

DERBYSHIRE COUNTY COUNCIL

AUDIT COMMITTEE

27 February 2019

Report of the Director of Finance & ICT

**EXTERNAL AUDIT ISA 260 REPORT 2017-18 - UPDATE ON
RECOMMENDATIONS**

1 Purpose of the Report

This report provides Members with an update of the actions taken in response to the external audit recommendations outlined in the External Audit ISA 260 Report 2017-18.

2 Information and Analysis

The external auditor presented its External Audit ISA 260 Report 2017-18 at the Audit Committee meeting on 26 July 2018. The external auditor again acknowledged the good accounts production process, the quality of supporting working papers with clear audit trails and the responsiveness of the finance teams and others during the audit, with officers dealing efficiently, promptly and helpfully with audit queries.

Audit adjustments were required to the Statement of Accounts in respect of Property, Plant and Equipment values, as indexation in relation to property valuation was not correctly applied. An oversight in the preparation of the valuation working papers was identified by internal audit, after the pre-audit statement of accounts had been issued. Audit work was completed to reach a conclusion that there were no unadjusted material errors.

The external auditor observed that 2017-18 property revaluation work was not progressed in a timely manner, which increased pressure on finance, internal audit and external audit to complete work on the statement of accounts associated with it. A detailed update on the actions being taken, in response to the valuation process control recommendations and two additional recommendations, is attached at Appendix One.

The external auditor also revisited recommendations from 2016-17, when four recommendations were raised. They concluded that the majority of the

recommendations relating to the financial statements were implemented in accordance with the timescales of the action plan, except for the recommendation in respect of property revaluation work because the 2017-18 revaluation was not progressed in a timely manner, as referred to above. An update on the action being taken in respect of the external auditor's revisit of 2016-17 recommendations is attached at Appendix Two.

The External Audit ISA 260 Report 2017-18 is attached at Appendix Three.

3 Considerations

In preparing this report the relevance of the following factors has been considered:- financial, human resources, legal and human rights, equality of opportunity, health, environmental, transport, property, crime and disorder and social value considerations.

4 Background Papers

Copies of the approved Statement of Accounts are held in Technical Section, Corporate Finance & ICT.

5 Officer's Recommendation

That Audit Committee notes the actions being taken in response to the external audit recommendations outlined in the External Audit ISA 260 Report 2017-18.

PETER HANDFORD

Director of Finance & ICT

2017-18 Recommendations

Recommendation	Management Response	Responsible Officer	Due date	Update
<p>Controls in place in regard to the valuation process</p> <p>Ensure that valuation work is completed and appropriately checked on a timely basis to enable accurate entries to be made in the pre-audit statement of accounts.</p>	<p>The full year impact of additional staffing resources, aligned with an earlier start date for the valuation work compared to 2017-18, will ensure that the property valuations are completed in a timely manner.</p> <p>Alongside additional validation checks, it is expected that the resulting data will be of the right quality for the accounts, in line with the requirements set out in the terms of engagement agreed between the Property and Finance & ICT Divisions. These processes will be documented in the Valuations Procedure Manual.</p>	Sarah Morris	Dec 2018	<p>The Asset Valuation manual has been updated to set out the checks and controls now used by the Asset Valuers in preparing their valuations. These include a stepped checking process and counter sign-off.</p> <p>Data prepared by third parties, for example Children's Services and Quantity Surveyors, is also validated and signed off by the respective 'owner', prior to it being utilised by the Valuation team. These measures will ensure that data of the right quality is used to produce the asset valuations.</p> <p>The manual is a living document and is updated each year, following publication of the accounts, with any improvements identified during the course of the valuation process for the preceding year.</p> <p>The start date to commence the 20% valuations is being brought forward to earlier in the year, to ensure that the stringent timescales set out in the Terms of Reference are achieved.</p>
<p>Controls in place in relation to SAP users with privileged access</p> <p>Implement controls to ensure: the activities of SAP users with privileged access can be monitored; appropriate segregation of duties is achieved; and access rights are withdrawn when individuals leave.</p>	<p>Agreed.</p> <p>Table logging – log T000 – will be switched on to record when SAP Production systems are opened.</p> <p>The number of users with privileged access has been reduced to four from eleven. Any change to the status of users with these privileged access will be actively managed by senior finance staff.</p> <p>Starters and Leavers process has been automated around payroll information.</p>	Wayne Sutton	Sep 2018	<p>Table logging was activated on the 6 October 2018.</p> <p>The number of users with privileged access was reduced from eleven to four on 22 May 2018. The four remaining staff require the privileged access to enable them to fulfil their duties and provide adequate system support.</p> <p>The starters and leavers process is automated around payroll information.</p>

2017-18 Recommendations

Recommendation	Management Response	Responsible Officer	Due date	Update
Financial Standing The Authority should constantly refresh savings plans to ensure they are achievable as well as minimise overspends against budget to reduce further savings required.	<p>Agreed, regular budget monitoring reporting at all levels within the organisation will contain updates on savings plans and provide a focus for holding budget holders to account for overspending.</p> <p>The Five Year Financial Plan will be updated over Summer 2018 and members and officers will work together to produce a set of proposals that will balance the budget over the medium term.</p>	Peter Handford	Sep 2018	<p>Audit Committee, Cabinet and Council Budget Monitoring Reports in 2018-19 have included updates on the achievement of in-year savings plans for all the Council's portfolios.</p> <p>Departmental Finance Officers have met with the S151 Finance Officer on a scheduled basis, throughout the year, to discuss their departmental budget monitoring position.</p> <p>The Five Year Financial Plan (FYFP) 2018-19 to 2022-23 was updated in Summer 2018 and taken to the Cabinet meeting on 20 September 2018. The FYFP 2019-20 to 2023-24 was prepared and approved by Council on 6 February 2019.</p> <p>The Budget Strategy Group, at which all departments are represented, has met regularly during the year, to report on and consider progress in respect of achievement of savings forecast in the FYFP.</p> <p>Reports have also been presented to Cabinet/CMT meetings during 2018-19 on Budget Prioritisation, Savings and Service Pressures, on Financial Resilience and on the Council's Plan for Achievement of Savings.</p>

2016-17 Recommendations – Update

Recommendation	Management Response	Responsible Officer	Update
<p>Controls in place in regard to valuation process</p> <p>In future years, management should obtain sufficient assurance as to the valuation of its asset base in advance of the final accounts audit.</p>	<p>Progress has been made in relation to capacity issues, terms of reference, asset notification changes (AMP1 forms) and other detailed issues. However, valuation work is still not being carried out on a timely basis that allows for appropriate checking to ensure accurate entries are made in the pre-audit statement of accounts.</p>	<p>Sarah Morris</p>	<p>The Council has now fully recruited to its in-house valuation team. The team is also supported, when required, by the addition of extra specialist capacity from an external framework arrangement. This has enabled asset valuations in 2018-19 to be completed on a timely basis, allowing sufficient time for appropriate checking, as set out in the valuation manual.</p>
<p>Implementation of Pensions Administration System</p> <p>We recommend the Authority continue to progress this matter and report to the Audit Committee on this issue.</p>	<p>There has been improvement during 2017-18, however with the demands on resources created by the migration to a new pensions administration system in 2018 and the impact of the LGPS Amendment Regulations in May 2018, it is not expected that the current rate of improvement will be maintained.</p>	<p>Dawn Kinley/ Nigel Dowey</p>	<p>A new Pension Administration System has been jointly procured with Leicestershire County Council and the contract for the new system was signed in June 2018. A comprehensive project governance regime was established to support the implementation of the new system and the “Go Live” date is 4 March 2019.</p>



Appendix 1

External Audit ISA260 Report 2017/18

**Derbyshire County Council
& Derbyshire Pension Fund**

July 2018

Summary for Audit Committee

This document summarises the key findings in relation to our 2017/18 external audit at Derbyshire County Council ('the Authority') and Derbyshire Pension Fund.

This report covers both our on-site work which was completed in February and June/July on the Authority and Pension Fund's significant risk areas, as well as other areas of your financial statements, and the control environment in place to support the production of timely and accurate financial statements. Our findings are summarised below.

Organisational and IT control environment

We have raised a recommendation relating to the Authority and Pension Fund's SAP IT control environment. This relates to the use of the logging facility, separation of duties and access rights for privileged users and can be found in Appendix 1.

Controls over key financial systems

Aside from the issues arising from the work completed with regard to the valuation of PPE we have only noted one other ongoing improvement point which relates to the operation of the Pension Administration system (see Appendix 2 for details).

Review of internal audit

We have reviewed internal audit's reports throughout the year to inform ourselves of any significant risks in relation to our opinion work. However, there have been no specific instances where we have sought to rely on the work of internal audit.

Accounts production

The Authority has good processes in place for the production of the accounts and good quality supporting working papers. Officers dealt efficiently and helpfully with audit queries.

Financial statements

Subject to all outstanding queries being resolved to our satisfaction we anticipate issuing an unqualified audit opinion on the Authority's financial statements before the deadline of 31 July 2018.

Based upon our initial assessment of risks to the financial statements (as reported to you in our *External Audit Plan 2017/18* and updated during our audit) we identified the following significant risks (excluding those mandated by International Standards on Auditing – see Page 9 for details):

- **Valuation of PPE** – In the prior year we reported significant issues with regard to PPE valuation which led to material amendments to the accounts. Whilst progress has been made, indexation was not correctly applied in the 2017/18 valuation work leading to material amendments to the 2017/18 accounts. The work in regard to resolving the PPE valuation issues faced in 2017/18 has led to significant extra work by both the audit team and officers of the authority; and
- **Pensions Liabilities** – There is a risk that the assumptions and methodology used in the valuation of the Authority's pension obligation are not reasonable. Our work on this has not identified any significant matters which we need to draw to your attention.

We have identified one major property value audit adjustment with a total value of £126 million and there were other minor amendments. These have some impact on revenue, see page 29 for details. The adjustments involved resulted in a net increase of £6.2 million in reported expenditure but no impact on the general fund balance.

Based on our work, we have raised 3 recommendations. Details of our recommendations can be found in Appendix 1. We are now in the completion stage of the audit and anticipate issuing our completion certificate and Annual Audit letter after our work on WGA is completed.

Summary for Audit Committee (cont.)

Pension Fund financial statements

We also anticipate issuing an unqualified audit opinion in relation to the Pension Fund's financial statements by 31 July 2018.

Based upon our initial assessment of risks to the Pension Fund financial statements (as reported to you in our *External Audit Plan 2017/18* and updated during our interim visit) we have identified the following significant risk (excluding those mandated by International Standards on Auditing – see Page 9 for details):

- **Valuation of hard to price investments** – The pricing of complex investment assets may be susceptible to pricing variances given the number of assumptions underlying the valuation. Our work on this did not identify any significant matters which we need to draw to your attention.

Value for money arrangements

We have completed our risk-based work to consider whether in all significant respects the Authority has proper arrangements to ensure it has taken properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. We have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We therefore anticipate issuing an unqualified value for money opinion.

We set out our assessment of those areas requiring additional risk based work in our *External Audit Plan 2017/18* and have updated this assessment during our interim visit. As a result of this we identified the following significant VFM audit risk:

- **Delivery of Budgets** – The Authority identified the need to make savings of £34 million during the 2017/18 financial year. The latest Medium Term Financial Plan identifies a further saving requirement of £52.9m in the period 2018/19 - 2022/23. The need for savings will continue to have a significant impact on the Authority's financial resilience. Our work on this has not identified any significant matters which we need to draw to your attention other than the ongoing importance of making the savings required. With this in mind we have made a recommendation that the Authority should constantly refresh savings plans to ensure they are achievable as well as minimise overspends against budgets to reduce the further savings required.

See further details on pages 22 and 23.

Exercising of audit powers

We have a duty to consider whether to issue a report in the public interest about something we believe the Authority should consider, or that the public should know about.

We have not identified any matters that would require us to issue a public interest report.

In addition, we have not had to exercise any other audit powers under the Local Audit & Accountability Act 2014.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and support in relation to our work.

Section one

Control Environment



Organisational and IT control environment

We have identified no fundamental issues with the Authority's organisational and IT control environment and consider that the overall arrangements that have been put in place are reasonable.

Despite this, we have noted a number of areas for further improvement:

- **the SAP logging facility is not currently being used, so there is no way of monitoring the activities of privileged users;**
- **a number of privileged users have access to both develop and implement changes in SAP; and**
- **leavers with privileged access were still active on the SAP system.**

Work completed

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit. We obtain an understanding of the Authority's overall control environment and determine if appropriate controls have been implemented. We do not complete detailed testing of these controls.

The Authority relies on information technology ("IT") to support both financial reporting and internal control processes. In order to satisfy ourselves that we can rely on the use of IT, we test controls over access to systems and data, system changes, system development and computer operations.

Key findings

We consider that your organisational and IT controls are effective overall, but noted a number of areas for further improvement:

- Issue 1: the SAP logging facility is not currently being used, so there is no way of monitoring the activities of privileged users;
- Issue 2: a number of privileged users have access to both develop and implement changes in SAP; and
- Issue 3: leavers with privileged access were still active on the SAP system.

These weaknesses meant that we needed to alter our audit strategy in relation to the testing of information produced by the entity. This involved additional substantive testing at the year-end.

A recommendation regarding these matters is included in Appendix 1.

Controls over key financial systems

The controls over the majority of the key financial systems are sound.

However, there are weaknesses in respect of the valuation of PPE

We needed to complete additional substantive work on the valuation of PPE at the year-end.

Work completed

We review the outcome of internal audit's work on the financial systems to influence our assessment of the overall control environment, which is a key factor when determining the external audit strategy.

Where we have determined that this is the most efficient audit approach to take, we evaluate the design and implementation of the control and then test selected controls that address key risks within these systems. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

Our assessment of a system will not always be in line with your internal auditors' opinion on that system. This is because we are solely interested in whether our audit risks are mitigated through effective controls, i.e. whether the system is likely to produce materially reliable figures for inclusion in the financial statements.

Key findings

Based on our work we have determined that the controls over the majority of the key financial systems are sound.

However, we noted some weaknesses in respect of individual financial systems that impacted on our audit:

- Weakness 1: indexation was not correctly applied in the 2017/18 valuation work leading to material amendments to the 2017/18 accounts. This issue with regard to PPE valuation has led to significant extra work by both the audit team and officers of the Authority; and
- Weakness 2: the 2017/18 property revaluation work was not progressed in a timely manner. This increased the pressure on finance, internal audit and ourselves to complete our associated work for 2017/18.

Internal audit have included associated recommendations on the PPE valuation process in their reports as appropriate.

A recommendation relating to these weaknesses in the PPE valuation process is included in Appendix 1.

An overhead photograph of four business professionals (three women and one man) seated around a white conference table. They are dressed in business attire (white shirts, light blue shirts, and a grey top). The table has two laptops and a black folder. The scene is brightly lit with natural light from windows on the right, creating strong shadows. A blue horizontal band is overlaid across the middle of the image, containing the text.

Section two

Financial Statements

Accounts production and audit process

Audit standards (ISA 260) require us to communicate our views on the significant qualitative aspects of the Authority’s accounting practices and financial reporting.

We also assessed the Authority’s process for preparing the accounts and its support for an efficient audit. The efficient production of the financial statements and good-quality working papers are critical to meeting the tighter deadlines.

The Authority’s overall process for the preparation of the financial statements is good.

The Authority has implemented the majority of the recommendations in our *ISA 260 Report 2016/17*.

Accounts practices and production process

The Authority incorporated a number of measures into its closedown plan to further improve the project management of this complex process. Specifically, the Authority recognised the additional pressures which the earlier closedown brought and we engaged with officers in the period leading up to the year end in order to proactively address issues as they emerged.

We consider that the overall process for the preparation of your financial statements is good. We also consider the Authority’s accounting practices appropriate.

Going concern

The financial statements of both the Authority and the Pension Fund have been prepared on a going concern basis. We confirm that we have identified no significant matters which would, in our view, affect the ability of the Authority or Pension Fund to continue as a going concern.

Further commentary on the Authority’s arrangements in place to secure the effective delivery of budgets is included on pages 22 and 23.

Implementation of recommendations

We raised 4 recommendations in our ISA 260 Report 2016/17. The Authority has implemented the majority of the recommendations relating to the financial statements in line with the timescales of the action plan. One exception to this relates to the 2017/18 property revaluation work not being progressed in a timely manner. This increased the pressure on finance, internal audit and ourselves to complete our associated work for 2017/18. The table below sets out the Authority’s progress against this high priority recommendation. Further details are included in Appendix 2.

Issue	Progress
<p>A large number of issues were noted as part of our 2016/17 work on the valuation of PPE held on the balance sheet. The initial trigger for this work was an audit request for information to explain all changes in asset values of over £2million.</p> <p>This then highlighted that a large number of these changes were due to errors in the calculation basis in either 2015/16 or 2016/17. For each of these issues audit work was completed to reach a conclusion that there is no unadjusted material error – however in future years management should obtain sufficient assurance as to the valuation of its asset base in advance of the final accounts audit.</p>	<p>Whilst some progress has been made, delays were experienced in obtaining sufficient assurance and indexation was not correctly applied in the 2017/18 valuation work. This led to material amendments to the 2017/18 accounts. The work with regard to PPE valuation has led to significant extra work by both the audit team and officers of the authority</p>

Accounts production and audit process (cont.)

Completeness of draft accounts

We received a complete set of draft accounts on 30 May 2018, which was in advance of the statutory deadline.

Quality of supporting working papers

We issued our Final Accounts Audit Protocol to the Finance Manager on 21 March 2018. This important document sets out our audit approach and timetable. It also summarises the working papers and other evidence we require the Authority to provide to support our audit work. This helps the Authority and the Pension Fund to provide audit evidence in line with our expectations. We worked with management to ensure that working paper requirements were understood and aligned to our expectations. We are pleased to report that this has resulted in good quality working papers with clear audit trails.

Response to audit queries

We are pleased to report that our agreed turnaround time for dealing with audit queries was achieved by officers, including those who are not part of the finance team.

Pension Fund audit

The audit of the Fund was completed alongside the main audit. There are no specific matters to bring to your attention relating to this.

Specific audit areas

We anticipate issuing an unqualified audit opinion on the Authority's 2017/18 financial statements and those of the Pension Fund by 31 July 2018.

Auditing standards require us to consider two standard risks for all organisations. We consider these as a matter of course in our audit and will have set out the findings arising from our work in our ISA 260 Report below.

Management override of controls

01

Professional standards require us to communicate the fraud risk from management override of controls as significant because management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Our audit methodology incorporates the risk of management override as a default significant risk. We have not identified any specific additional risks of management override relating to this audit.

In line with our methodology, we carried out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.

There are no matters arising from this work that we need to bring to your attention.

02

Fraudulent revenue recognition

Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk.

In our *External Audit Plan 2017/18* we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.

This is still the case. Since we have rebutted this presumed risk, there has been no impact on our audit work.

Over the following pages we have set out our assessment of the specific significant risks and areas of audit focus we identified in relation to the audit of the Authority's financial statements and those of the Pension Fund.

Specific audit areas

Significant Audit Risks – Authority

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error in relation to the Authority.

Risk:	Valuation of PPE <p>The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Authority has adopted a rolling revaluation model which sees all land and buildings revalued over a five year cycle. As a result of this, however, individual assets may not be revalued for four years.</p> <p>This creates a risk that the carrying value of those assets not revalued in year differs materially from the year end fair value. In the prior year we reported significant issues in regard to the PPE valuation which led to material amendments to the accounts.</p>
Our assessment and work undertaken:	<p>We reviewed the approach that the Authority adopted to assess the risk that assets not subject to valuation are materially misstated and considered the robustness of that approach. We also assessed the risk of the valuation changing materially during the year.</p> <p>In addition, we considered movements in market indices between revaluation dates and the year end in order to determine whether these indicate that fair values have moved materially over that time.</p> <p>In relation to those assets which have been revalued during the year we reviewed the accounting entries made to record the results of the revaluation in order to ensure that they were appropriate.</p> <p>We also assessed the valuer’s qualifications, objectivity and independence to carry out such valuations and reviewed the methodology used (including testing the underlying data and assumptions).</p> <p>During a review of the valuation process internal audit noted that indexation was not correctly applied in the 2017/18 valuation work. This led to material amendments to the 2017/18 accounts being required. We have set out our view of the assumptions used in relation to accounting for Property, Plant and Equipment at page 14.</p>

Specific audit areas (cont.)

Significant Audit Risks – Authority (cont.)

Risk:	<p>Pension Liabilities</p> <p>The net pension liability represents a material element of the Authority’s balance sheet. The Authority is an admitted body of the Derbyshire County Council Pension Fund (the Pension Fund), which had its last triennial valuation completed as at 31 March 2016. This forms an integral basis of the valuation as at 31 March 2018.</p> <p>The valuation of the Local Government Pension Scheme relies on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which results in the Authority’s overall valuation.</p> <p>There are financial assumptions and demographic assumptions used in the calculation of the Authority’s valuation, such as the discount rate, inflation rates, mortality rates etc. The assumptions should also reflect the profile of the Authority’s employees, and should be based on appropriate data. The basis of the assumptions is derived on a consistent basis year to year, or updated to reflect any changes.</p> <p>There is a risk that the assumptions and methodology used in the valuation of the Authority’s pension obligation are not reasonable. This could have a material impact to net pension liability accounted for in the financial statements.</p>
Our assessment and work undertaken:	<p>As part of our work we reviewed the controls that the Authority has in place over the information sent to the scheme actuary, including the Authority’s process and controls with respect to the assumptions used in the valuation. We also evaluated the competency, objectivity and independence of Hymans Robertson LLP.</p> <p>We reviewed the appropriateness of the key assumptions included within the valuation, compared them to expected ranges, and involved a KPMG Actuary to provide a specialist assessment of those assumptions. We also reviewed the methodology applied in the valuation by Hymans Robertson LLP.</p> <p>In addition, we reviewed the overall actuarial valuation and considered the disclosure implications in the financial statements.</p> <p>In order to determine whether the net pension liability has been appropriately accounted for we also considered the valuation of pension assets. As part of our audit of the Pension Fund we gained assurance over the overall value of fund assets. We then liaised with the actuary to understand how these assets are allocated across participating bodies and re-performed this allocation.</p> <p>We have no issues to report as a result of our work in this area.</p> <p>We have set out our view of the assumptions used in valuing pension assets and liabilities at page 14.</p>

Specific audit areas (cont.)

Significant Audit Risks – Pension Fund

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error in relation to the Pension Fund.

Risk:	<p>Valuation of hard to price investments</p> <p>The Pension Fund invests in a wide range of assets and investment funds, some of which are inherently harder to value or do not have publicly available quoted prices, requiring professional judgement or assumptions to be made at year end. The pricing of complex investment assets may also be susceptible to pricing variances given the number of assumptions underlying the valuation.</p>
Our assessment and work undertaken:	<p>As part of our audit of the Pension Fund, we independently verified a selection of investment asset prices to third party information and obtained independent confirmation on asset existence. We also tested the extent to which the Pension Fund had challenged the valuations reported by investment managers for harder to price investments and obtained independent assessment of the figures.</p> <p>We have no issues to report as a result of our work in this area.</p>

Specific audit areas (cont.)

Other areas of audit focus

Those risks with less likelihood of giving rise to a material error but which are nevertheless worthy of audit understanding.

Issue:	Implementation of Previous Recommendations Recommendations were made in our 2016/17 audit findings report in relation to PPE valuations and embedding the pension fund administration system.
Our assessment and work undertaken:	We have followed up our prior year recommendations with the finance team and reported on the progress made regarding the implementation of the recommendations in Appendix 2. The Authority has implemented the majority of the recommendations relating to the financial statements in line with the timescales of the action plan. The exception to this relates to the 2017/18 property revaluation work not being progressed in a timely manner.

Issue:	Related Party Transactions Under accounting standards and the Code the Authority is required to list all transactions and outstanding balances with related parties in a note to the financial statements. Due to the establishment of subsidiary entities this disclosure is likely to require more detail than previously shown.
Our assessment and work undertaken:	We reviewed the process and controls in place to gather this information and reviewed the disclosures made within the financial statements. We also completed a review of a sample of the returns made by individual officers and Councillors and checked for payments made to any interest declared. We have no issues to report as a result of our work in this area.

Issue:	Group Accounts During the year a subsidiary of the Authority (Derbyshire Developments Ltd) has become operational and is preparing financial statements. Accounting standards and the Code of Practice both require each subsidiary to be accounted for and, if required, group accounts prepared. Should group accounts be prepared then additional disclosures are required within the financial statements. The Authority decided not to produce group accounts on the grounds of materiality and this judgement has been documented and explained within the narrative report.
Our assessment and work undertaken:	We reviewed the assessment made by the Authority with regard to group accounts and carried out work on each subsidiary to gain assurance that each body has an acceptably low risk of material misstatement. As the Authority decided not to adopt group accounts we assessed this decision and reviewed the judgements made in reaching this conclusion. We have no issues to report as a result of our work in this area.

Judgements

We have considered the level of prudence within key judgements in your 2017/18 financial statements and accounting estimates. We have set out our view below across the following range of judgements.

Level of prudence

0	1	2	3	4	5	6
Audit Difference	Cautious		Balanced		Optimistic	Audit Difference
	Acceptable Range					

Subjective area

2017/18 2016/17 Commentary

Provisions (excluding Business Rates)	3	3	Provisions totalled £13m (£13m – 2016/17). A £7m provision is made for the cost of insurance excesses (£6m - 2016/17) and a £4m provision for the cost of voluntary redundancies (£6m – 2016/17).																																
Property Plant & Equipment	3	3	The Authority continues its use of a cyclical valuation methodology based around the revaluation of all assets at least once within a five year timeframe. The Authority has utilised an internal valuation expert to provide valuation estimates. We have reviewed the instructions provided and deem that apart from the indexation adjustment which has been corrected the valuation exercise is in line with the instructions. The resulting change is in line with the indices provided by Gerald Eve, the valuation firm engaged by the NAO to provide supporting valuation information.																																
Valuation of pension assets and liabilities	3	3	<p>The Authority continues to use Hymans Robertson LLP to provide actuarial valuations in relation to the assets and liabilities recognised as a result of participation in the Local Government Pension Scheme. Due to the overall value of the pension assets and liabilities, small movements in the assumptions can have a significant impact on the overall valuation. The actual assumptions adopted by the actuary fell within our expected ranges. As outlined on page 11 we determined that pension liabilities and assets were appropriately accounted for. For example, a 0.5% change in the discount rate would change the net liability by £270 million.</p> <p>The assumptions adopted by the actuary fell within our expected ranges with the exception of the discount rate as set out below. Whilst ordinarily the discount rate would be deemed to be outside our acceptable range, the net discount rate (our baseline assessment of prudence) is well within the acceptable range and therefore the effect of the discount rate is deemed acceptable overall.</p> <table><tr><th>Assumption</th><th>Actuary Value</th><th>KPMG Range</th><th>Level of prudence</th></tr><tr><td>Discount rate</td><td>2.70%</td><td>2.35-2.65%</td><td>4</td></tr><tr><td>CPI inflation</td><td>2.40%</td><td>1.91-2.41%</td><td>2</td></tr><tr><td>Net discount rate</td><td>0.3%</td><td>0.19-0.49%</td><td>3</td></tr><tr><td>Salary Growth</td><td>2.90%</td><td>2.40-4.40%</td><td>3</td></tr><tr><td>Life expectancy</td><td></td><td></td><td></td></tr><tr><td>Current male / female</td><td>23.9/ 26.5</td><td>23.5/25.4</td><td>3</td></tr><tr><td>Future male/female</td><td>21.9/ 24.4</td><td>22.1/23.9</td><td></td></tr></table>	Assumption	Actuary Value	KPMG Range	Level of prudence	Discount rate	2.70%	2.35-2.65%	4	CPI inflation	2.40%	1.91-2.41%	2	Net discount rate	0.3%	0.19-0.49%	3	Salary Growth	2.90%	2.40-4.40%	3	Life expectancy				Current male / female	23.9/ 26.5	23.5/25.4	3	Future male/female	21.9/ 24.4	22.1/23.9	
Assumption	Actuary Value	KPMG Range	Level of prudence																																
Discount rate	2.70%	2.35-2.65%	4																																
CPI inflation	2.40%	1.91-2.41%	2																																
Net discount rate	0.3%	0.19-0.49%	3																																
Salary Growth	2.90%	2.40-4.40%	3																																
Life expectancy																																			
Current male / female	23.9/ 26.5	23.5/25.4	3																																
Future male/female	21.9/ 24.4	22.1/23.9																																	

Proposed opinion and audit differences

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Authority’s 2017/18 financial statements following approval of the Statement of Accounts by the Audit Committee on 26 July 2018.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

The final materiality (see Appendix 4) for this year’s audit was set at £16 million. Audit differences below £800k are not considered significant.

There was one significant audit difference relating to the Authority’s failure to apply indexation during its revaluation work, which we set out in Appendix 3. It is our understanding that this will be adjusted in the final version of the financial statements.

The tables below illustrate the total impact of audit differences on the Authority’s movements on the General Fund for the year and Balance Sheet as at 31 March 2018. There is no net impact on the General Fund as a result of the audit adjustments made.

In addition, we identified a small number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 (‘the Code’). We understand that the Authority is addressing these.

Movement on the General Fund 2017/18				Balance Sheet as at 31 March 2018			
£m	Pre-Audit	Post-Audit	Ref ¹	£m	Pre-Audit	Post-Audit	Ref ¹
(Surplus)/Deficit on the provision of services	216	223	1A	Property, Plant & Equipment	2,060	2,186	1A
Adjustments between accounting basis and funding basis under regulations	(217)	(224)	1A	Other long term assets	119	119	
Transfers from/(to) earmarked reserves	15	15		Current assets	273	273	
Increase in General Fund	14	14		Current liabilities	(126)	(126)	
				Long term liabilities	(1,066)	(1,066)	
				Net worth	1,260	1,386	
				General Fund	65	65	
				Other useable reserves	242	242	
				Unusable reserves	953	1,079	1A
				Total Reserves	1,260	1,386	

¹ See referenced adjustments in Appendix 3.

Proposed opinion and audit differences (cont.)

Annual governance statement

We have reviewed the Authority's 2017/18 Annual Governance Statement and confirmed that:

- It is not misleading and is consistent with other information we are aware of from our audit of the financial statements.

Narrative report

We have reviewed the Authority's 2017/18 narrative report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.



Pension Fund financial statements

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Pension Fund’s 2017/18 financial statements following approval of the Statement of Accounts by the Audit Committee on 26 July 2018.

Pension Fund audit

Our audit of the Fund also did not identify any material misstatements.

For the audit of the Fund we used a materiality level of £36 million. Audit differences below £1.2 million are not considered significant.

As indicated below there are no audit differences to be adjusted in the final version of the pension fund financial statements.

Fund account as at 31 March 2018			Net assets as at 31 March 2018		
£m	Pre-Audit	Post-Audit	£m	Pre-Audit	Post-Audit
Opening net assets of the scheme	4,472	4,472	Net investments	4,619	4,619
Contributions	177	177	Net current assets	25	25
Benefits	(172)	(172)	Net assets of the scheme	4,644	4,644
Management expenses	(25)	(25)			
Return on investments	192	192			
Closing net assets of the scheme	4,644	4,644			

Annual report

We have reviewed the Pension Fund Annual Report and confirmed that:

- It complies with the requirements of the Local Government Pension Scheme (Administration) Regulations 2008; and
- The financial and non-financial information it contains is not inconsistent with the financial information contained in the audited financial statements.

We anticipate issuing an unqualified opinion on the Pension Fund Annual Report at the same time as our opinion on the Statement of Accounts.

Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's 2017/18 financial statements.

Before we can issue our opinion we require a signed management representation letter.

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of Derbyshire County Council[and Derbyshire Pension Fund for the year ending 31 March 2018, we confirm that there were no relationships between KPMG LLP and Derbyshire County Council and Derbyshire Pension Fund, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 5 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to the Finance Manager for presentation to the Audit Committee. We require a signed copy of your management representations before we issue our audit opinion.

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- Significant difficulties encountered during the audit;
- Significant matters arising from the audit that were discussed, or subject to correspondence with management;
- Other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and
- Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, public interest reporting, questions/objections, opening balances etc.).

There are no other matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority's 2017/18 financial statements.

Value for Money Arrangements



Specific value for money risk areas

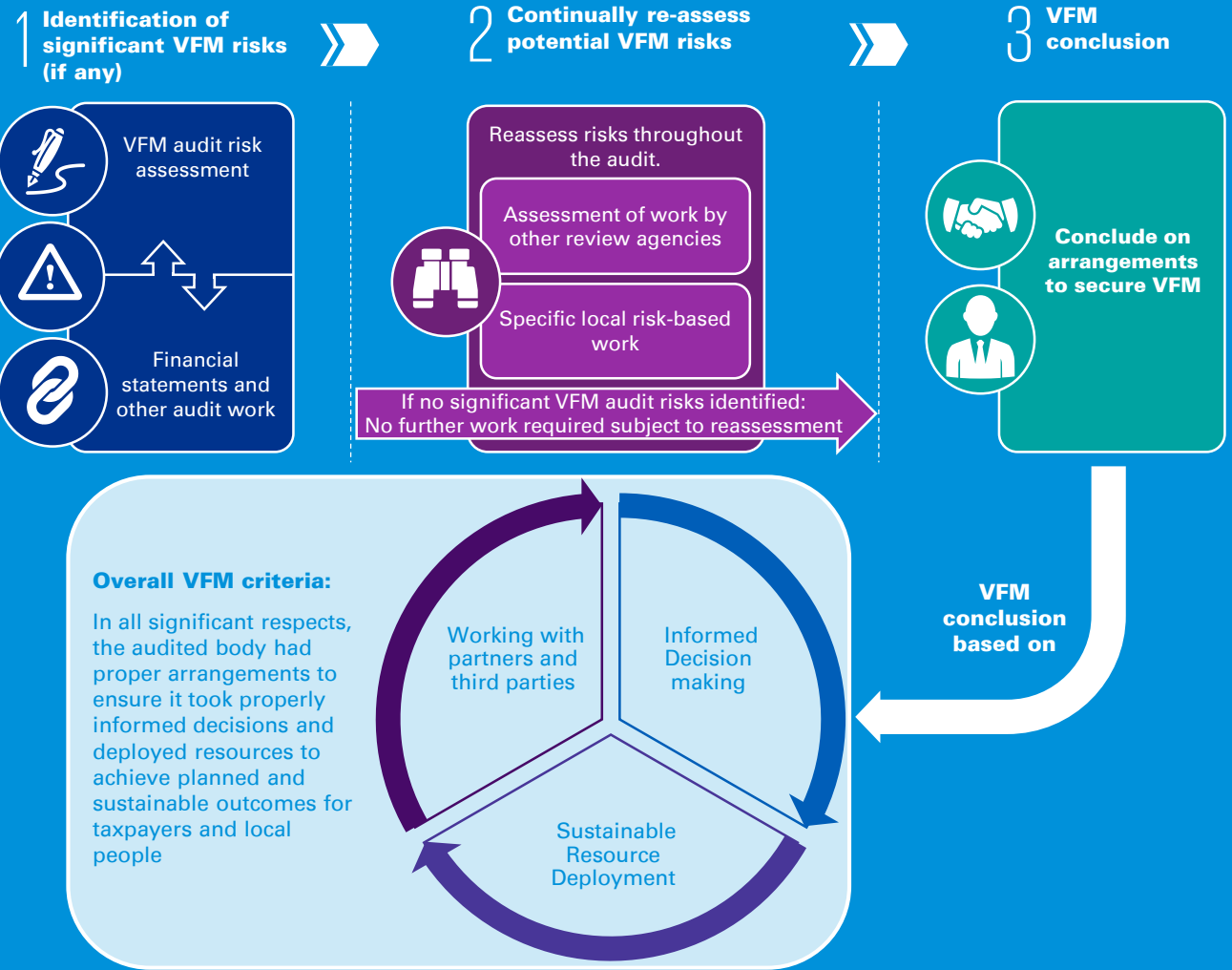
Our 2017/18 VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We have concluded that the Authority has made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the authority ‘has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources’.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to ‘take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor’s judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body’s arrangements.’

We follow a risk based approach to target audit effort on the areas of greatest audit risk.



Specific value for money risk areas (cont.)

The table below summarises our assessment of the individual VFM risk identified against the three sub-criteria. This directly feeds into the overall VFM criteria and our value for money opinion.

Applicability of VFM Risks to VFM sub-criteria			
VFM Risk	Informed decision making	Sustainable resource deployment	Working with partner and third parties
Delivery of budgets	✓	✓	✓

In consideration of the above, we have concluded that in 2017/18, the Authority made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Further details on the work done and our assessment are provided on the following pages.



Specific value for money risk areas (cont.)

As communicated to you in our *External Audit Plan 2017/18* we identified one risk requiring specific audit attention and procedures to address the likelihood that proper arrangements are not in place to deliver value for money.

In all cases we are satisfied that external or internal scrutiny provides sufficient assurance that the Authority’s current arrangements in relation to these risk areas are adequate.

We have provided below a summary of the risk area identified, our work undertaken and the conclusions reached.

Risk:	<p>Delivery of budgets</p> <p>The Authority identified the need to make savings of £34m during the 2017/18 financial year. The latest Medium Term Financial Plan identifies a further saving requirement of £53m in the period 2018/19 - 2022/23.</p> <p>This highlights a total savings requirement of £87m for the full period including 2017/18. These savings are to principally address future reductions to local authority funding alongside service cost and demand pressures within Adult Care and Young People’s Services.</p> <p>As a result, the need for savings will continue to have a significant impact on the Authority’s financial resilience.</p>
Our assessment and work undertaken:	<p>Like most of local government, the Authority faces a challenging future driven by funding reductions and an increase in demand for services. However, the Authority reported an overall underspend on its 2017/18 budgets of £26m. This enabled the General Fund balance to increase to £65m as of 31 March 2018.</p> <p>2018/19 budget</p> <p>In February 2018, the Authority approved a balanced 2018/19 budget. The budget included the required S.151 Officer assurances relating to the robustness of the budget and the adequacy of the level of reserves, but acknowledged the risks around the delivery and timing of savings initiatives and the need to address the medium term budget shortfall from 2019-20 onwards. The budget reflects a mixed approach to addressing the cost pressures identified (£40m) and highlights that savings amounting to £12m have been identified with a further £0.4m required in-year. The Authority approved:</p> <ul style="list-style-type: none">• a 4.99% increase in Council Tax, including 2% for the ‘social care precept’;• savings plans of £12m; and• a £11m transfer from General Reserves during the year as part of the medium term financial plan. <p>We have reviewed the budgeting process, looked at the assumptions included within the calculations and reviewed how savings plans have been identified. We have also looked at the information presented to members as part of this process and have confirmed that detailed supporting documents are made available as part of this process. Overall, we do not have concerns with the arrangements in place.</p>

Specific value for money risk areas (cont.)

Significant VFM Risks (cont.)

Our
assessment
and work
undertaken
(cont.):

Medium term financial planning

During 2017/18 the Authority has been developing further its options for securing medium term financial sustainability. The overall financial planning framework reflects the Government’s four year funding settlement with the Council. Managers have been confirming their assessment of the expected cost pressures due to demographic changes and other factors.

We have met with each Executive lead for the significant functions of the Council during 2017/18 who evidenced the progress being made with the proposals to inform the 2018/19 budget setting process. The emerging framework indicates a way forward for the Authority to balance its budgets for 2018/19 onward which includes a combination of the use of reserves and additional savings. The planned use of reserves is set to reduce to £3m per annum from 2020/21 onwards. The current medium term position was reported to members in February 2018 and highlights an underlying need for £53m of savings which are required by the end of 2021/22. In recognition of the challenging agenda faced, we have made a recommendation that the Authority should constantly refresh savings plans to ensure they are achievable as well as minimise overspends against budgets to reduce the further savings required.

Appendices



Key issues and recommendations

Our audit work on the Authority’s 2017-18 financial statements has identified a number of issues. We have listed these issues in this appendix together with our recommendations which we have agreed with Management. We have also included Management’s responses to these recommendations.

The Authority should closely monitor progress in addressing these risks, including the implementation of our recommendations.

We have given each recommendation a risk rating and agreed what action management will need to take.

Priority Rating for Recommendations

1	Priority One: Issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	2	Priority Two: Issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	3	Priority Three: Issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.
Recommendations Raised: 1		Recommendations Raised: 2		Recommendations Raised: 0	

No.	Risk	Issue & Recommendation	Management Response
1	1	Controls in place in regard to the valuation process Risk As documented earlier in this report a number of issues were noted as part of our work on the valuation of PPE held in the balance sheet. The most notable of these was the Authority’s failure to apply indexation in undertaking its 2017/18 valuation work. This issue resulted from an oversight in the preparation of the valuation working papers and was identified by internal audit work after the pre-audit statement of accounts had been issued. This resulted an audit misstatement amounting to £132m as detailed in Appendix 3. Last year we recommended that management should obtain sufficient assurance as to the valuation of its asset base in advance of the final accounts audit and against this backdrop we are making a similar recommendation this year that management should resolve the issues encountered in the valuation process. Recommendation Ensure that valuation work is completed and appropriately checked on a timely basis to enable accurate entries to be made in the pre-audit statement of accounts.	<p>The full year impact of additional staffing resources aligned with an earlier start date for the valuation work compared to 2017-18 will ensure that the property valuations are completed in a timely manner.</p> <p>Alongside additional validation checks it is expected that the resulting data will be of the right quality for the accounts in line with the requirements set out in the terms of engagement agreed between the Property and Finance & ICT Divisions.</p> <p>These processes will be documented in the Valuations Procedure Manual.</p> <p>Responsible Officer Sarah Morris</p> <p>Implementation Deadline December 2018</p>

Key issues and recommendations (cont.)

Our audit work on the Authority’s 2017-18 financial statements has identified a number of issues. We have listed these issues in this appendix together with our recommendations which we have agreed with Management. We have also included Management’s responses to these recommendations.

The Authority should closely monitor progress in addressing the risks, including the implementation of our recommendations.

We have given each recommendation a risk rating and agreed what action management will need to take.

Priority Rating for Recommendations

1	Priority One: Issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	2	Priority Two: Issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	3	Priority Three: Issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.
Recommendations Raised: 1		Recommendations Raised:2		Recommendations Raised: 0	

No.	Risk	Issue & Recommendation	Management Response
2	2	Controls in place in relation to SAP users with privileged access Risk Our IT audit team reviewed the SAP control environment and established that certain weaknesses exist. The issues involved are detailed below: 1) No table logging is currently activated for system logs (T000 in particular). Hence the Authority is not able to generate a log of direct changes made to the SAP system by users with privileged access. 2) 11 users with privileged access can both develop and implement changes in the production process of the SAP system. These arrangements do not give segregation in relation to the duties performed. 3) Active leavers with privileged access were on the SAP system post their leaving date representing poor management of starters and leavers with privileged access. Recommendation Implement controls to ensure: the activities of SAP users with privileged access can be monitored; appropriate segregation of duties is achieved; and access rights are withdrawn when individuals leave.	Agreed. Table logging – log T000 - will be switched on to record when SAP Production systems are opened. The number of users with privileged access has been reduced to four from eleven. Any change to the status of users with these privileged access will be actively managed by senior finance staff. Starters and Leavers process has been automated around payroll information. Responsible Officer Wayne Sutton Implementation Deadline September 2018

Key issues and recommendations (cont.)

Our audit work on the Authority’s 2017-18 financial statements has identified a number of issues. We have listed these issues in this appendix together with our recommendations which we have agreed with Management. We have also included Management’s responses to these recommendations.

The Authority should closely monitor progress in addressing the risks, including the implementation of our recommendations.

We have given each recommendation a risk rating and agreed what action management will need to take.

Priority Rating for Recommendations

1	Priority One: Issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk. Recommendations Raised: 1	2	Priority Two: Issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system. Recommendations Raised:2	3	Priority Three: Issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them. Recommendations Raised: 0
---	---	---	--	---	--

No.	Risk	Issue & Recommendation	Management Response
3	2	Financial Standing Risk During 2017/18 the Authority has been developing further its options for securing medium term financial sustainability. The emerging framework indicates a way forward for the Authority to balance its budgets for 2018/19 onward which includes a combination of the use of reserves and additional savings. The planned use of reserves is set to reduce to £3m per annum from 2020/21 onwards. The current medium term position was reported to members in February 2018 and highlights an underlying need for £53m of savings which are required by the end of 2021/22. In recognition of the challenging agenda faced, we have made the recommendation detailed below. Recommendation The Authority should constantly refresh savings plans to ensure they are achievable as well as minimise overspends against budget to reduce the further savings required.	Agreed, regular budget monitoring reporting at all levels within the organisation will contain updates on savings plans and provide a focus for holding budget holders to account for overspending. The Five Year Financial Plan will be updated over Summer 2018 and members and officers will work together to produce a set of proposals that will balance the budget over the medium term. Responsible Officer Peter Handford Implementation Deadline September 2018

Follow-up of prior year recommendations

The Authority has not implemented all of the recommendations raised through our previous audit work.

We re-iterate the importance of the outstanding recommendations and recommend that these are implemented.

This appendix summarises the progress made to implement the recommendations identified in our *ISA 260 Report 2016/17* and outstanding recommendations from previous audit years and re-iterates any recommendations still outstanding.

Number of recommendations that were

Included in the original report	4
Implemented in year or superseded	2
Outstanding at the time of our audit and detailed below	2

No.	Risk	Issue & Recommendation	Status as at July 2018
1	1	Controls in place in regard to valuation process <i>Risk</i> A large number of issues were noted as part of our 2016/17 work in the valuation of PPE held on the balance sheet. <i>Recommendation</i> In future years management should obtain sufficient assurance as to the valuation of its asset base in advance of the final accounts audit.	Progress has been made in relation to capacity issues, terms of reference, AMP1 forms and other detailed issues. However, valuation work is still not being carried out on a timely basis that allows for appropriate checking to ensure accurate entries are made in the pre-audit statement of accounts.
2	3	Implementation of Pensions Administration System <i>Risk</i> Whilst progress has been made further work is required to fully embed the operation of the Pensions Administration System. <i>Recommendation</i> We recommend the Authority continue to progress this matter and report to the Audit Committee on this issue.	There has been improvement during 2017/18, however with the demands on resources created by the migration to a new pensions administration system in 2018 and the impact of the LGPS Amendment Regulations in May 2018, it is not expected that the current rate of improvement will be maintained.

Audit differences

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit Committee).

We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

A number of minor amendments focused on presentational improvements have been made to the 2017/18 draft financial statements. The Finance team remains committed to continuous improvement in the quality of the financial statements submitted for audit in future years.

Adjusted audit differences – Authority

The following table sets out the significant audit differences identified during our audit of Derbyshire County Council's financial statements for the year ended 31 March 2018. We have received a revised set of financial statements which confirm this.

Table 1: Adjusted audit differences – Authority (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
1A	Dr £125,882k (revaluation gains/losses below the net cost of services line)	Cr £125,882k (change in CIES total)	Dr £125,882k (property, plant & equipment)		Cr £125,882k (revaluation reserve and capital adjustment account)	Asset uplift resulting from the application of indexation omitted in error. Whilst the £125,882k only impacts on the Income and Expenditure statement below the net cost of services line, £6,228k of this amount increases the Authority's deficit on the provision of services.
	Dr £125,882k	Cr £125,882k	Dr £125,882k	Dr/Cr £nil	Cr £125,882k	Total impact of adjustments

Unadjusted audit differences

The following table sets out the uncorrected audit differences identified by our audit of Derbyshire County Council's financial statements for the year ended 31 March 2018. These differences are individually below our materiality level of £16m. Cumulatively, the impact of these uncorrected audit differences is well below materiality. We have also considered the cumulative impact of these unadjusted audit differences on the Authority's financial statements in forming our audit opinion.

Table 2: Unadjusted audit differences – Authority (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
1U	Dr £645k (revaluation gains/losses below the net cost of services)	Cr £645k (change in CIES total)	Dr £645k (property, plant & equipment)		Cr £645k (revaluation reserve and capital adjustment account)	Reversal of revaluation losses incorrectly taken to the income and expenditure account as a result of not applying indexation (for numerous buildings and not adjusted for due to workload considerations).
2U	Cr £409k			Dr £409k (stock creditor)		Invalid creditor relating to stock ordered before the implementation of the SAP stores system in a service area and not outstanding. Some minor adjustments may be required to the amount detailed.
	Dr £236k	Cr £645k	Dr £645k	Dr £409k	Cr £645k	Total impact of adjustments

Materiality and reporting of audit differences

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects: materiality by value, nature and context.

Material errors by value are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements.

Errors which are material by nature may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff.

Errors that are material by context are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our *External Audit Plan 2017/18*, presented to you in February 2018.

Materiality for the Authority's accounts was set at £16 million which equates to just under one percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision (£12million).

Reporting to the Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any misstatements of lesser amounts to the extent that these are identified by our audit work.

Under ISA 260, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

ISA 450 requires us to request that uncorrected misstatements are corrected.

In the context of the Authority, an individual difference is considered to be clearly trivial if it is less than £0.8 million for the Authority.

Where management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit Committee to assist it in fulfilling its governance responsibilities.

Materiality – Pension fund audit

The same principles apply in setting materiality for the Pension Fund audit. Materiality for the Pension Fund was set at £36 million which equates to just under one percent of total assets.

We design our procedures to detect errors at a lower level of precision, set at £27 million for 2017/18.

Appendix 5:

Required communications with the Audit Committee

We have provided below at-a-glance summary of the information we are required to report to you in writing by International Auditing Standards.

Required Communication	Commentary
Our draft management representation letter	We have not requested any specific representations in addition to those areas normally covered by our standard representation letter for the year ended 31 March 2018.
Adjusted audit differences	We have identified one adjusted audit difference in relation to the valuation of assets with a value of £126 million. See page 29 for further details. This adjustment did not impact on the net cost of services and only £6.2 million of this amount increased the reported deficit on provision of services.
Unadjusted audit differences	The net impact of unadjusted audit differences on the deficit on provision of services would be clearly trivial.
Related parties	There were no significant matters that arose during the audit in connection with the entity's related parties.
Other matters warranting attention by the Audit Committee	There were no matters to report arising from the audit that, in our professional judgment, are significant to the oversight of the financial reporting process.
Control deficiencies	<p>We have set out our assessment of the Authority's internal control environment in Section one of this report (see pages 4 and 5). This includes confirmation that apart from the controls relating to the valuation of property there were no significant deficiencies identified.</p> <p>We communicated to management any deficiencies in internal control over financial reporting of a lesser magnitude than the significant deficiencies highlighted during the course of our audit.</p>
Actual or suspected fraud, noncompliance with laws or regulations or illegal acts	We identified no actual or suspected fraud involving the Authority's Member or officers with significant roles in internal control, or where the fraud resulted in a material misstatement in the financial statements.
Significant difficulties	No significant difficulties were encountered during the audit.
Modifications to auditor's report	There are no modifications to our audit report.
Disagreements with management or scope limitations	The engagement team had no disagreements with management and no scope limitations were imposed by management during the audit.

Appendix 5:

Required communications with the Audit Committee (cont.)

Required Communication	Commentary
Other information	<p>No material inconsistencies were identified related to other information in the Narrative Report or Annual Governance Statement.</p> <p>These reports were found to be fair, balanced and comprehensive, and compliant with applicable requirements.</p>
Our declaration of independence and any breaches of independence	<p>No matters to report.</p> <p>The engagement team have complied with relevant ethical requirements regarding independence.</p> <p>See Appendix 6 for further details.</p>
Accounting practices	<p>Over the course of our audit, we have evaluated the appropriateness of the Authority's accounting policies, accounting estimates and financial statement disclosures. In general, we believe these are appropriate.</p> <p>We have set out our view of the assumptions used in valuing pension assets and liabilities at page 14.</p>
Significant matters discussed or subject to correspondence with management	<p>There were no significant matters arising from the audit which were discussed, or subject to correspondence, with management other than the matters highlighted in this report.</p>



Declaration of independence

ASSESSMENT OF OUR OBJECTIVITY AND INDEPENDENCE AS AUDITOR OF DERBYSHIRE COUNTY COUNCIL AND DERBYSHIRE PENSION FUND

Professional ethical standards require us to provide to you at the conclusion of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code of Audit Practice, the provisions of Public Sector Audit Appointments Limited's ('PSAA's') Terms of Appointment relating to independence, the requirements of the FRC Ethical Standard and the requirements of Auditor Guidance Note 1 - General Guidance Supporting Local Audit (AGN01) issued by the National Audit Office ('NAO') on behalf of the Comptroller and Auditor General.

This Statement is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

- General procedures to safeguard independence and objectivity;
- Independence and objectivity considerations relating to the provision of non-audit services; and
- Independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners, Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Communications
- Internal accountability
- Risk management
- Independent reviews.

The conclusion of the audit engagement leader as to our compliance with the FRC Ethical Standard in relation to our audit engagement for the Derbyshire Pension Fund is subject to review by an engagement quality control reviewer, who is a Audit Director not otherwise involved in your affairs.

We are satisfied that our general procedures support our independence and objectivity.

Declaration of independence (cont.)

Independence and objectivity considerations relating to the provision of non-audit services

Summary of fees

We have considered the fees charged by us to the authority for professional services provided by us during the reporting period. We have detailed the fees charged by us to the authority and its controlled entities for significant professional services provided by us during the reporting period in Appendix 7, as well as the amounts of any future services which have been contracted or where a written proposal has been submitted. Total fees charged by us for the period ended 31 March 2018 can be analysed as follows:

	2017-18 £	2016-17 £
Audit of the Authority	125,356	137,122
Audit of the Pension Fund	28,672	35,204
Audit of Derbyshire Developments Ltd	4,000	5,000
Total audit services	158,028	177,326
Audit related assurance services (Grant certification – Teachers Pensions)	3,500	3,500
Total Non Audit Services	3,500	3,500

We are required by AGN 01 to limit the proportion of fees charged for non-audit services (excluding mandatory assurance services) to 70% of the total fee for all audit work carried out in respect of the Authority under the Code of Audit Practice for the year. The ratio of non-audit fees to audit fees for the year was 1:45. We do not consider that the total of non-audit fees creates a self-interest threat since the absolute level of fees is not significant to our firm as a whole.

Facts and matters related to the provision of non-audit services and the safeguards put in place that bear upon our independence and objectivity, are set out in the table on the following page.

Declaration of independence (cont.)

Analysis of Non-audit services for the year ended 31 March 2018

Description of scope of services	Principal threats to independence and Safeguards applied	Basis of fee	Value of services delivered in the year ended 31 March 2018 £	Value of services committed but not yet delivered £
Audit-related assurance services				
Grant Certification – Teachers Pensions Return	<p>The nature of this audit-related service is to provide independent assurance on this return. As such we do not consider it creates any independence threats which we have considered as detailed below.</p> <p>Self-interest: This engagement is entirely separate from the audit and there is a separate engagement letter in place.</p> <p>Self-review: The nature of this work is to issue the Accountant’s Independent Assurance Report in accordance with the specific assurance instructions set out by the TPA. It does not impact on our opinion and we do not consider that the outcome of this work is a threat to our role as external auditors.</p> <p>Management threat: This work was undertaken in accordance with the Assurance Instruction provided by the TPA.</p> <p>Familiarity: This threat is limited given the scale, nature and timing of the work.</p> <p>Advocacy: We will not act as advocates for the Authority in any aspect of this work.</p> <p>Intimidation: Not applicable</p>	Fixed Fee	3,500	3,500

Appendix 6:

Declaration of independence (cont.)

Independence and objectivity considerations relating to other matters

There are no other matters that, in our professional judgment, bear on our independence which need to be disclosed to the Audit Committee.

Confirmation of audit independence

We confirm that as of the date of this report, in our professional judgment, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This report is intended solely for the information of the Audit Committee of the authority and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.



KPMG LLP

Appendix 7:

Audit fees

As communicated to you in our *External Audit Plan 2017-18*, our scale fee for the audit is £154,028 plus VAT (£154,028 in 2016/17), which is consistent with the scale fee from the prior year.

Planned fees for grants and claims which do not fall under the PSAA arrangements amount to £3,500 plus VAT (£3,500 in 2016/17), see further details below.

Component of the audit	2017-18 Planned Fee £	2016-17 Actual Fee £
Accounts opinion and value for money work		
PSAA Scale fee (Derbyshire County Council)	125,356	125,356
PSAA Scale fee (Derbyshire Pension Fund)	28,672	28,672
Additional fees in relation to PPE work and delays	To be confirmed	18,298
Audit of Derbyshire Developments Ltd	4,000	5,000
Total audit services	158,028	177,326
Audit-related assurance services		
Teachers' Pension Return (work planned for July/August)	3,500	3,500
Total audit-related assurance services	3,500	3,500
Total non-audit services	3,500	3,500
Grand total fees for the Authority	161,528	180,826

All fees quoted are exclusive of VAT.





The key contacts in relation to our audit are:

John Cornett

Director

T: +44 (0) 116 256 6064

E: john.cornett@kpmg.co.uk

Richard Walton

Senior Manager

T: +44 (0) 115 945 4471

E: richard.walton@kpmg.co.uk

John Pressley

Assistant Manager

T: +44 (0) 115 935 3471

E: john.pressley@kpmg.co.uk

kpmg.com/uk



This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. We draw your attention to the Statement of Responsibilities of auditors and audited bodies, which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact John Cornett, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers, by email to Andrew.Sayers@kpmg.co.uk. After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

© 2018 KPMG LLP, a UK limited liability partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.

CREATE: CRT086281A