ITEM 5

Deloitte.

North Yorkshire County Council

North Yorkshire County Council

Report to the Audit Committee on the audit for the year ended 31 March 2019

Issued 19 July 2019 for the meeting on 22 July 2019

Contents

Partner introduction

The key messages in this report:

I have pleasure in presenting our final report to the Audit Committee for the 2019 audit. I would like to draw your attention to the key messages of this paper:

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the financial statements.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

Status of the audit

We have the following principal matters to complete as part of our audit:

- Notes testing including cash flow;
- Completion of VfM work;
- Update of the pension liability and disclosures for the impact of the McCloud judgement;
- Receipt of information from Pension Fund auditors;
- Journals testing;
- Testing of bad debt provision;
- Completion of provisions testing;
- Testing of headcount reports;
- Testing of off ledger adjustments;
- Completion of revaluation work;
- Fees and charges income and expenditure testing;
- Completion of internal quality assurance procedures including follow-up queries arising from these; and
- Receipt of signed management representation letter; and
- Our review of events since 31 March 2019 through to signing.

Conclusions from our testing

The key judgements in the audit process related to:

- Completeness and cut-off of service line expenditure;
- Property Valuation;
- Pension liabilities; and
- Management override of controls.

We have identified a number of immaterial audit adjustments and disclosure deficiencies as part of our audit, management are in the process of updating these in the financial statements and we will conduct a final review once completed. Audit insights, recommendations and unadjusted misstatements are discussed on pages 13, 14 and 23 respectively.

Based on the current status of our audit work, we envisage issuing an unmodified audit opinion, with no reference to any matters in respect of the Council’s arrangements to secure economy, efficiency and effectiveness in the use of resources, or the Annual Governance Statement.

Partner introduction
The key messages in this report (continued)

Financial sustainability and Value for Money	• The Council reported a deficit on the provision of services of £108m for the year which included a one off charge of £104m in respect of schools converting to academies. As at 31 March 2019, the Council had £234m of useable reserves. Cost saving delivery in 2018/19 was £16.0m against a £15.5m target. • The Council set a balanced budget for 2019/20 which included use of £5.3m reserves. The budget assumes £15.4m of savings which is broadly consistent with savings achieved in 2018/19. • We do not anticipate reporting any matters within our audit report in respect of the Council's arrangements for securing the economy, efficiency and effectiveness of the use of resources.
Narrative Report & Annual Governance Statement	• We have reviewed the Council's Annual Report & Annual Governance Statement to consider whether it is misleading or inconsistent with other information known to us from our audit work. • The Annual Governance Statement complies with the Delivering Good Governance guidance issued by CIPFA/SOLACE. • We have suggested a number of minor changes to management for consideration.
Duties as public auditor	• We did not receive any queries or objections from local electors this year. • We have not identified any matters that would require us to issue a public interest report. We have not had to exercise any other audit powers under the Local Audit and Accountability Act 2014.
Whole of Government Accounts	• We are required to report our overall audit opinion and key issues from our audit to the National Audit Office following completion of the audit. We are required to perform testing on the Council's WGA submission, checking its consistency to the audited financial statements and reporting our findings to the National Audit Office (together with our audit opinion and key issues from our audit.

Paul Thomson
Audit Partner

Our audit explained

Conclude on significant risk areas

We draw to the Audit Committee's attention to our update on the significant audit risks. See pages 7 to 11.

Final audit report

In this report we have concluded on the audit risks identified in our planning report and any other key findings from the audit.

Key developments in your business

As noted in our planning report, the Council continues to face challenges in relation to overspend in Children and Young People's Services.

Materiality

Group materiality of £20.8m (Council only £20.7m) has been based on the benchmark of gross expenditure and is a small increase from what we reported in our planning paper due to the updated final figures.

We have used these as the basis for our scoping exercise and initial risk assessment. We have reported to you all uncorrected misstatements greater than £1m.

Significant risks

Our risk assessment process is a continuous cycle throughout the year. Page 7 provides a summary of our risk assessment of your significant risks.

Quality and Independence

We confirm we are independent of North Yorkshire County Council. We take our independence and the quality of the audit work we perform very seriously. Audit quality is our number one priority.

Scope of the audit

We have scoped in line with the Code of Audit Practice issued by the NAO.

We have audited the group financial statements for the year ended 31 March 2019 of North Yorkshire County Council. This includes the Council, and the consolidated balances from NYnet Limited and Yorwaste Limited.

Timeline 2018/19

November 2018 – February 2019
Meetings with management and other staff to develop our understanding of the council's processes and controls.

26 February 2019
Presented planning paper to the Audit Committee

31 March 2019
Year end

June-July 2019
Review of draft accounts, testing of significant risk and performance of substantive testing of results.

8 July2019
Audit close meeting

22 July 2019
Audit Committee meeting

31 July 2019
Accounts sign off

Our audit explained: Scope of work and approach

We have three key areas of responsibility under the Audit Code

Financial statements

We have conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISA (UK and Ireland)") as adopted by the UK Auditing Practices Board ("APB") and Code of Audit Practice issued by the National Audit Office ("NAO"). The Council have prepared its accounts under the Code of Practice on Local Authority Accounting ("the Code") issued by CIPFA and LASAAC.

We are also required to issue a separate assurance report to the NAO on the Council's separate return required for the purposes of its audit of the Whole of Government Accounts and departmental accounts. This has a deadline of the 13th of September, which we expect to achieve.

Annual Governance Statement

We have considered the completeness of the disclosures in the Annual Governance Statement in meeting the relevant requirements and identified any inconsistencies between the disclosures and the information that we are aware of from our work on the financial statements and other work.

As part of our work we have reviewed the remuneration report and annual report and compared with other available information to ensure there are no material inconsistencies. We have also reviewed any reports from other relevant regulatory bodies and any related action plans developed by the Council.

Value for Money conclusion

We have satisfied ourselves that the Council has made proper arrangements for securing financial sustainability and economy, efficiency and effectiveness in its use of resources.
To perform this work, we have:

- planned our work based on consideration of the significant risks of giving a wrong conclusion; and
- carried out as much work as is appropriate to enable us to give a safe conclusion on the arrangements to secure VFM.

Our work therefore included a detailed risk assessment based on the risk factors identified in the course of our audits. No significant risks were identified based on our risk assessment and therefore no specific detailed testing was undertaken.

We have then provided a conclusion on these arrangements as part of our final reporting to you, see page 12.

Significant risks
Dashboard

Risk	Material	Fraud risk	Planned approach to controls	Controls D+I testing conclusion	Consistency of judgements with Deloitte's expectations	Slide no.
Completeness and Cut off of expenditure	✓	✓	D+I	Satisfactory	TBC	7
Property valuations	✓	✗	D+I	Satisfactory	TBC	8
Management override of controls	✓	✓	D+I	Satisfactory	TBC	9
Pension Liabilities	✓	✗	D+I	Satisfactory	TBC	10

Overly prudent, likely to lead to future credit − − ● + + Overly optimistic, likely to lead to future debit.

D+I: Assessing the design and determining the implementation of key controls

Significant risks
Completeness and cut off of service line expenditure

Risk identified	Under UK auditing standards, there is a presumed risk of revenue recognition due to fraud. We have rebutted this risk, and instead believe that the fraud risk lies with the completeness and cut-off of expenditure. We identify this as expenditure excluding payroll costs, depreciation and amortisation and expenditure which is grant backed. There is an inherent fraud risk associated with the under recording of expenditure in order for the Council to report a more favourable year-end position.
Deloitte response	Our work in this area included the following: • We obtained an understanding of the design and implementation of the key controls in place in relation to recording completeness and cut-off of expenditure (excluding payroll, depreciation and amortisation, and expenditure which is grant backed); • We performed focused testing in relation to the completeness and cut-off of service line expenditure (excluding the areas set out above) including detailed reviews of provisions and accruals; and, • We are in the process of completing our review and challenge of the assumptions made in relation to year-end estimates and judgements to assess completeness and accuracy of recorded service line expenditure.
Conclusion	From our work to date we have not identified any errors in our testing of completeness and cut off of service line expenditure, and have noted no issues with management’s judgements in relation to this risk. However, as our work in this area remains in progress we will provide a verbal update at the Committee meeting.

Significant risks

Property valuations

Risk identified	The council held £1,009m of land and building property assets at 31 March 2018 which has decreased to £963m as at 31 March 2019. The decrease was primarily due to disposals of £106m offset by £6m of additions, and upwards revaluations of £54m as a result of the Council undertaking a revaluation exercise in 2018/19. 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 Council 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. There is therefore a risk that that the value of property assets materially differ from the year end fair value.
Deloitte response	Our work in this area included the following: • We tested the design and implementation of key controls in place around the property valuation; and • We tested a sample of revalued assets and re-performed the calculation assessing whether the movement has been recorded through the correct line of the accounts. We utilised our valuation specialists, Deloitte Real Estate, to support our work in the following areas: • We reviewed revaluations performed in the year, and assessed whether they have been performed in a reasonable manner, on a timely basis and by suitably qualified individuals, using appropriate inputs and that appropriate consideration and adjustment has been made to ensure that the valuation as at the valuation date is valid at the year end; • We reviewed the approach used by the Council to assess the risk that assets not subject to revaluation are materially misstated; and • We challenge the appropriateness of the Council's assumptions on its asset valuations between April 2018 and year end.
Conclusion	We have raised a number of recommendations in relation to the Council's processes around the property valuation. Please see page 14 for details. From our work to date, we have not identified any indications that the net book value of property assets is materially misstated. The Council's valuation assumptions are generally reasonable, in line with other Councils and fall within the expected range highlighted by our valuation specialists, Deloitte Real Estate. As our work in this area remains in progress we will provide a verbal update at the Committee meeting.

Significant risks
Management override of controls

Risk identified	In accordance with ISA 240 (UK and Ireland) management override of controls is a significant risk due to fraud for all entities. This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Council's controls for specific transactions. The key judgements in the financial statements include those which we have selected to be the significant audit risks, (completeness and cut-off of expenditure, Pensions liabilities, and the Council's property valuations) and any one off and unusual transactions where management could show bias. These are inherently the areas in which management has the potential to use their judgment to influence the financial statements.
Deloitte response	In considering the risk of management override, we have performed the following audit procedures that directly address this risk: • We tested the design and implementation of key controls in place around journal entries and key management estimates; • We risk assessed journals and selected items for detailed testing. The journal entries were selected using computer-assisted profiling based on areas which we considered to be of increased interest; • We reviewed accounting estimates for biases that could result in material misstatements due to fraud; and, • We obtained an understanding of the business rationale of significant transactions that we became aware of that are outside of the normal course of business for the Council, or that otherwise appeared to be unusual, given our understanding of the entity and its environment.
Conclusion	Our work in relation to this risk is ongoing but to date we have not identified any issues in relation to management override. We will provide a verbal update to the Committee on our progress.

Significant risks
Pension Liabilities

Risk identified	The net pension liability is a material element of the Council's balance sheet. The Council is an admitted body of the North Yorkshire Pension Fund. The actuarial valuation of the Scheme relies on a number of assumptions, including actuarial assumptions, and actuarial methodology which results in the Council's overall valuation. Furthermore there are financial and demographic assumptions used in the calculation of the Council's valuation – e.g. the discount rate, inflation rates, mortality rates. These assumptions should also reflect the profile of the Council's employees, and should be based on appropriate data. There is a risk that the assumptions and methodology used in the valuation of the Council's pension obligation are not reasonable. This could have a material impact to the net pension liability accounted for in the financial statements.
Deloitte response	Our work in this area included the following: • We obtained an understanding of the design and implementation of the key controls in place in relation to the assumptions used by the Council and over information sent to the Scheme actuary; • We have evaluated the competency, objectivity and independence of the actuarial specialist; • We have reviewed the methodology and appropriateness of the assumptions used in the valuation, utilising a Deloitte Actuary to provide specialist assessment of the variables used; • We have engaged with the Deloitte Pension Fund audit team to gain further assurance over the completeness and accuracy of pension data provided to the Pension Fund; • We have reviewed the pension related disclosures in the financial accounts; and, • We have considered the valuation of pension assets.
Conclusion	The Council obtained an updated actuarial report to allow them to adjust the pension liability for the impact of the McCloud case, the adjustment has been included in the latest version of the financial statements. Our internal pensions specialists are in the process of reviewing the updated report. As our work in this area remains in progress we will provide a verbal update at the Committee meeting.

Value for Money

We have not identified any VfM significant risks

Under the National Audit Office's Code of Audit Practice, we are required to report whether, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources. The Code and supporting Auditor Guidance Notes require us to perform a risk assessment to identify any risks that have the potential to cause us to reach an inappropriate conclusion on the audited body's arrangements. We are required to carry out further work where we identify a significant risk - if we do not identify any significant risks, there is no requirement to carry out further work.

Our response

Our work in this area included:

- Obtaining an understanding of the Council's Medium Term Financial Plan, budget for 2019/20 and transformation programmes.
- Discussions with the Corporate Director – Strategic Resources, and senior operational staff;
- Review of the Council's draft Narrative Report, Annual Governance Statement and Council papers and minutes;
- Consideration of issues identified in our financial statements audit work;
- Consideration of the Council's financial results, including delivery of savings, and the Council's medium term financial plan; and
- Review of any reports from regulators e.g. Ofsted, issued in the year.

Our work is ongoing but we have not currently identified any significant VfM risks.

Deloitte view

The Council current has a strong financial position with large useable reserves. The Council expects that it will be required to deliver £40.3m of savings between 2019/20 and 2021/22 of which currently proposals for £26.3m have been identified. Achievement of identified savings and development of further savings opportunities will play an important role in the Council's ability to meet its medium term plans.

Other matters
Implementation of IFRS 9 and IFRS 15

Matter identified	The Council is required to adopt the new accounting standards IFRS 9 *Financial Instruments* and IFRS 15 *Revenues from contracts with customers* in the year ended 31 March 2019. In both cases, the Council is using a modified retrospective approach to implementation where effectively the cumulative impact of transition to 1 April 2018 is posted as an adjustment to reserves. The scope of IFRS 9 and IFRS 15 is limited to balances arising on "exchange" transactions. Non-exchange debtors, such as council tax and rates are outside of the scope of IFRS 9 and IFRS 15. The Council has posted no retrospective adjustments with regard to IFRS 9 or IFRS 15 as there is no material impact on the financial statements.
Response	Management held discussions regarding the accounting impact of the new standards on the Council for the period and determined that the impact is immaterial. The key element impacted by IFRS 9 is the accounting for the bad debt provision for debtors, which must move to a methodology of expected credit losses. Whilst the provision as a whole is not material, we have reviewed the revised calculation methodology and considered the assumptions in light of past experience. We have concluded that IFRS 9 has been applied appropriately and no material adjustment is needed. As a point of best practice consideration could be given to adapting the presentation of the note for the new standard. Regarding IFRS 15, management was satisfied that no transitional adjustments would be required due to the Council's sources of income not requiring material adjustment under the new standard. We have reviewed and challenged management's assumptions in light of the Council's contractual arrangements with no issues noted.

Deloitte view

We agree with management's position that the new accounting standards do not have a material impact for the Council. No issues to note.

Other significant findings
Internal control and risk management

During the course of our audit we have identified a number of internal control and risk management findings, which we have included below for information.

Area	Observation	Priority
Preparation for IFRS 16	The implementation of IFRS 16, Leases, for 2020/21 is expected to have a greater and more complex impact upon most Councils than the adoption of IFRS 9 and 15. The scope and potential complexity of work required, which may require system or process changes to underpin correct accounting under the standard, will require work to be completed at a significantly earlier stage than has been the case for IFRS 9 and 15 to allow for financial reporting timetables to be met. We recommend the Council targets completion of its IFRS 16 impact analysis during 2019/20, and to calculate an adjusted opening balance sheet position for audit following the 31 March 2020 audit. We recommend early consideration following the impact analysis of actions required to embed IFRS 16 accounting in the Council's underlying accounting systems.	
Review of property valuation figures by Finance	Whilst there is a process in place where finance review the draft valuation figures and discuss any large movements with the valuer, this process is not formally documented. It is recommended that finance document their review of the draft valuation report, and any subsequent challenge made to the valuer.	
Journal process controls	From our work on the design and implementation of the controls in place around the posting of journals, it has been noted that there is no review of journals performed prior to posting. In addition to this, there is also no limits in place on the value of journals an individual can post. We recommend that controls in place around the journal process are tightened to ensure a review takes place prior to posting.	
Property valuations	For assets in categories which are not part of the formal revaluation in the current year a sample of individual assets is reviewed to identify any significant movements. Our audit work in this area identified a potential issue where a sampled asset with an unrepresentative valuation movement may distort the overall movement being applied to the wider category of assets. We recommend that as part of the process an exercise is undertaken to confirm that the valuation movements on the samples assets are representative of the wider movements within the category.	

Other significant findings (continued)
Internal control and risk management

During the course of our audit we have identified a number of internal control and risk management findings, which we have included below for information.

Area	Observation	Priority
No formal classification of data regarding its sensitivity	It has been noted that the Council do not formally classify data in terms of its sensitivity. The failure to classify data in the correct manner increases the risk that sensitive data is improperly handled by staff members or third parties culminating in an information security breach, which may result in a financial, legal and reputation impact.	
No formal SLAs in place with third party Heywood	It has been noted that there are no formal Service Level Agreements (SLAs) in place with the third party, Heywood and the Pension Fund. This leads to the Pension Fund receiving no assurance over the operational of key IT general computer controls including information security, change management and IT operations.	

Our audit report

Matters relating to the form and content of our report

Here we discuss how the results of the audit impact on other significant sections of our audit report. As noted throughout this report, our work in a number of areas remains ongoing and it is possible that the conclusions below will change as a result of further findings. We will update the Committee in due course.

Our opinion on the financial statements

Based on our work to date we expect our opinion on the financial statements to be unmodified.

Material uncertainty related to going concern

We have not identified a material uncertainty related to going concern and will report by exception regarding the appropriateness of the use of the going concern basis of accounting.

Emphasis of matter and other matter paragraphs

There are no matters we judge to be of fundamental importance in the financial statements that we consider it necessary to draw attention to in an emphasis of matter paragraph.

There are no matters relevant to users' understanding of the audit that we consider necessary to communicate in an other matter paragraph.

Our value for money conclusion

We are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources (value for money).

Based on our work to date we expect our conclusion on the Council's arrangements to be unmodified.

Other reporting responsibilities

The Annual Report is reviewed in its entirety for material consistency with the financial statements and the audit work performed and to ensure that they are fair, balanced and reasonable.

Your annual report

We are required to provide an opinion on the auditable parts of the remuneration report, the annual governance statement and whether the management commentary has been prepared in accordance with the statutory guidance.

	Requirement	Deloitte response
Narrative Report	The Narrative Report is expected to address (as relevant to the Council): - Organisational overview and external environment; - Governance; - Operational Model; - Risks and opportunities; - Strategy and resource allocation; - Performance; - Outlook; and - Basis of preparation.	We have assessed whether the Narrative Report has been prepared in accordance with CIPFA guidance. We have also read the Narrative Report for consistency with the annual accounts and our knowledge acquired during the course of performing the audit, and is not otherwise misleading. Our review identified a number of areas where the Narrative Reports needed revising in order to comply with guidance and to ensure that they were fair, balanced and understandable, these changes have been reflected in the final version.
Annual Governance Statement	The Annual Governance Statement reports that North Yorkshire County Council's governance arrangements provide assurance, are adequate and are operating effectively.	We have assessed whether the information given in the Annual Governance Statement meets the disclosure requirements set out in CIPFA/SOLACE guidance, is misleading, or is inconsistent with other information from our audit. No issues were noted from our review.

UK exit from the EU

Navigating uncertainty – key questions for the audit committee

Is North Yorkshire County Council set up to navigate the change?

Have you assessed the impact of potential changes and identified key decision points?

Does your assessment include how Brexit could impact on your residents, supply chain and people?

Will additional financing facilities be needed?

Have you defined the options there are to respond? E.g. scenario or contingency planning?

Are you monitoring developments and are you ready to act proportionately at the right time?

Are all the right people involved? Does this include discussion with key stakeholders?

Are channels of communication clear, both internally and externally, and have company spokespeople been fully briefed?

FRC Letter to CFOs and Audit Committee Chairs, October 2018:

"We encourage companies to provide disclosure which distinguishes between the specific and direct challenges to their business model and operations from the broader economic uncertainties which may still attach to the UK's position when they report. Where there are particular threats, for example the possible effect of changes in import/export taxes or delays to their supply chain, we expect these to be clearly identified and for management to describe any actions they are taking, or have taken, to manage the potential impact. In some circumstances this may mean recognising or re-measuring certain items in the balance sheet.

The broad uncertainties that may still attach to Brexit when companies report will require disclosure of sufficient information to help users understand the degree of sensitivity of assets and liabilities to changes in management's assumptions."

UK exit from the EU

Navigating uncertainty – key questions for the audit committee

Impact on internal planning, forecasting and strategy

Is management using forward-looking indicators such as forward bookings, contact conversion rates and supplier forward pricing?

Is there a significant impact from foreign exchange changes and volatility?

Have cash reserves, financing requirements and longer term viability all been assessed?

Have opportunities as well as risks been considered?

Impact on internal and external audit

Should the scope and plan for internal audit be amended to include contingency planning, or testing key risk indicators?

Should internal audit be asked to perform work on longer term viability?

Is there an impact on critical accounting judgments and areas of estimation uncertainty that need to be discussed with the external auditor?

Impact on external reporting

Will disclosures on principal risks and uncertainties need to be revisited now Article 50 has been triggered and the draft Withdrawal Treaty has been published.

Does longer term viability statement account for the fact that the end of the exit negotiation period is now within the lookout period?

Does the Narrative report include appropriately detailed disclosure?

UK exit from the EU (continued)

Impact on our audit

There is a need to consider implications for your business and for accounting and reporting matters to address in annual reporting.

Area	Management actions	Impact on financial statements	Impact on our audit
Principal risks and uncertainties	Management have undertaken a detailed review that considered a wide range of potential impacts. A Brexit risk has been included with the Corporate Risk Register and is being monitored by senior officers and reported to the Audit Committee. Relevant disclosures have been made in the Annual Governance Statement.	You have updated your principal risks to reflect the uncertain position in relation to Brexit.	We have considered the disclosures in your annual report and AGS and no issues were noted.

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our report is designed to help the Audit Committee and the Members discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA (UK) 260 to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes:

- Results of our work on key audit judgements and our observations on the quality of your Narrative Report.
- Our internal control observations.
- Other insights we have identified from our audit.

What we don't report

As you will be aware, our audit was not designed to identify all matters that may be relevant to the Council.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

The scope of our work

Our observations are developed in the context of our audit of the financial statements.

We described the scope of our work in our audit plan.

Use of this report

This report has been prepared for the Audit Committee and the Council, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

We welcome the opportunity to discuss our report with you and receive your feedback.

Deloitte LLP

Leeds| 19 July 2019

Appendices

Audit adjustments

Unadjusted misstatements

The following uncorrected misstatements have been identified up to the date of this report which we request that you ask management to correct as required by ISAs (UK). Uncorrected misstatements increase the deficit by £6 million, (decrease) net assets by £6 million and would (decrease) the general fund by £1 million.

		Debit/ (credit) income statement £m	Debit/ (credit) in net assets £m	Debit/ (credit) prior year retained earnings £m	Debit/ (credit) OCI/Equity £m	If applicable, control deficiency identified
Misstatements identified in current year						
Dr Pension	[1]	5				
Cr Pension liability	[1]		(5)			
Aggregation of misstatements individually < £1m						
	[2]	1	(1)			
Total		**6**	**(6)**			

[1] Judgemental balance in relation to the recognition of an element of the impact of GMP equalisation in the pension liability.

[2] Aggregate of a small number misstatement below our clearly trivial threshold largest of which relates to an adjustment to the bad debt provision.

Audit adjustments
Disclosures

Disclosure misstatements

From our work to date a number of disclosure deficiencies were identified, management have confirmed that they will update for all significant deficiencies and we will undertake a final review once this have been completed. However, our work is ongoing and we will provide an update to the committee on any additional disclosure deficiencies identified.

Fraud responsibilities and representations

Responsibilities explained

Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.

Required representations:

We have asked the Council to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the financial statements may be materially misstated as a result of fraud and that you are not aware of any fraud or suspected fraud that affects the entity or group.

We have also asked the Council to confirm in writing their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

Audit work performed:

In our planning we identified the risk of fraud in management override of controls, and completeness and cut-off of expenditure as a key audit risk for your organisation.

During the course of our audit, we have had discussions with management and those charged with governance, and no significant issues were raised that would require a change to our audit plan.

In addition, we have reviewed management's own documented procedures regarding fraud and error in the financial statements

We have reviewed the paper prepared by management for the audit committee on the process for identifying, evaluating and managing the system of internal financial control.

Concerns:

No concerns have been identified from whistle blowing procedures and our audit procedures.

Independence and fees

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Council and and our objectivity is not compromised.
Fees	There are no non-audit fees for 2018/19.
Non-audit services	In our opinion there are no inconsistencies between the FRC's Ethical Standard and the company's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.
Relationships	We have not other relationships with the Council, its directors, senior managers and affiliates, and have not supplied any services to other known connected parties.

Independence and fees

The professional fees expected to be charged by Deloitte in the period from 1 April 2018 to 31 March 2019 are as follows:

	Current year £
Financial statement audit including Whole of Government and procedures in respect of Value for Money assessment	72,757
Total audit	**72,757**
Audit related assurance services	-
Total assurance services	**-**
Total fees	**72,757**

Deloitte.

North Yorkshire Pension Fund

Final report to the Audit Committee for the year ended 31 March 2019

Issued 19 July 2019 for the meeting on 22 July 2019

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Contents

Partner introduction
The key messages in this report

I have pleasure in presenting our final report for the 2019 audit of North Yorkshire Pension Fund ("the Fund"). The areas of significant risk identified in that report have remained consistent throughout our testing and have been focal to the performance of our audit. I would like to draw your attention to the following key messages:

Audit quality is our number one priority.

We plan our audit to focus on audit quality and have followed the following audit quality objectives for this audit:

- A **robust** challenge of the key judgements taken in the preparation of the financial statements.
- A strong **understanding** of your internal control environment.
- A **well planned** and delivered audit that raises findings early with those charged with governance.

Significant audit risk and areas of audit focus

In our planning report we identified management override of controls as our significant risk. Further details of the audit procedures on the significant audit risk can be found on page 6.

The audit procedures on the areas of focus can be found on pages 8 to 10.

Status of the audit

We are currently progressing the audit towards completion. We have detailed the procedures still to be completed in appendix 4 and our final opinion is subject to completion of these items.

Audit Quality & Insight

We have completed our audit in line with our planning report dated February 2019.

We have committed to delivering a robust challenge of the key judgements taken in the preparation of the financial statements; to gain a strong understanding of your internal control environment; and to deliver a well planned audit that raises findings early with those charged with governance.

Our audit findings and insights can be found on pages 12 to 16. A detail of unadjusted misstatements can be found in appendix 3.

Subject to the satisfactory receipt and the completion of the items above we expect to issue an unmodified audit opinion on the financial statements.

Paul Thomson
Audit Partner

Materiality

Our approach to materiality - Fund

Basis of our materiality benchmark

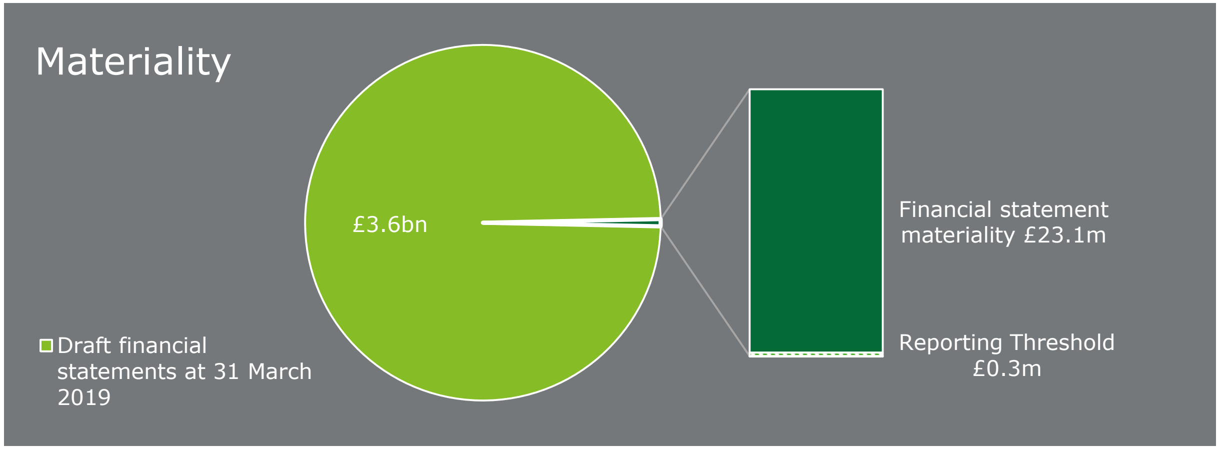
- We have determined financial statement materiality to be £23.1m based on professional judgement, the requirement of auditing standards, and the net assets of the Fund. During the audit we have considered, together with the North Yorkshire County Council audit team, whether any reduction is required to the level of materiality applied to the Fund.
- We have used the lower of 1% of Fund net assets and the grossed up materiality of the smallest body we are giving assurance to. 1% of net assets is £35.7m and the grossed up materiality of the smallest body we are giving assurance to is £23.1m, so we have capped materiality to the latter amount.

Reporting to those charged with governance

- We will report to you all misstatements found in excess of 5% of financial statement materiality. We will report to you misstatements below this threshold if we consider them to be material by nature.

Materiality calculation

Although materiality is the judgement of the audit partner, the Audit Committee members must satisfy themselves that the level of materiality chosen is appropriate for the scope of the audit.



Significant audit risks and other areas of audit focus

An overview

Risk Identified	Material Balance	Management Judgement	Proposed Approach	Fraud Risk	Further Details
Significant risk Management override of controls	✗	△	**D&I**	✓	Pg. 7
Other Focus Area Completeness & valuation of investments	✓	△	**D&I**	✗	Pg. 9
Other Focus Area Completeness & accuracy of contributions	✓	△	**D&I**	✗	Pg. 10

Significant risk	Low levels of management judgement/complexity	**D&I** Design and Implementation
Other area of audit focus	Medium levels of management judgement/complexity	**OE** Operating Effectiveness
	High degree of management judgement/complexity	

Significant audit risks

Significant risks

Management override of controls

Significant Risk

D&I

Risk identified

In accordance with ISA 240 (UK) management override is always a significant risk for financial statement audits. The primary risk areas surrounding the management override of internal controls are over the processing of journal entries and the key assumptions and estimates made by management.

Response of those charged with governance	Deloitte response to significant risk identified
The financial reporting process in place has an adequate level of segregation of duties.	In order to address the significant risk our audit procedures consisted of the following: • Used Spotlight, our data analytics software, in our journals testing to interrogate 100% of journals posted across the Fund. This uses intelligent algorithms that identify higher risk and unusual items; • Made inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments; • Performed a walkthrough of the financial reporting process to identify the controls over journal entries and other adjustments posted in the preparation of the financial statements; • Assessed whether that there is an appropriate level of segregation of duties over processing journal entries to the financial statements throughout the year; • Tested the design and implementation of controls around the journals process; • Reviewed related party transactions and balances to identify if any inappropriate transactions have taken place; and • Reviewed the accounting estimates for bias, that could result in material misstatement due to fraud, including whether any differences between estimates best supported by evidence and those in the financial statements, even if individually reasonable, indicate a possible bias on the part of management.

Findings

There are no issues arising from our testing performed to date that would indicate that there have been any instances of management override of controls during the period.

There is no review of individual journals posted, increasing the risk for errors. This is partly mitigated through a weekly bank reconciliation, which covers the majority of contributions and benefits journals.

Audit focus areas

Audit focus areas
Completeness and valuation of investments

Focus Area

D&I

Area of focus identified

The Fund holds a large and highly material portfolio of investments and due to the ongoing changes and numerous transactions within this portfolio, there is considered an increased risk of material misstatement.

Additionally, within this portfolio is a range of alternative investments, including c.£157m invested with Leadenhall during the Fund year. These funds do not have publicly available prices and are often infrequently priced increasing the risk of stale pricing.

As a result of this we consider the completeness and valuation of these investments to be an area of audit focus.

Response of those charged with governance

The Fund appoints various investment managers and BNYM as custodian for these investments. These parties have strong control environments in place.

Findings

From our audit testing to date, we noted the following:

- The Aberdeen Standard Liquidity Fund (£7.0m year end value) is currently disclosed under Cash and cash equivalents in note 14a of the draft financial statements. As this is a Pooled Investment Vehicle, it should be disclosed under that heading. The result of the current classification is that £21.3m purchases and £14.4m sales are not presented accurately in note 11a. While not considered material, this is a disclosure deficiency.
- A judgemental difference in the valuation of fixed interest securities between M&G and Bloomberg of £2.8m.

Finally we noted a judgemental unreconciled difference of £5.4m (or 0.2%) between the investment manager reports received directly by Deloitte and the BNYM custodian report. Whilst not material to the accounts, this amount is included on Appendix 3 as an unadjusted error.

Deloitte response to the focus area identified

In order to address this area of audit focus, we have performed the following audit procedures:

- Reviewed the design and implementation of key controls over the completeness and valuation of investments by obtaining the investment manager internal control reports (where applicable) and evaluating the implications for our audit of any exceptions noted;
- Agreed year end valuations, sales and purchases amounts in the accounts to the reports received directly from BNYM (investment custodian) and reconciled these to the individual confirmations received from the investment managers;
- Agreed registered funds and directly held investments to publicly available prices;
- Performed independent valuation testing for a sample of year end alternative investment holdings by rolling forward the valuation as per the latest audited account using cashflows and an appropriate index as a benchmark;
- Ensured appropriate stale price adjustments have been posted to the financial statements;
- Performed a unit reconciliation in which the opening investment balances and unit quantities are reconciled to the closing investment balances and unit quantities by taking into account the movement that occurred during the year, (i.e. sales, purchases, change in market value); and
- Tested the completeness of investments by agreeing a sample of sales and purchases transactions to the investment manager confirmations.

Audit focus areas
Completeness and accuracy of contributions

Focus Area

D&I

Area of focus identified

There is some complexity surrounding the completeness and accuracy of employer and employee contributions received by the Fund. The employer primary and secondary contribution rates are dictated by the actuarial valuation and these vary between the contributing employers. Employee contributions are based on varying percentages of employee pensionable pay, this can vary month to month and the Fund has no oversight of the individual employer payrolls.

As a result of this we would expect the accuracy and completeness of contributions to be an area of audit focus.

Response of those charged with governance

The administration team monitors the due dates of contributions and that the correct amounts are received into the Fund bank account to ensure that payments are in accordance with the actuarial valuation.

Employers must also complete a contributions return confirming that the contributions paid during the year are accurate and complete.

Findings

There are no issues arising from our testing performed.

Deloitte response to the focus area identified

In order to address this area of audit focus, we performed the following audit procedures:

- Considered the design and implementation of key controls over the contribution process;
- Performed an analytical review of the employer and employee normal contributions received in the year, basing our expectation on the prior year audited balance, adjusted for the movement in active member numbers, contribution rate changes and any average pay rise awarded in the year;
- Tied a sample of employer contributions received during the year back to the contribution rates stipulated in the 31 March 2016 actuarial valuation; and
- For a sample of active members across the Fund, we recalculated individual contribution deductions to confirm that these were calculated in accordance with the rates stipulated by the LGPS and in the 31 March 2016 actuarial valuation.

Other findings

Other findings

Finding

Heywood Altair system – no formal Service Level Agreement (SLA)

Finding

It has been noted that the North Yorkshire County Council (the ‘Council’) are responsible for the hosting and maintenance of the Heywood Altair system, the main pension administration system for North Yorkshire Pension Fund. The Pension Fund do not receive Service Auditor Reports (SARs) from the Council and there are no formal SLAs in place with them. There is also no independent monitoring from management at North Yorkshire Pension Fund over the main pension administration system that is hosted externally. This leads to the Pension Fund receiving no assurance over the operation of key IT general computer controls including information security, change management and IT operations.

In mitigation, there are general SLAs in place within the Council that are used across all services that the Council obtain a business relationship with therefore there are general expectations outlined between the Council and Pension Fund, although not specific to the needs of the Pension Fund. The Council hosts a range of services for external organisations. With this, the Pension Fund are able to gain a some assurance over the security and operating effectiveness of the controls the Council holds over the underlying infrastructure of the Heywood Altair system.

Recommendation

Formal Service Level Agreements should be put in place between the Council and the Fund, so as to ensure that the Fund receives assurance over the operation of key IT general computer controls.

Other findings

Unit reconciliation of investments

Finding

Finding

We have found that the pensions team does not perform a unit reconciliation of investments, but instead rely on what is done by the global custodian, BNY Mellon. This increases the risk that a sale and/or purchase of an investment goes unnoticed, as the change in market value is in effect a balancing number in the annual reconciliation.

Recommendation

We recommend that the pensions team perform a regular unit reconciliation of the investment holdings, thus ensuring completeness of transactions.

Such a reconciliation would also provide a robust process of control for monitoring a key service organisation.

Other findings

Contributions workbook

Finding

Finding

An excel workbook is sent to all employers by the pensions administration team at the start of the Fund year stating the employer rates required, any deficit payments as well as the type of payment (12 set monthly payments based on a fixed amount or monthly payments based on pension payroll). This workbook has to be populated by the employers (with member numbers and salaries) and returned to the pensions administration team on a monthly basis. Employers do not always return this form on a monthly basis which can lead to error in recording contributions expected against received. In addition, without the documentation provided the administration team cannot ensure that payments have been received correctly

Moreover, we noted that the Excel workbook rates are not protected, and the employer can change the rates. As the rates are not checked when the workbook is returned, there is an increased risk that any rate changes go unnoticed and contributions are not being paid in line with the rates stipulated by the LGPS guidelines, or latest actuarial valuation.

Recommendation

We recommend that the pensions administration team puts in place a formal requirement for the paperwork to be returned on a monthly basis by the employers, thus ensuring the contributions received are correct.

We also recommend that the workbook that is sent to the employers at the start of the year with the prepopulated rates is protected, thus preventing any changes in rates going unnoticed or being accidently deleted.

Other findings

Contributions payments

Finding

Finding

From discussions with the pension administration team it was noted that a number of smaller employers had not paid contributions on time. We have enquired of the team as to progress in obtaining missed or late contributions and have been informed that these have not been followed up on due to other priorities. There is a risk that required contribution payments by employers go unnoticed, thus increasing the risk of cashflow issues for the Fund.

In addition, we noted that the contributions payments are collated by one member of staff, without backup for when this member is absent. No reconciliation work is as a result done in periods of absence. We also noted the absence of management review of this reconciliation work.

Recommendation

We recommend that the administration team does a monthly reconciliation of missing contributions and puts in place a structure for chasing the relevant employers, with appropriate escalation.

We also recommend that the tracking of pension contributions and all tasks relating to that role are extended to a number of members of the team so that documentation can be kept up to date at all times and that specialist knowledge is not lost. In addition, there should be a regular review of contributions paid by a senior member of the pension team with the random tracing of a sample of payments received to the bank and the monthly contribution workbook provided by the employer.

Other findings

IFA checks

Finding

Finding

When a member is transferring out, the Fund does not perform any checks on whether the Independent Financial Advisor (IFA) is appropriately qualified and registered with the Financial Conduct Authority (FCA). The benefits team does ensure it is authorised to work with the IFA in regards the member information. This increases the risk that the member has not been appropriately advised on transfer options, increasing the risk of legal action against the Fund.

Recommendation

We recommend that the benefits team perform an IFA check as part of the standard checks they do when a member decides to transfer out. In addition, the Regulator recommends that these checks are performed.

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our respective responsibilities are set out in "PSAA Statement of responsibilities of auditors and audited bodies: Principal Local Authorities and Police Bodies.” The responsibilities of auditors are derived from statute, principally the Local Audit and Accountability Act 2014 and from the NAO Code of Audit Practice. The responsibilities of audited bodies are derived principally the Local Audit and Accountability Act 2014 and from the Accounts and Audit Regulations 2015.

Our report is designed to communicate our audit findings. Our report includes our preliminary audit findings, including our conclusions on the significant risks identified in our planning report.

What we don’t report

- As you will be aware, our audit is not designed to identify all matters that may be relevant to the Fund.
- Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by officers or by other specialist advisers.
- Finally, the views on internal controls and business risk assessment in our final report should not be taken as comprehensive or as an opinion on effectiveness since they will be based solely on the audit procedures performed in the audit of the statement of accounts and the other procedures performed in fulfilling our audit plan.

Other relevant communications

We will update you if there are any additional findings resulting from the concluding of the outstanding audit procedures.

This report has been prepared for the Audit Committee, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

Paul Thomson

for and on behalf of Deloitte LLP

Leeds | 19 July 2019

Appendices

Appendix 1: Fraud responsibilities and representations

Responsibilities explained

Your Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and the Panel, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Our responsibilities:

- We are required to obtain representations from your management regarding internal controls, assessment of risk and any known or suspected fraud or misstatement.
- As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.
- As set out in the significant risks section of this document, we have identified the management override of controls as the key audit risk for the Fund.

Fraud Characteristics:

- Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional.
- Two types of intentional misstatements are relevant to us as auditors – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.

We will request the following to be stated in the representation letter signed on behalf of the Audit Committee:

- We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.
- We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- We are not aware of any fraud or suspected fraud in relation to fraud or suspected fraud that we are aware of and that affects the entity or group and involves:
  - (i) management;
  - (ii) employees who have significant roles in internal control; or
  - (iii) others where the fraud could have a material effect on the financial statements.
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

Appendix 1: Fraud responsibilities and representations (continued)

Inquiries

We will make the following inquiries regarding fraud:

Management:

- Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Management's process for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to the Audit Committee regarding its processes for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to employees regarding its views on business practices and ethical behaviour.
- Whether management has knowledge of any actual, suspected or alleged fraud affecting the entity.
- We plan to involve management from outside the finance function in our inquiries.

Internal audit

- Whether internal audit has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain its views about the risks of fraud.

The Audit Committee

- How the Audit Committee exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks.
- Whether the Audit Committee has knowledge of any actual, suspected or alleged fraud affecting the entity.
- The views of the Audit Committee on the most significant fraud risk factors affecting the entity.

Appendix 2: Independence and fees

A Fair and Transparent Fee

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Fund.
Fees	Our audit fee for the year ended 31 March 2019 is £19,206 for the Fund. The above fees exclude VAT and include out of pocket expenses.
Non-audit fees	There are no non-audit fees.
Independence monitoring	We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.
Relationships	We have no other relationships with the Authority, its members, officers and affiliates, and have not supplied any services to other known connected parties.

Appendix 3: Audit adjustments

Unadjusted misstatements and disclosure deficiencies

We have identified the following misstatements and disclosure deficiencies from our audit work, most of which have been corrected by management but we nonetheless bring to your attention.

	Debit/ (credit) in Fund Account £'000	Debit/ (credit) in net assets £'000	If applicable, control deficiency identified
Uncorrected misstatements			
Difference between BNYM custodian report and investment manager reports (judgemental)	5,411	(5,411)	
Difference in valuation of fixed interest securities between M&G and Bloomberg (judgemental)	(2,844)	2,844	
Corrected misstatements			
None			
Total			

Disclosure deficiencies

1) The Aberdeen Standard Liquidity Fund (£7.0m year end value) is currently disclosed under Cash and cash equivalents in note 14a of the financial statements. As this is a Pooled Investment Vehicle, it should really be disclosed under that heading. The result of the current classification is that £21.3m purchases and £14.4m sales are not presented in note 11a. While not considered material, this is a disclosure deficiency.

Appendix 4: Outstanding items

Items outstanding at the date of draft report and still being worked on

- Internal audit reports issued during financial year 2018/19 to obtain and review. These reports were requested.
- Independent bank confirmation at 31 March 2019
- Finalisation of our internal quality control procedures
- Final partner and technical review clearance
- Receipt of the final version of the financial statements
- Receipt of signed management representations letter
- Satisfactory completion of our post year-end events review