

# Annual Audit Letter

## Rochdale Borough Council

Year ending 31 March 2020





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# 1. EXECUTIVE SUMMARY

## Purpose of the Annual Audit Letter

Our Annual Audit Letter summarises the work we have undertaken as the auditor Rochdale Borough Council (the Council) for the year ended 31 March 2020. Although this letter is addressed to the Council, it is designed to be read by a wider audience including members of the public and other external stakeholders.

Our responsibilities are defined by the Local Audit and Accountability Act 2014 (the 2014 Act) and the Code of Audit Practice issued by the National Audit Office (the NAO). The detailed sections of this letter provide details on those responsibilities, the work we have done to discharge them, and the key findings arising from our work. These are summarised below.

Area of responsibility	Summary
Audit of the financial statements	<p>Our auditor's report issued on 27 November 2020 included our opinion that the financial statements:</p> <ul style="list-style-type: none"><li>• give a true and fair view of the Council's financial position as at 31 March 2020 and of its expenditure and income for the year then ended; and</li><li>• have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20</li></ul>
Other information published alongside the audited financial statements	<p>Our auditor's report included our opinion that:</p> <ul style="list-style-type: none"><li>• the other information in the Statement of Accounts is consistent with the audited financial statements.</li></ul>
Value for money conclusion	<p>Our auditor's report concluded that we are satisfied that in all significant respects, the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2020, except for in relation to non-compliance with the Council's Constitution in respect of the key decision making process.</p>
Reporting to the group auditor	<p>In line with group audit instructions, issued by the NAO on 4<sup>th</sup> November, we reported to the group auditor in line with the requirements applicable to the Council's WGA return.</p>
Statutory reporting	<p>Our auditor's report confirmed that we did not use our powers under s24 of the 2014 Act to issue a report in the public interest or to make written recommendations to the Council.</p>



## 2. AUDIT OF THE FINANCIAL STATEMENTS

Opinion on the financial statements

**Unqualified**

### The scope of our audit and the results of our work

The purpose of our audit is to provide reasonable assurance to users that the financial statements are free from material error. We do this by expressing an opinion on whether the statements are prepared, in all material respects, in line with the financial reporting framework applicable to the Council and whether they give a true and fair view of the Council's financial position as at 31 March 2020 and of its financial performance for the year then ended.

Our audit was conducted in accordance with the requirements of the Code of Audit Practice issued by the NAO, and International Standards on Auditing (ISAs). These require us to consider whether:

the accounting policies are appropriate to the Council's circumstances and have been consistently applied and adequately disclosed;

the significant accounting estimates made by management in the preparation of the financial statements are reasonable; and

the overall presentation of the financial statements provides a true and fair view.

Our auditor's report, stated that in our view, the financial statements give a true and fair view of the Council's financial position as at 31 March 2020 and of its financial performance for the year then ended. The report included an emphasis of matter paragraph in relation to material uncertainties in the valuation of the Council's investment properties and surplus assets and the Council's share of pension fund property assets.

### Our approach to materiality

We apply the concept of materiality when planning and performing our audit, and when evaluating the effect of misstatements identified as part of our work. We consider the concept of materiality at numerous stages throughout the audit process, in particular when determining the nature, timing and extent of our audit procedures, and when evaluating the effect of uncorrected misstatements. An item is considered material if its misstatement or omission could reasonably be expected to influence the economic decisions of users of the financial statements.

Judgements about materiality are made in the light of surrounding circumstances and are affected by both qualitative and quantitative factors. As a result we have set materiality for the financial statements as a whole (financial statement materiality) and a lower level of materiality for specific items of account (specific materiality) due to the nature of these items or because they attract public interest. We also set a threshold for reporting identified misstatements to the Audit and Governance Committee. We call this our trivial threshold.

The table below provides details of the materiality levels applied in the audit of the financial statements for the year ended 31 March 2020:

Financial statement materiality	Our financial statement materiality is based on 2% of gross operating expenditure.	£12.1m
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	£0.4m
Specific materiality	We have applied a lower level of materiality to the following areas of the accounts: - senior officers remuneration	£5,000



## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our response to significant risks

As part of our continuous planning procedures we considered whether there were risks of material misstatement in the Council's financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Audit and Governance Committee within our Audit Strategy Memorandum and provided details of how we responded to those risks in our Audit Completion Report. The table below outlines the identified significant risks, the work we carried out on those risks and our conclusions.

Identified significant risk	Our response	Our findings and conclusions
<p><b>Management override of controls</b> In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Because of the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits</p>	<p>We addressed this risk through performing audit work over:</p> <ul style="list-style-type: none"> <li>Accounting estimates impacting on amounts included in the financial statements;</li> <li>Consideration of identified significant transactions outside the normal course of business; and</li> <li>Journals recorded in the general ledger and other adjustments made in preparation of the financial statements.</li> </ul>	<p>Our audit work provided the assurance we sought.</p> <p>There are no issues to bring to your attention.</p>
<p><b>Defined benefit liability valuation</b> The net pension liability represents a material element of the Council's balance sheet. The Council is an admitted body of Greater Manchester Pension Fund, which had its last triennial valuation completed as at 31 March 2019. 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 Council's overall valuation. There is a risk that the assumptions and methodology used in valuing the Council's pension obligation are not reasonable or appropriate to the Council's circumstances.</p>	<p>We have reviewed the controls that the Council has in place over the information sent to the Scheme Actuary, including the Council's process and controls with respect to the assumptions used in the valuation. We have also evaluated the competency, objectivity and independence of the scheme Actuary, Hymans Robertson.</p> <p>We reviewed the appropriateness of the methodology applied, and the key assumptions included within the valuation, comparing them to expected ranges, utilising the information provided by PwC, consulting actuary engaged by the National Audit Office. We reviewed the methodology applied in the valuation of the liability by Hymans Robertson.</p>	<p>Our audit work provided the assurance we sought.</p> <p>Due to the increased market uncertainty arising from the COVID-19 pandemic, management obtained an updated valuation report during the course of the audit. The updated report confirmed the liability had decreased by £18m. As this was materially different to the original valuation management adjusted the financial statements to reflect the most up-to-date information.</p> <p>The pension fund accounts disclosed a material valuation uncertainty in relation to property investment valuations. This has been disclosed in Note 3 of the Council's financial statements. Our audit opinion included an 'Emphasis of Matter' paragraph which draws readers' attention to the appropriate disclosures. This does not constitute a modification to our audit opinion.</p>



## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our response to significant risks continued

Identified significant risk	Our response	Our findings and conclusions
<p><b>Valuation of Property, Plant and Equipment (land and buildings including investment properties)</b></p> <p>The CIPFA Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Council has adopted a rolling revaluation model which sees all land and buildings revalued over a four year cycle.</p> <p>The valuation of Property, Plant &amp; Equipment and Investment Properties involves the use of a management expert (the valuer), and incorporates assumptions and estimates which impact materially on the reported value. There are risks relating to the valuation process which reflect the significant impact of the valuation judgements and assumptions and the degree of estimation uncertainty.</p> <p>In addition, as a result of the rolling programme of revaluations, there is a risk that individual assets which have not been revalued for up to three years are not valued at their materially correct fair value.</p> <p>Due to the availability of market data as a result of the COVID-19 pandemic, the valuer has included a 'material uncertainty' disclosure within the valuation report.</p>	<p>In relation to the assets which have been revalued during 2019/20 we have assessed the Council's valuer's qualifications, objectivity and independence to carry out such valuations, and then reviewed the valuation methodology used, including testing the underlying data and challenging the assumptions.</p> <p>We have reviewed the approach that the Council has adopted to address the risk that assets not subject to valuation in 2019/20 are materially misstated and considered the robustness of that approach in light of the valuation information reported by the Council's valuers.</p> <p>In addition, we have considered movement 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>We employed an external valuations expert to consider the impact of the 'material uncertainty' disclosure. Based on their work, we are satisfied the valuation can still be relied upon. During the course of the audit we obtained up-to-date market data and compared this to the Council's asset valuations. This confirmed the valuations were in line with wider market data.</p>	<p>Our audit work provided the assurance we sought.</p> <p>Our sample testing identified a total understatement is £435k in relation to land values. This was not adjusted in the audited accounts as the amount was not material and will be corrected in future years.</p> <p>Our work on the valuations confirmed the Council's valuer's had included a 'Material Valuation Uncertainty' paragraph in their valuation reports due to the impact of COVID-19 pandemic on the real estate market. Through our work we are satisfied this does not mean the valuations cannot be relied upon, only that less certainty can be attached to the valuations than would normally be the case.</p> <p>The Council made appropriate disclosures regarding this in Note 3 to the accounts. Our audit opinion included an 'Emphasis of Matter' paragraph which draws readers' attention to the appropriate disclosures. This does not constitute a modification to our audit opinion.</p>



## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Internal control recommendations

As part of our audit we considered the internal controls in place that are relevant to the preparation of the financial statements. We did this to design audit procedures that allow us to express our opinion on the financial statements, but this did not extend to us expressing an opinion on the effectiveness of internal controls. We did not identify any control deficiencies during the course of the audit.



### 3. VALUE FOR MONEY CONCLUSION

Value for money conclusion	Qualified
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#### Our audit approach

We are required to consider whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out in order to form our conclusion, and sets out the criterion and sub-criteria that we are required to consider.

The overall criterion is that, ‘in all significant respects, the Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.’ To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:

- informed decision making;
- sustainable resource deployment; and
- working with partners and other third parties.

Our auditor's report, stated that that, in all significant respects, the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31st March 2020, except for in relation to non-compliance with the Council's Constitution in respect of the key decision making process. Further detail is provided on the following page.



### 3. VALUE FOR MONEY CONCLUSION

#### Significant audit risks

The NAO’s guidance requires us to carry out work to identify whether or not a risk to our conclusion exists. Risk, in the context of our work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Council being inadequate. We reported that we had identified two significant audit risks. The work we carried out in relation to significant risks is outlined below.

Risk	Commentary	Conclusion
<p><b>Key Decision Making</b></p> <p>During the course of the year the Council's Internal Audit team identified non-compliance with the Council's Constitution in respect of the Key Decision process in the Adult Care and Public Health services. Further work undertaken by Internal Audit team identified non-compliance across the Council's services.</p> <p>Non-compliance with the Council's Constitution in respect of Key Decisions presents a significant audit risk in respect of the Council's arrangements to support informed decision making.</p>	<p>Our review of the work of Internal Audit confirmed the Council's non-compliance with the Council's Constitution on taking key decisions.</p> <p>Following the initial findings in relation to Adult Care and Public Health, internal audit completed a review of 45 'live' contracts which appeared to meet the definition of a key decision. This review concluded that a significant value of the Council's expenditure had not been through the formal process of key decision making. This creates a risk to the overall transparency of the proposed procurement process to Councillors and inhibits the potential for challenge or call in through the scrutiny process.</p> <p>The Head of Internal Audit reported this matter in his overall opinion on the Council's control environment for 2019/20 and this has, in turn, been disclosed in the Council's Annual Governance Statement.</p> <p>Management responded quickly and positively to the issue and developed an action to address the findings from the initial report. This includes updated governance procedures in relation to procurement, refreshed training for Officers and a review of the Council's Constitution to clarify the definition of a key decision. Management also conducted a detailed review of all exceptions identified by Internal Audit and have taken appropriate action to address.</p> <p>Whilst we note the progress made since Internal Audit issued their report, we conclude that for 2019/20 the Council did not have proper arrangements to support informed decision making in respect of the key decision making process. As such we issued a qualified 'except for' value for money conclusion.</p>	<p>We concluded that for 2019/20 the Council did not have proper arrangements to support informed decision making in respect of the key decision making process.</p>



### 3. VALUE FOR MONEY CONCLUSION

#### Significant audit risks continued

Risk	Commentary	Conclusion
<p><b>Financial Resilience</b></p> <p>The Council’s medium term financial strategy for the period 2020/21 to 2024/25 sets out the financial challenges it faces. The mid year reporting for 2019/20 indicates that the Council’s general services spending is projecting to be overspent by £5.9m, placing further pressure on service delivery and increasing the use of reserves to support the revenue expenditure.</p> <p>The Council’s Budget Report 2020/21 identifies a budget gap of £2.0m by 2022/23 following delivery of identified savings proposals and a transfer from the Council’s contingency reserve. The £2.0m forms part of a wider gap within the Pooled Fund for Health and Social Care which the Council operates with Heywood, Middleton and Rochdale CCG. The gap on the Pooled Fund is currently forecast to reach £18.5m by 2021/22.</p> <p>The continuing challenges the Council faces are not new and are not unique to Rochdale Borough Council. The challenges do, however, present a significant audit risk in respect of considering the arrangements that the Council has in place to deliver financially sustainability over the medium term.</p>	<p>The Council set robust and balanced budgets for 2019/20 and 2020/21. In 2019/20 the Council intended to apply some reserves but the 2020/21 budget reflected a contribution to reserves of £2.5m. The reserves were intended to allow the Council to support budgetary pressures identified as likely to arise in future years.</p> <p>Detailed progress reports are provided to Cabinet on a quarterly basis allowing for effective monitoring of progress against budget.</p> <p>The Council’s final reported outturn was a break even position. This was achieved after significant overspends in respect of demand led services in Children’s Services and Adult Care, which were offset by underspends elsewhere and a contribution from the Council’s Equalisation Reserve of £3.2m. The Council is working to identify ways of mitigating these demand pressures for future years.</p> <p>However, the outbreak of the COVID-19 presents a new and significant challenge to the Council’s longer-term financial sustainability for the coming years. Additional cost pressures and reduced income have led to the need for the Council to reassess its 2020-21 budget and medium term financial strategy. Work is now well underway to assess the impact of the pandemic on the Council’s operations its financial position. This work will continue over the coming months.</p> <p>The Council continues to work closely with Heywood, Middleton and Rochdale CCG to manage the Pooled Fund for Health and Social Care through the Integrated Commissioning Board. The Council and CCG closed the gap on the pooled fund in 2019-20 through the use of one-off contributions. Due to the COVID-19 pandemic the Council and the CCG have agreed to suspend the risk sharing agreement for 2020-21 so that each organisation takes responsibility for its own budget gaps. This provides clarity on the pressures each organisation faces as they attempt to deal with the impact of the pandemic.</p>	<p>We concluded that for 2019/20 the Council has made proper arrangements to deliver financial sustainability in the medium term.</p>



## 4. OTHER REPORTING RESPONSIBILITIES

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

The NAO's Code of Audit Practice and the 2014 Act place wider reporting responsibilities on us, as the Council's external auditor. We set out below, the context of these reporting responsibilities and our findings for each.

### Matters on which we report by exception

The 2014 Act provides us with specific powers where matters come to our attention that, in our judgement, require reporting action to be taken. We have the power to:

- issue a report in the public interest;
- make statutory recommendations that must be considered and responded to publicly;
- apply to the court for a declaration that an item of account is contrary to law; and
- issue an advisory notice under schedule 8 of the 2014 Act.

We have not exercised any of these statutory reporting powers.

The 2014 Act also gives rights to local electors and other parties, such as the right to ask questions of the auditor and the right to make an objection to an item of account. We did not receive any such objections or questions.

### Reporting to the NAO in respect of Whole of Government Accounts consolidation data

The NAO, as group auditor, requires us to complete the WGA Assurance Statement in respect of its consolidation data, and to carry out certain tests on the data. We submitted this information to the NAO on 16 February 2021.

### Other information published alongside the financial statements

The Code of Audit Practice requires us to consider whether information published alongside the financial statements is consistent with those statements and our knowledge and understanding of the Council. In our opinion, the other information in the Statement of Accounts is consistent with the audited financial statements.



## 5. OUR FEES

### Fees for work as the Council's auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum, presented to Audit and Governance Committee in March 2020.

Having completed our work for the 2019/20 financial year, we can confirm that our final fees are as follows:

Area of work	2019/20 proposed fee	2019/20 final fee
Delivery of audit work under the NAO Code of Audit Practice	£105,007	£129,657

Our final fee reflects the increased work required in respect of the Council's PPE and defined benefit liability valuations as a result of changes in the regulatory environment within which we operate. We have also undertaken additional work in relation to the impact of COVID-19 in respect of property valuations and pensions (material valuation uncertainty), the Council's going concern assessment, and value for money arrangements in respect of the Council's non-compliance with its key decision making process.

### Fees for other work

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



## 6. FORWARD LOOK

### Changes to the Code of Audit Practice

The Code of Audit Practice (the Audit Code), issued by the Comptroller and Auditor General, prescribes the way we carry out our responsibilities as your auditors. On 1<sup>st</sup> April 2020 a new Code came in to force and will apply to our work from 2020/21 onwards.

The new Audit Code continues to apply the requirements of International Standards on Auditing (ISAs) to our audit of the financial statements. While there are changes to the ISAs that are effective from 2020/21 the Audit Code has not introduced any changes to the scope of our audit of the financial statements. We will continue to give our opinion on the financial statements in our independent auditor's report.

There are however significant changes to the work on value for money arrangements, and the way we report the outcomes of our work to you.

#### The auditor's work on value for money arrangements

From 2020/21 we are still required to satisfy ourselves that you have made proper arrangements for securing the economy, efficiency and effectiveness in your use of resources, however unlike under the 2015 Audit Code, we will no longer report in the form of a conclusion on arrangements. Instead, where our work identifies significant weaknesses in arrangements, we are required to report those weaknesses to you, along with the actions that need to be taken to address those weaknesses.

Our work on value for money arrangements will focus on three criteria, specified in the revised Audit Code:

- Financial sustainability: how the body plans and manages its resources to ensure it can continue to deliver its services;
- Governance: how the body ensures that it makes informed decisions and properly manages its risks; and
- Improving economy, efficiency and effectiveness: how the body uses information about its costs and performance to improve the way it manages and delivers its services.

Under the new Audit Code we will be expected to report and make recommendations as soon as we identify a significant weakness in arrangements, as opposed to reporting our conclusion on arrangements at the end of the audit cycle as has previously been the case.

#### Reporting the results of the auditor's work

We currently issue you with an Annual Audit Letter which provides a summary of our work across all aspects of our audit. From 2020/21 the Annual Audit Letter will be replaced by the Auditor's Annual Report. This will continue to provide a summary of our work over the year of audit but will also include a detailed commentary on your arrangements in place to achieve economy, efficiency and effectiveness. This commentary replaces the conclusion on arrangements that was previously provided and will include details of any significant weakness identified and reported to you, follow up of any previous recommendations made, and the our view as to whether recommendations have been implemented satisfactorily.

The guidance supporting the new Audit Code is being developed by the National Audit Office and we will provide you with any further updates to our approach arising from this guidance when it is released.



## 6. FORWARD LOOK

### Redmond Review

In September 2020, Sir Tony Redmond published the findings of his independent review into the oversight of local audit and the transparency of local authority financial reporting. The report makes several recommendations that, if implemented, could affect both the financial statements that local authorities are required to prepare and the work that we as auditors are required to do.

The report and recommendations are wide-ranging, and includes:

- the creation of the Office of Local Audit and Regulation (OLAR), be created to manage, oversee and regulate local audit;
- reviewing reporting deadlines;
- reviewing governance arrangements in local authorities, including the membership of the Audit Committee; and
- increasing transparency and reducing the complexity of local authority financial statements.

The recommendations and findings will now be considered by the Ministry of Housing, Communities and Local Government and we look forward to working with all stakeholders to implement changes to ensure the development and sustainability of local audit.

The full report is available here: <https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-independent-review>



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