p>Critical judgements include:</p> <ul style="list-style-type: none"> • Recognition of grants and contributions • Accounting treatment of the Council's PFI scheme • Whether group accounts should be prepared • Applying the statutory override in not making a charge to the Council's general fund in respect of 3 schools that converted to academy status in the year <p>Key estimates include:</p> <ul style="list-style-type: none"> • The useful lives of property, plant & equipment • Provisions • Pensions liability • Provision for the impairment of receivables 	<ul style="list-style-type: none"> • Critical judgements and estimation uncertainties are disclosed in notes 3 and 4 of the financial statements and are in line with the requirements of the Code. • Whilst the Council's companies are numerically immaterial to the financial statements, the Council has still prepared group accounts this year. • The Council's judgement in relation to the schools converting to academies has been referred to by means of a disclosure in the revised financial statements. Further detail is provided on page 17 of this report. 	 Green

Page 230

Assessment

- Marginal accounting policy which could potentially attract attention from regulators
 - Accounting policy appropriate but scope for improved disclosure
- Accounting policy appropriate and disclosures sufficient

Accounting policies, estimates & judgements (continued)

Accounting area	Summary of policy	Comments	Assessment
Judgements - local authority maintained schools premises	As a result of guidance requiring local authorities to account for maintained schools within their single entity accounts, the Council has undertaken a review of its schools to determine which of these to include in its accounts.	The Council has included in the revised financial statements an expanded disclosure of their judgements made over schools consolidation that more fully reflects the decisions taken.	 Green
Going concern	The Directors have a reasonable expectation that the services provided by the Council will continue for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.	We have reviewed the Directors' assessment and are satisfied with managements' assessment that the going concern basis is appropriate for the 2014/15 financial statements.	 Green
Other accounting policies	We have reviewed the Council's policies against the requirements of the CIPFA Code and accounting standards.	Our review of accounting policies has not highlighted any issues which we wish to bring to your attention	 Green

Page 231

Assessment

- Marginal accounting policy which could potentially attract attention from regulators
- Accounting policy appropriate and disclosures sufficient
- Accounting policy appropriate but scope for improved disclosure



Accounting policies, estimates & judgements (continued)

Accounting area	Summary of policy	Comments
<p>Judgements - schools converting to academy status during the year</p>	<p>There were 3 foundation schools within the county that gained academy status during 2014/15. When this transfer took place the schools were removed from the council's accounts. There are two approaches that determine the accounting treatment when this takes place:</p> <ul style="list-style-type: none"> • If a foundation school is on the council's balance sheet by virtue of the council owning the land, and if the school becomes an academy, then when it is written off, a statutory adjustment is made against the capital adjustment account. • If a foundation school is on the council's balance sheet by virtue of the school's control, and the school becomes an academy, it is unclear whether this adjustment against the CAA is permitted and as a result the loss should be charged to the general fund. The general fund is used by the council as a basis for setting its annual budget each year. <p>The Council has three foundation schools that have become academies during the year and which fit into the second category above. The impairment charge in respect of these schools would be £23.3m. Management have not applied this charge to the general fund in the draft financial statements and it is unclear whether the regulations permit this approach. CIPFA's view is that the applicable statutory adjustment is for the authority to determine and the Council should obtain its own advice as to the statutory basis for the reversal of the loss.</p>	<p>Management has decided not to charge this amount to the general fund as they consider that this would represent a double charge to the public purse in respect of these assets. We are awaiting receipt of the Council's legal advice on this matter.</p>

Other communication requirements

We set out below details of other matters which we are required by auditing standards to communicate to those charged with governance.

	Issue	Commentary
1.	Matters in relation to fraud	<ul style="list-style-type: none"> We have previously discussed the risk of fraud with the Audit and Governance Committee and have not been made aware of any incidents in the period and no other issues have been identified during the course of our audit.
2.	Matters in relation to laws and regulations	<ul style="list-style-type: none"> We are not aware of any significant incidences of non-compliance with relevant laws and regulations.
3.	Written representations	<ul style="list-style-type: none"> A standard letter of representation has been requested from the Council.
4.	Disclosures	<ul style="list-style-type: none"> Our review found no non-trivial omissions in the financial statements.
5.	Matters in relation to related parties	<ul style="list-style-type: none"> We are not aware of any related party transactions which have not been disclosed.
6.	Confirmation requests from third parties	<ul style="list-style-type: none"> We obtained direct confirmations from the PWLB, the Council's bank and counterparties with whom the Council has placed investment deposits. All of these confirmations positively stated the balances included in the Council's financial statements.

Page 233



Internal controls

The purpose of an audit is to express an opinion on the financial statements.

Our audit included consideration of internal controls relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. We considered and walked through the internal controls for Property, Plant & Equipment, Employee Remuneration and Operating Expenses as set out on page 13.

The controls were found to be operating effectively and we have no matters to report to the Audit and Governance Committee.

Adjusted misstatements

A number of adjustments to the draft financial statements have been identified during the audit process. We are required to report all non-trivial misstatements to those charged with governance, whether or not the financial statements have been adjusted by management. The table below summarises the adjustments arising from the audit which have been processed by management. There were no unadjusted misstatements.

Impact of adjusted misstatements

All adjusted misstatements are set out below along with the impact on the primary statements and the reported financial position.

Detail	Comprehensive Income and Expenditure Account £'000	Balance Sheet £'000	Impact on total net expenditure £000
1 The Council has processed an adjustment to the collection fund in respect of council tax and business rate returns received from Surrey District and Borough Councils. We have agreed the final details of this adjustment with the finance team.	Cr local taxation 4,424	Dr debtors 5,187 Dr creditors 1,288 Cr provisions 2,051 Cr unusable reserves – collection fund adjustment account 4,424	Cr deficit on provision of services 4,424
2 The revaluation gain on Foundation Schools as at 31 March 2015 was incorrectly recorded in the draft financial statements. This has no net impact on the Council's recorded financial position and has been corrected by management.	Nil	Dr property, plant & equipment 6,260 Dr unusable reserves - revaluation reserve 3,024 Cr property, plant & equipment 3,024	Nil
3 The upward revaluation of three foundation schools in 2013/14 that converted to academy status in 2014/15 has been incorrectly accounted for in the draft financial statements. This has no net impact on the Council's recorded financial position and management have agreed to correct for this in the revised financial statements. We are awaiting evidence to support the impact on the financial statements.	Dr cost of services – education and children's services 22,131	Cr unusable reserves – revaluation reserve 5,871 Cr unusable reserves – capital adjustment account 389	Dr deficit on provision of services 22,131
Overall impact	(17,707)	(7,660)	(17,707)

Impact of uncorrected misstatements in the prior year

Detail	Comprehensive Income and Expenditure Account £'000	Balance Sheet £'000	Reason for not adjusting
1 Incorrect calculation of depreciation on infrastructure assets	(2,715)	2,715	This adjustment was immaterial to the 13/14 financial statements. Management have corrected for this in the 14/15 financial statements.
Overall impact	(2,715)	2,715	

Misclassifications & 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.

Adjustment type	Value £'000	Account balance	Impact on the financial statements
1 Disclosure	n/a	Note 12 – Property, plant & equipment and Note 14 – Foundation, voluntary aided and voluntary controlled schools and academies	The Council has agreed to update these disclosures to reflect: <ul style="list-style-type: none"> - The rationale for judgements made over which local authority maintained schools to include in the council's accounts (note 14) - An inconsistency between reference to historical cost and a rolling programme of asset revaluation (note 12)
2 Disclosure	n/a	Note 27 – Senior officer remuneration	The Council has revised this disclosure to correct for small errors in the 2014/15 salary figures of four officers.
3 Disclosure	n/a	Note 30 – External audit costs	To ensure compliance with the CIPFA Code of Local Practice, the Council has amended this disclosure so as to include the current and prior year external audit fees at their gross values, before deduction of rebates received from the Audit Commission.

Section 3: Value for Money

- 01. Executive summary
- 02. Audit findings
- 03. Value for Money**
- 04. Fees, non-audit services and independence
- 05. Communication of audit matters

Value for Money

Value for money conclusion

The Code of Audit Practice 2010 (the Code) describes the Council's responsibilities to put in place proper arrangements to:

- secure economy, efficiency and effectiveness in its use of resources;
- ensure proper stewardship and governance; and
- review regularly the adequacy and effectiveness of these arrangements.

We are required to give our VfM conclusion based on two criteria specified by the Audit Commission which support our reporting responsibilities under the Code.

These criteria are:

The Council has proper arrangements in place for securing financial

Resilience - the Council has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.

The Council has proper arrangements for challenging how it secures

economy, efficiency and effectiveness - the Council is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

Key findings

Securing financial resilience

We have undertaken a review which considered the Council's arrangements against the three expected characteristics of proper arrangements as defined by the Audit Commission:

- Financial governance;
- Financial planning; and
- Financial control.

Our work highlighted that the Council has taken positive action to address the recommendations we raised in our 2013/14 VfM report and continues to maintain proper arrangements in these areas. It develops appropriate responses to external developments, such as the implementation of the Better Care Fund, and internal developments, such as the establishment of S.E. Business Services Ltd. and Surrey Choices Ltd.

We have highlighted one risk in respect of the Council's identification of plans for achieving the level of savings required over the next 5 years.

Challenging economy, efficiency and effectiveness

We have considered the Council's arrangements to challenge economy, efficiency and effectiveness against the following themes:

- Prioritising resources
- Improving efficiency & productivity

Overall VfM conclusion

In overall terms, the Council has good arrangements in place across a number of key areas. We have drawn attention in our draft conclusion to the following matter:

- The overall judgement in the Ofsted report published on 3 June 2015 and based on their new style multi-agency inspection in November and December 2014 is that children's services were inadequate. This judgement is evidence of weaknesses in arrangements for promoting and demonstrating the principles and values of good governance within the Council's Children's Services directorate. Immediately following the inspection the Council established an Improvement Board to action Ofsted's recommendations

On the basis of our work, and having regard to the guidance on the specified criteria published by the Audit Commission, with the exception of the matters reported in the basis for qualified conclusion paragraph above, 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 ending 31 March 2015. Our judgement is based on the outcome of Ofsted's inspection and not on any further work performed by ourselves in respect of children's services.

We set out below our detailed findings against six risk areas which have been used to assess the Council's performance against the Audit Commission's criteria. We summarise our assessment of each risk area using a red, amber or green (RAG) rating, based on the following definitions:

Green	Adequate arrangements
Amber	Adequate arrangements, with areas for development
Red	Inadequate arrangements

The table below and overleaf summarises our overall rating for each of the themes reviewed:

Theme	Summary findings	RAG rating 2013/14	RAG rating 2014/15
Key indicators of performance	<p>The Council achieved an underspend of £13m against its revenue budget in 2014/15 and of £10.2m on its re-profiled capital budget of £209.5m. For 2014/15 the Council had a savings target of £72.3m, and achieved efficiencies and savings of £74.1m.</p> <p>As at 31 March 2015 the Council has net liabilities of £206m (net liabilities of £127m as at 31 March 2014 and net assets of £79m as at 31 March 2013). The increase in net liabilities is due to the increase in the pension fund liability as a result of falling real bond yields.</p> <p>A specific policy statement on reserves and balances was presented to the Cabinet at its meeting on 3 February 2015. This report advised that it was considered prudent to maintain a minimum level of available general balances of between 2.0% to 2.5% of the sum of council tax plus settlement funding i.e. between £16m and £20m. In terms of addressing the specific point regarding pension fund liabilities raised in our 2013/14 VfM report, the Council has this year established a pensions stabilisation reserve within earmarked reserves of £1.1m. This was set aside to meet the increases in back funding that the Council anticipates for 2015/16.</p>	Green	Green

Theme	Summary findings	RAG rating 2013/14	RAG rating 2014/15
Strategic financial planning	<p>The Medium Term Financial Plan presented to the Cabinet in February 2015 estimated that the total savings identified for the period 2015/16 to 2019/20 were £147m, of which £67.3m were due for 2015/16. At that time officers recognised that there were a number of uncertainties, such as the result of the General Election, which could have a significant impact on future funding streams and hence the level of savings and efficiencies required. It was agreed that a refresh of the MTFP would take place in summer 2015, and this is currently in progress. Early indications are that increasing demand, together with cost and funding pressures may require the level of savings over the next 5 years to rise to £320m unless additional funding sources can be identified.</p> <p>The Council has satisfactorily implemented the recommendations we raised in our 2013/14 VfM report and the implications of the Care Act and the Better Care Fund plans for Surrey are reflected in the MTFP. An additional £18.2m is included in the 2015/16 revenue budget to cover the Council's responsibilities in respect of the Care Act, Independent Living Fund and Public Health. Internal Audit's reviews of Care Act Preparedness and Preparation for the Better Care Fund concluded that the Council's arrangements were effective.</p> <p>The demand for school places is continuing to rise and this is reflected in the Council's capital programme, which includes £289.9m on Schools Basic Need over the 5 year period. The Council has been successful in its applications for Schools Basic Needs top-up grants (£41.3m) and increases to Schools Basic Need funding and Schools Maintenance Capital funding.</p> <p>We recommend the Council build on the lessons it has learned from previous successful efficiency programmes to address the increasing financial challenges it faces.</p>	Green	Green
Financial governance	<p>Progress is being made in embedding use of the finance dashboards, including the cultural change required within the central finance team in terms of relinquishing responsibility for budget monitoring and moving this out to budget holders. The final sessions of the forecasting tool roll-out took place in May and July 2014 and the financial management training pathway has just been launched.</p> <p>The Council has embraced early close down, and reported its 2014/15 outturn position in April 2015, a month earlier than in 2013/14.</p>	Green	Green
Financial control	<p>The Council has taken positive action to address the recommendation we raised in our 2013/14 VfM report in respect of its arrangements for project managing and profiling capital expenditure and presented an update report to the Audit & Governance Committee meeting on 9 April 2015.</p> <p>Property Services has reviewed its procedures for profiling capital spend and the way that it forecasts this spend in year. The service held a workshop on 8 July 2014 to investigate the reasons for the slippage and identified the following: planning permission, intrusive investigations and severe weather. The service has also improved the robustness of the challenge of forecasts made by the senior management team and documented the procedures that need to be followed to ensure good capital profiling and monitoring.</p>	Green	Green

Theme	Summary findings	RAG rating 2013/14	RAG rating 2014/15
Prioritising resources	<p>The Council continues to demonstrate a sound understanding of the main risks it faces, which relate to failure to achieve the MTFP, safeguarding in children's services and adult social care, central government policy development, integration of health and social care, and the 2015 Comprehensive Spending Review.</p> <p>In our 2013/14 VfM report we commented that information governance was a high risk area and that significant further work was required to raise awareness of the risks across the organisation. The Council has now implemented its action plan and Internal Audit's follow up report in December 2014 gave an overall green assessment.</p>	Green	Green
Improving efficiency & productivity	<p>The Council invited OFSTED to carry out an inspection of its children's services based on the new multi-agency framework , following a reorganisation of its children in need teams and the establishment of the referral, assessment and intervention service (RIAS). OFSTED undertook its review in October and November 2014. Its report was published on 3 June 2015 with the overall judgement that children's services are inadequate. It states that 'there are widespread and serious failures that potentially leave children at risk of harm.' The main failing relates to the lack of management oversight of cases which were stepped down, with the risk that children do not receive the services that they need. The Council accepts this finding.</p> <p>An action plan was developed as soon as the inspection had concluded. This was divided into immediate short-term actions to correct failings, and longer-term more sustainable solutions. The formal action plan is currently being developed with support from the Department for Education and will be submitted to OFSTED within the required timeframe. The Strategic Director, Business Services, has taken on an interim role as Deputy Chief Executive and also assumed strategic responsibility for Children, Schools and Families with effect from June 2015.</p> <p>Progress is reported to the Improvement Board, which has met fortnightly since December. Membership of the Board consists of the Leaders of each political party on the Council.</p> <p>Having considered the work undertaken by OFSTED we have concluded that the arrangements for promoting and demonstrating the principles and values of good governance within children's services are inadequate. We are satisfied from our overall review of the Council that the arrangements in respect of other services, including its Local Authority Trading Companies (S.E. Business Services Ltd. and Surrey Choices Ltd.) are adequate. We propose to issue a qualified 'except for' value for money conclusion.</p>	Green	Red
Management of natural resources	<p>The Council continues to progress the development of the Eco Park as a key aspect of its waste strategy. Having satisfied itself that all necessary preconditions, including the value for money criterion, have been met, the Cabinet approved the issue of the second notice to proceed on 28 April 2015.</p>	Green	Green

To support our VfM conclusion against the specified criteria we performed a risk assessment against VfM risk indicators specified by the Audit Commission, and additional indicators identified by ourselves. Following completion of our work we noted the following residual risk to our VfM conclusion:

Residual risk identified	Summary findings
Identification of sustainable long term savings	As highlighted above, the current refresh of the Medium Term Financial Plan has indicated that the level of savings that the Council is required to make over the next 5 years may more than double from £147m to £320m. The Council needs to build on the lessons it has learned from previous successful efficiency programmes to address the increasing financial challenges it faces.

Section 4: Fees, non-audit services and independence

- 01. Executive summary
- 02. Audit findings
- 03. Value for Money
- 04. Fees, non-audit services and independence**
- 05. Communication of audit matters

Fees, non-audit services and independence

We confirm below our final fees charged for the audit and confirm there were no fees for the provision of non audit services.

Fees

	Initial Audit plan £	Revised Plan £	Actual fees £
Council audit	189,464	189,464	189,464
S. E. Business Services Limited *	TBC	15,000	15,000
Surrey Choices Limited *	TBC	9,000	9,000
Total audit fees	189,464	213,464	213,464

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 Standards and therefore we 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 Auditing Practices Board's Ethical Standards.

* S. E. Business Services Limited and Surrey Choices Limited: Work still in progress.

Fees for other services

Service	Fees £
Audit related services	
Certification of Teachers' Pensions return*	TBC
Non audit related services	Nil

*We have not yet agreed with the Council terms of engagement in relation to this work, nor the fee.

Section 5: Communication of audit matters

- 01. Executive summary
- 02. Audit findings
- 03. Value for Money
- 04. Fees, non-audit services and independence
- 05. Communication of audit matters

Communication of audit matters to those charged with governance

International Standard on Auditing ISA (UK&) 260, as well as other (UK&I) ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table opposite.

The Audit Plan outlined our audit strategy and plan to deliver the audit, while this Audit Findings report presents the key issues and other matters arising from the audit, together with an explanation as to how these have been resolved.

Respective responsibilities

The Audit Findings Report has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission (www.audit-commission.gov.uk).

We have been appointed as the Council's independent external auditors by the Audit Commission, the body responsible for appointing external auditors to local public bodies in England. As external auditors, we have a broad remit covering finance and governance matters.

Our annual work programme is set in accordance with the Code of Audit Practice (the Code) issued by the Audit Commission and includes nationally prescribed and locally determined work. Our work considers the Council's key risks when reaching our conclusions under the Code.

It is the responsibility of the Council to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the Council is fulfilling these responsibilities.

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance	✓	
Overview of the planned scope and timing of the audit. Form, timing and expected general content of communications	✓	
Views about the qualitative aspects of the entity's accounting and financial reporting practices, significant matters and issues arising during the audit and written representations that have been sought		✓
Confirmation of independence and objectivity	✓	✓
A statement that we have complied with relevant ethical requirements regarding independence, relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged Details of safeguards applied to threats to independence	✓	✓
Material weaknesses in internal control identified during the audit		✓
Identification or suspicion of fraud involving management and/or others which results in material misstatement of the financial statements		✓
Compliance with laws and regulations		✓
Expected auditor's report		✓
Uncorrected misstatements		✓
Significant matters arising in connection with related parties		✓
Significant matters in relation to going concern		✓
Matters in relation to the Group audit, including: Scope of work on components, involvement of group auditors in component audits, concerns over quality of component auditors' work, limitations of scope on the group audit, fraud or suspected fraud	✓	✓

Page 248
Appendices

Appendix A: Action plan

The following recommendations have been agreed with management:

Rec No.	Recommendations for 2015/16	Priority	Management response	Implementation date & responsibility
1	Obtain legal advice to ensure that the approach taken to the de-recognition of schools and the use of the statutory override is appropriate.	High	This issue represents a significant financial risk to the council in future years. The council will seek legal advice on the appropriateness of the statutory override	Deputy Chief Finance Officer December 2015
2	Ensure the accounts fully disclose all key judgements made in applying its accounting policies and the rationale for determining them.	Medium	Managers concur that the accounts fully disclose all judgements, and their rationale	Principal Accountant – Financial Accounting May 2016
3	Undertake a review of the 2014/15 closedown and identify areas where the timeliness of response to audit queries can be improved.	Medium	The Closing Working Group will develop plans to more effectively communicate the importance of the timeliness of response to audit queries	Principal Accountant – Financial Accounting
4	Build on the lessons learned from previous successful efficiency programmes to address the increasing financial challenges it faces.	Medium	Officers will develop further service transformational strategies necessary for the council to meet its financial challenges and prepare a draft Medium Term Financial Plan 2016 to 2021 for the Cabinet Meeting in November 2015	Director of Finance November 2015

Appendix B: Audit opinion

We anticipate we will provide the Council with an unqualified opinion on its financial statements and a modified value for money conclusion

DRAFT INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SURREY COUNTY COUNCIL

We have audited the financial statements of Surrey County Council for the year ended 31 March 2015 under the Audit Commission Act 1998. The financial statements comprise the Movement in Reserves Statement, the Group Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Group Comprehensive Income and Expenditure Statement, the Balance Sheet, the Group Balance Sheet, the Cash Flow Statement, the Group Cash Flow Statement, the annex containing the accounting policies, and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2014/15.

This report is made solely to the members of Surrey County Council, as a body, in accordance with Part II of the Audit Commission Act 1998 and as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010. Our audit work has been undertaken so that we might state to the members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Director of Finance and auditor

As explained more fully in the Statement of Responsibilities, the Director of Finance is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2014/15, and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards also require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority's and Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance; and the overall

presentation of the financial statements. In addition, we read all the financial and non-financial information in the explanatory foreword and the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the financial position of Surrey County Council as at 31 March 2015 and of its expenditure and income for the year then ended;
- give a true and fair view of the financial position of the Group as at 31 March 2015 and of its expenditure and income for the year then ended; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2014/15 and applicable law.

Opinion on other matters

In our opinion, the information given in the explanatory foreword and the Annual Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we report by exception

We are required to report to you if:

- in our opinion the annual governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007; or
- we issue a report in the public interest under section 8 of the Audit Commission Act 1998; or
- we designate under section 11 of the Audit Commission Act 1998 a recommendation as one that requires the Authority to consider it at a public meeting and to decide what action to take in response; or
- we exercise any other special powers of the auditor under the Audit Commission Act 1998.

We have nothing to report in these respects.

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

Respective responsibilities of the Authority and the auditor

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

We are required under Section 5 of the Audit Commission Act 1998 to satisfy ourselves that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires us to report to you our conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission in October 2014.

We report if significant matters have come to our attention which prevent us from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We are not required to consider, nor have we considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

We have undertaken our review in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2014, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for us to consider under the Code of Audit Practice in satisfying ourselves whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2015.

We planned our work in accordance with the Code of Audit Practice. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Basis of qualified conclusion

In seeking to satisfy ourselves that the Authority has made proper arrangements for challenging how it secures economy, efficiency and effectiveness in its use of resources, we have considered reports issued by other regulators. An Ofsted inspection report published in June 2015 concluded that the overall arrangements for Children's Services in the Surrey County Council area were judged to be 'inadequate'. This judgement is evidence of weaknesses in the Authority's arrangements for promoting and demonstrating the principles and values of good governance within the Council's Children's Services directorate.

Qualified conclusion

On the basis of our work, and having regard to the guidance on the specified criteria published by the Audit Commission in October 2014, with the exception of the matter reported in the basis for qualified conclusion paragraph above, we are satisfied that in all significant respects Surrey County Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2015.

Delay in certification of completion of the audit

We are required to give an opinion on the consistency of the pension fund financial statements of Surrey County Council included in the Pension Fund Annual Report with the pension fund financial statements included in the Statement of Accounts. The Local Government Pension Scheme Regulations 2013 require authorities to publish the Pension Fund Annual Report by 1 December 2015. As the Authority has not prepared the Pension Fund Annual Report at the time of this report we have yet to issue our report on the consistency of the pension fund financial statements. Until we have done so, we are unable to certify that we have completed the audit of the financial statements in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission.

We cannot formally conclude the audit and issue an audit certificate until we have completed the work necessary to issue our assurance statement in respect of the authority's Whole of Government Accounts consolidation pack. We are satisfied that this work does not have a material effect on the financial statements or on our value for money conclusion.

Andy Mack
for and on behalf of Grant Thornton UK LLP, Appointed Auditor
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DRAFT July 2015



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