



Annual Audit Letter

Year ending 31 March 2018

Council of the Isles of Scilly
March 2019



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Your key Grant Thornton team members are:

Geraldine Daly
Associate Director
T: 0117 305 7741
E: geri.n.daly@uk.gt.com

Andrew Davies
Audit Manager
T: 0117 305 7844
E: andrew.davies@uk.gt.com

Peter Brereton
Executive
T: 0117 305 7888
E: peter.d.brereton@uk.gt.com

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Executive Summary

Purpose

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at the Council of the Isles of Scilly (the Council) for the year ended 31 March 2018.

This Letter is intended to provide a commentary on the results of our work to the Council and external stakeholders, and to highlight issues that we wish to draw to the attention of the public. In preparing this Letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'. We reported the detailed findings from our audit work to full Council as those charged with governance in our Audit Findings Report on 14 December 2018.

Our work

Respective responsibilities

We have carried out our audit in accordance with the NAO's Code of Audit Practice, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

- give an opinion on the Council's financial statements (section two)
- assess the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources (the value for money conclusion) (section three).

In our audit of the Council's financial statements, we comply with International Standards on Auditing (UK) (ISAs) and other guidance issued by the NAO.

| | |
|-------------------------------------|--|
| Materiality | We determined materiality for the audit of the Council's financial statements to be £0.166m, which is 1.3% of the Council's gross revenue expenditure. |
| Financial Statements opinion | We gave an unqualified opinion on the Council's financial statements on 24 December 2018. |
| Use of statutory powers | <p>In 2015/16 we concluded that it was appropriate for us to use our powers to make formal recommendations under section 24 (para 7.2) of the Act due to the Council's current and forecast financial position. Our Audit Findings report dated 14 December 2018 set out the Council's progress against each of these recommendations. This is recreated at on page 5 of this letter.</p> <p>Progress has been made against each of these recommendations, however this has been slow and somewhat disappointing. Whilst we accept that time is needed to fully address each of these points and to ensure they are fully embedded, the Council do need to ensure meaningful long-term progress is made against each of these points in the 2018/19 financial year.</p> <p>Due to the timing of this letter we note that there has been further progress against these recommendations and we will review this progress further as part of our 2018/19 Value for Money work.</p> |
| Value for Money arrangements | <p>We were not satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources. We therefore issued an adverse value for money conclusion in our audit report to the Council on 24 December 2018. The basis for this was:</p> <ul style="list-style-type: none">• The lack of progress in relation to the S24 recommendations around budgetary control, medium term financial planning, capacity and skills and the level of general fund reserves. These have not been fully implemented 2 years after the recommendations were made,• Weaknesses in the overall control environment,• Weaknesses in the arrangements for financial management, and• The findings of an Ofsted report rating the overall effectiveness of the school as inadequate. |

Executive Summary

| | |
|---|---|
| Whole of Government Accounts (WGA) | We completed work on the Council's consolidation return following guidance issued by the NAO. |
| Certification of Grants | We also carry out work to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. Our work on this claim was completed before the national deadline of 30 November 2018. |
| Certificate | We certify that we have completed the audit of the accounts of the Council of the Isles of Scilly in accordance with the requirements of the Code of Audit Practice. |

Working with the Council

The 2017/18 audit process was much improved on previous years with only minor issues noted. The key challenge for the year was the change in accounting systems. Our work concluded that this process was generally well managed. We have supported the Council through this process by:

- Fully engaging and discussing emerging issues throughout the process with both officers and members,
- Providing training to members on the role of audit, our value for money conclusion and section 24 recommendations,
- Undertaking work on the transfer of systems early to give assurance on the overall IT control environment and data transfer,
- We adapted our approach where required,
- We followed up and challenged the S24 recommendations – to drive the required improvements forward.

We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Council's staff.

Grant Thornton UK LLP
March 2019

Responding to our Statutory Recommendations

The table below shows the progress made by the Council in addressing our Section 24 recommendations. This was the position as at December 2018.

| Recommendation | Audit Update | Progress |
|--|---|----------------------|
| <p>Review budgetary control procedures to improve efficiency and timeliness of financial reporting to budget holders and Members, so that Members can make informed decisions through the use of accurate data, forecasting and budget monitoring reports.</p> | <p>Budget monitoring has improved. Quarterly reports were taken to Council throughout 2017/18. Internal audit however gave limited assurance in respect of budget monitoring. This was in relation to training being provided and financial policies being updated. We understand that Internal Audits recommendations have been addressed, however, we have not yet re-assessed this progress.</p> <p>Whilst progress has been made, this recommendation remains in progress.</p> | <p>● (Amber)</p> |
| <p>Review the assumptions underpinning the medium term financial strategy to ensure that adequate resources are available to deliver strategic priorities. This may involve engagement with the relevant Government departments and should include a review of cost pressures being faced in 2017/18 so that appropriate action can be taken through the review of costs, income, savings plans and cash flow forecasts.</p> | <p>The Council have a interim MTFP in place. In reality the Council are concentrating very much on the here and now. The S151 plans to produce a full 4 year MTFP as part of the 2019/20 budget setting process. This will involve revisiting all key underlying assumptions. The LGA will also be involved in this process.</p> <p>This recommendation remains in progress and it is crucial that this actioned within 2018/19. We have re-iterated in this report that the Council have to develop a robust medium term financial plan that supports the Council's strategy.</p> | <p>● (Amber)</p> |
| <p>Ensure that plans are further developed to ensure that they are supported by detailed underlying assumptions that are deliverable and can be monitored.</p> | <p>Savings plans are being developed and will be looked at again in more detail as part of developing the MTFP. There is a current shortfall against the £215k savings target of circa £80k. Reliance upon reserves is not sustainable and therefore it is crucial that as part of developing a medium term financial plan that clear plans are in place to address budget gaps.</p> | <p>● (Amber)</p> |
| <p>Review the capacity and skills required within the finance team.</p> | <p>The Strategic Collaboration has had a positive impact on financial monitoring and reporting as well as service delivery. There are some aspects of the general control environment that still remain to be fully addressed, however this forms part of this collaboration agreement. It is pleasing to note that the Council of the Isles of Scilly have put in place arrangements to monitor the performance of the collaboration and to ensure the services provided are adequate. Capacity and capability have been addressed within the finance and legal functions, however there still remains capacity issues in other areas.</p> <p>This recommendation remains in progress.</p> | <p>● (Amber)</p> |
| <p>Re-examine the level of General Fund reserves. As part of this, the Council should review all grant and reserve balances to ensure that they are being held in accordance with the terms and conditions or for specific purposes.</p> | <p>This exercise was completed when we reported in January 2018. The financial statements presented for audit as at the year end 31/03/18, show that general fund reserves have fallen from £0.999m to £0.802m whilst general fund earmarked reserves have increased slightly from £2.991m to £3.001m. The general fund balance remains below the approved level. The level of reserves have to be continually monitored in light of the councils ongoing financial challenge.</p> | <p>● (Amber)</p> |
| <p>Carry out a 12 month rolling cash flow forecast - as well as a 14 month cash flow forecast from the end of January 2017.</p> | <p>During 2016/17 the CIOS had begun forecasting cash for Treasury Management purposes and to ensure that the relevant finance was available to pay creditors as they arise. We are pleased to be able to report that this forecasting remains in place.</p> | <p>● (Green)</p> |

Audit of the Accounts

Our audit approach

Materiality

In our audit of the Council's financial statements, we use the concept of materiality to determine the nature, timing and extent of our work, and in evaluating the results of our work. We define materiality as the size of the misstatement in the financial statements that would lead a reasonably knowledgeable person to change or influence their economic decisions.

We determined materiality for the audit of the Council's accounts to be £0.166m, which is 1.3% of the Council's gross revenue expenditure. We used this benchmark as, in our view, users of the Council's financial statements are most interested in where the Council has spent its revenue in the year.

We set a lower threshold of £8,300, above which we reported errors to the Council in our Audit Findings Report.

The scope of our audit

Our audit involves obtaining sufficient evidence about the amounts and disclosures in the financial statements to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error. This includes assessing whether:

- the accounting policies are appropriate, have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management are reasonable; and
- the overall presentation of the financial statements gives a true and fair view.

We also read the remainder of the Statement of Accounts, the narrative report and annual governance statement to check they are consistent with our understanding of the Council and with the accounts on which we give our opinion.

We carry out our audit in accordance with ISAs (UK) and the NAO Code of Audit Practice. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach is based on a thorough understanding of the Council's business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks and the results of this work.

Audit of the Accounts

Significant Audit Risks

These are the significant risks which had the greatest impact on our overall strategy and where we focused more of our work.

| Risks identified in our audit plan | How we responded to the risk | Findings and conclusions |
|--|---|--|
| <p>Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue.</p> <p>For the Council of the Isles of Scilly, we have concluded that the greatest risk of material misstatement relates to the occurrence of other income.</p> <p>In 2015/16 we identified a number of material errors where income had been incorrectly recognised. We further reported in 2016/17 that a grant totalling £124k had been incorrectly included in the net cost of services. This was due to the terms and conditions having not been met.</p> <p>Our work in this area also identified a material weakness in controls. This was in relation to the way in which grant income is recognised. The system its current form does not allow efficient and effective recording (and subsequent treatment) of grant income into the general ledger.</p> <p>For these reasons we are unable to rebut the risk of revenue recognition.</p> | <p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> walked through the material revenues streams, for example grant revenues, trading accounts and other revenues. reviewed the application of the revenue recognition policy for all income streams. undertook substantive testing of material revenue transactions and reviewed unusual significant transactions. undertook substantive testing of year end debtors including after date receipts. reviewed control account reconciliations. | <p>In 2016/17 we reported a material weakness in the way that grant income is recognised and subsequently released. Whilst there have been no changes in these processes and controls interim arrangements have ensured that the correct balances have been reported in the 2017/18 financial statements.</p> <p>Our audit work did not identified any issues in respect of revenue recognition.</p> |
| <p>Management override of controls</p> <p>Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities.</p> <p>We identified management override of controls as a risk requiring special audit consideration.</p> | <p>Auditor commentary</p> <p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> reviewed accounting estimates, judgements and decisions made by management. reviewed unusual significant transactions. reviewed significant related party transactions outside the normal course of business. | <p>Our audit work did not identified any issues in respect of revenue recognition.</p> |

Significant audit risk - Going concern

Our responsibility

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

Going concern commentary

Management's assessment process

Management carried out a detailed assessment of the Council's ability to continue as a going concern. This process included undertaking a detailed cash flow forecasts through to 2021-22. As part of this assessment management have considered their general fund and earmarked reserves balances as well as their net current asset position on their balance sheet.

Auditor commentary

- We concluded that management's process were adequate and that the assessment was supported by robust assumptions.

Work performed

We:

- discussed with management the financial standing of the Council;
- reviewed and challenged management's assessment of going concern assumptions and supporting information, e.g. medium term financial planning assumptions and cash flow forecasts;
- reviewed savings targets over the medium term as part of drawing our VFM conclusion.

Auditor commentary

- We reviewed managements assessment and did not identified any issues that lead us to believe that there was a material uncertainty in the Council's assumption in preparing the financial statements on a going concern basis.
- Whilst we qualified the VFM conclusion due to a weak control environment and financial resilience. These were not issues that impact on the Council's ability to continue as a going concern for 12 months from the signing of our audit opinion.
- The Council's General Fund Reserves were below the required £1m level, however, the Council does have the ability to borrow over the medium term.

Concluding comments

Following our review we were satisfied with management's assessment of the use of going concern basis of accounting.

Auditor commentary

Based on the work completed we issued an unmodified audit opinion in relation to going concern.

Our audit work detailed in the VFM section this letter provides more commentary regarding the financial challenge faced by the Council. As part of this work we have recommended that:

- The Council develop a robust medium term financial plan that supports the Councils strategy.
- All assumptions and budget gaps are fully supported and monitored to ensure that they stay relevant, accurate and in line with the Council's strategy.
- Reserve balances are further reviewed to ensure the balances are appropriate.

Audit of the Accounts

Significant Audit Risks (continued)

| Risks identified in our audit plan | How we responded to the risk | Findings and conclusions |
|---|---|---|
| <p>Valuation of property, plant and equipment The Council revalues its assets on a rolling basis over a five year period. The Code requires that the Council ensures that the carrying value at the balance sheet date is not materially different from the current value. This represents a significant estimate by management in the financial statements.</p> <p>We identified the revaluation of land and buildings as a risk requiring special audit consideration.</p> | <p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> • reviewed management's processes and assumptions for the calculation of the estimate. • reviewed the competence, expertise and objectivity of any management experts used. • reviewed the instructions issued to valuation experts and the scope of their work. • held discussions with the Council's valuer about the basis on which the valuation was carried out, challenging the key assumptions. • reviewed and challenged the information used by the valuer to ensure it was robust and consistent with our understanding. • tested revaluations made during the year to ensure they were input correctly into the Council's asset register. | <p>Our audit work did not identify any significant issues in respect of the valuation of property, plant and equipment.</p> <p>As part of our work on the valuation of PPE we noted that the valuation of three assets had not been included in the final AMS report used to produce the financial statements. This led to an understatement on the valuation of PPE of £8,300.</p> <p>This is reported as it is at our level of triviality and hence is required to be reported.</p> |
| <p>Valuation of pension fund net liability The Council's pension fund asset and liability as reflected in its balance sheet represent a significant estimate in the financial statements.</p> <p>We identified the valuation of the pension fund net liability as a risk requiring special audit consideration.</p> | <p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> • identified the controls put in place by management to ensure that the pension fund net liability is not materially misstated and assessed whether those controls were implemented as expected and whether they were sufficient to mitigate the risk of material misstatement. • reviewed the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation. • gained an understanding of the basis on which the IAS 19 valuation was carried out. We also undertook procedures to confirm the reasonableness of the actuarial assumptions made. • reviewed the consistency of the pension fund net liability disclosures in the notes to the financial statements with the actuarial report from your actuary. • obtained assurances from the Auditor of the Pension Fund in relation to their findings. | <p>Our audit work did not identify any issues in respect of the valuation of the pension fund net liability.</p> |

Audit of the Accounts

Significant Audit Risks (continued)

| Risks identified in our audit plan | How we responded to the risk | Findings and conclusions |
|--|--|---|
| <p>Introduction of a new financial system (transfer of data onto ERP)</p> | <p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> • tested the migration of data from the old system to the new, to ensure completeness and accuracy of data. • gained an understanding and documented the processes for both new and old system. • ensured the coding structure in the new systems was capturing the migrated data against the correct account headings. This was to ensure that expenditure was classified correctly. • Completed a review of the overall IT control environment to ensure that the new system included appropriate and expected controls. | <p>No significant issues were identified as part of our work, however the following risks were identified:</p> <p>Alignment of Information Security Policies and Procedures - IT delivery, system and application management is now being co-sourced by Cornwall Council and hence changes have been made in year to the IT arrangements and processes in place at the Council for the Isles of Scilly (COIS). During this period of change it is essential to establish that appropriate security arrangements are in place and that staff are fully aware of any changes in policies they need to abide by. Where policies have not been aligned there is a risk that staff breach organisational, legislative or regulatory requirements by not understanding what their responsibilities are. Also, that staff who do breach security requirements cannot be held accountable through lack of enforceable arrangements to inform them of the responsibilities by Council management.</p> <p>IT Risk Management - During any co-sourcing or shared service arrangement, IT risks should still be reviewed by the individual organisations involved and monitored on a regular basis. The failure to identify, monitor and manage risk could give rise to unexpected system disruption arising from a threat that was not properly assessed and mitigated.</p> <p>Monitoring Service Levels - To ensure an effective co-sourcing or shared service arrangement, management should monitor defined service levels to ensure that the services provided do meet their organisation's needs and ensure satisfactory system performance. These should be monitored on a regular basis. The failure to monitor service levels could mean that system performance is not reviewed for adequacy and anticipated benefits arising from the co-sourcing or shared service arrangements may not be fully realised.</p> <p>We have raised recommendations against each of these risks in Appendix C to this report.</p> |

Audit of the Accounts

Other Audit Risks

In this section we detail our response to the other risks of material misstatement.

| Risks identified in our audit plan | How we responded to the risk | Findings and conclusions |
|--|---|--|
| <p>Employee remuneration Payroll expenditure represents a significant percentage of the Council's operating expenses.</p> <p>As the payroll expenditure comes from a number of individual transactions and an interface with a sub-system there is a risk that payroll expenditure in the accounts could be understated. We therefore identified completeness of payroll expenses as a risk requiring particular audit attention.</p> | <p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> evaluated the Council's accounting policy for recognising payroll expenditure for appropriateness. documented our understanding of processes and key controls over the transaction cycle. Undertook a walkthrough of the key controls to assess whether those controls were in line with our documented understanding. reconciled payroll expenditure reported in the financial statements to total expenditure recorded in the payroll system. performed substantive analytical procedures. | <p>Our audit work did not identified any issues in respect of this risk.</p> |
| <p>Operating expenses Non-pay expenses on other goods and services also represents a significant percentage of the Council's operating expenses. Management uses judgement to estimate accruals of un-invoiced costs.</p> <p>We identified completeness of non- pay expenses as a risk requiring particular audit attention.</p> | <p>We undertook the following work in relation to this risk:</p> <ul style="list-style-type: none"> gained an understanding of the Council's system for accounting for non-pay expenditure and evaluate the design of the associated controls. evaluated the Council's accounting policy for recognition of non-pay expenditure for appropriateness. agreed creditors to the ledger. substantively tested significant creditor balances. reviewed after date payments to ensure all liabilities have been identified. | <p>Our audit work did not identified any significant issues in respect of this risk. We did note that the Council does not currently have an accounting policy which sets a de-minimus level under which amounts are not required to accrued. We raised a recommendation to the Council to implement such a policy as this will ensure decisions not to accrue expenditure are fully documented.</p> |

Audit of the Accounts

Audit opinion

We gave an unqualified opinion on the Council's financial statements on 24 December 2018.

Preparation of the accounts

The Council presented us with draft accounts, and provided a good set of working papers to support them. Whilst this was not in line with the National deadlines the submissions date was improved on the previous year. The finance team responded promptly and efficiently to our queries during the course of the audit.

Issues arising from the audit of the accounts

We reported the key issues from our audit to the Council on 14 December 2018. Recommendations agreed with management can be seen at appendix C.

Annual Governance Statement and Narrative Report

We are required to review the Council's Annual Governance Statement and Narrative Report. It published them on its website in the Statement of Accounts. This was however not in line with the National deadline.

Both documents were prepared in line with the CIPFA Code and relevant supporting guidance. We confirmed that both documents were consistent with the financial statements prepared by the Council and with our knowledge of the Council.

Whole of Government Accounts (WGA)

We are required to carry out specified procedures (on behalf of the NAO) on the Whole of Government Accounts (WGA) consolidation pack under WGA group audit instructions.

This detailed work is not required as the Council does not exceed the threshold.

Other statutory powers

We also have additional powers and duties under the Act, including powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about the Council's accounts and to raise objections received in relation to the accounts.

In 2015/16 we concluded that it was appropriate for us to use our powers to make recommendations under section 24 (para 7.2) of the Act due to the Council's current and forecast financial position.

More detail on progress against these recommendations can be seen at page 5 of this letter.

Certificate of closure of the audit

We are also required to certify that we have completed the audit of the accounts of the Council of the Isles of Scilly in accordance with the requirements of the Code of Audit Practice.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice, following the guidance issued by the NAO in November 2017 which specified the criterion for auditors to evaluate:

In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.

Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the key risks where we concentrated our work.

The key risks we identified and the work we performed are set out overleaf.

As part of our Audit Findings report agreed with the Council in December 2018, we agreed recommendations to address our findings.

- The Council have to develop a robust medium term financial plan that supports the Council's strategy.
- All assumptions and budget gaps should be fully supported and monitored to ensure that they stay relevant, accurate and in line with the Council's strategy.
- Reserve balances have to be further reviewed to ensure the balances are appropriate.
- The Council have to review capacity across the Council to ensure adequate resource is available to achieve the Council's strategy.
- The Council should start to monitor and report against key non financial KPI's as well as key strategic risks.
- The Council should continue to perform key monthly control account reconciliations including cash, purchase and sales ledgers.

Overall Value for Money conclusion

Because of the significance of the matters we identified in our work, we were not satisfied that the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2018. The key factors we considered in reaching this conclusions were:

- The Council's overall control environment,
- Weaknesses in budgetary control,
- The lack of a robust medium term financial plan,
- The uncertainty over the financial challenge,
- The lack of non –financial performance and risk reporting and monitoring,

In addition the Five Islands School remains rated as inadequate, despite visits from inspectors concluding that progress is being made. Until such time as Ofsted has confirmed that adequate arrangements are in place this remains a part of our assessment of the Council's arrangements. In 2018/19 the Five Islands School has become Academy and as such will not form part of our assessment in 2018/19.

Whilst we only consider the arrangements in place during 2017/18 it should be noted that further progress has been made in 2018/19 which is reflected in the narrative on the following pages, but will formally form part of our 2018/19 assessment.

Value for Money conclusion

Key Value for Money Risks

| Risks identified in our audit plan | Findings | Conclusion |
|---|--|---|
| <p>Financial Sustainability The Council has a put a MTFP in place. There are plans to revisit and revise this over the coming months. The Council has reported a draft revenue underspend of £0.109m against a £4.798m budget. This budget included delivery of £0.609m savings of which forecast deliver is reported as being £0.539m. Further savings totalling £0.216m are required in 2018/19.</p> <p>We will review and update our understanding on the MTFP and the assumptions that underpin it. We will review the performance against the 2017/18 savings target and will review the 2018/19 savings plans to ensure that these are realistic and achievable.</p> | <p>In 2017/18 an interim MTFP was put in place, however this was only interim and focused more on the short term i.e the here and now. The Council plan to produce a more robust MTFP in 2018/19 and re-assess the assumptions and savings plans that underpin the plan. The LGA will be involved in this process.</p> <p>In 2017-18 the Council needed to make £0.609m of savings with an additional circa £0.500m over the medium term. The savings target for 2017/18 were effectively delivered as a £0.109m surplus was reported. However this was only achieved by the S151 introducing a moratorium on spend in the latter few months. One off measures and controls like this are not sustainable. General Fund Non earmarked reserves have fallen from £0.999 to £0.802m which is below the required £1m level.</p> <p>It is also unclear if the 17/18 savings were achieved as these were not reported separately.</p> <p>The Council will need to save circa £0.500m over the medium term. This will be a challenge. Schemes are in place for 2018/19 totalling £0.215m, however at quarter 2 2018/19 a shortfall of circa £0.080m is forecast.</p> <p>Reporting performance against savings in 2018/19 are much improved with detailed reports going to Council quarterly.</p> | <p>Based on the arrangements in place for 2017/18 we concluded that there are weaknesses in the Councils arrangements for planning finances to support the sustainable delivery of strategic priorities and maintain statutory functions and planning, organising and developing the workforce effectively to deliver strategic priorities.</p> <p>This conclusion is underpinned by the S24 recommendations that were made in 2015/16. Key to addressing these recommendations are:</p> <ul style="list-style-type: none"> • The Council have to develop a robust medium term financial plan that supports the Councils strategy. • All assumptions and budget gaps have to be fully supported and monitored to ensure that they stay relevant, accurate and in line with the Council's strategy. • Reserve balances have to be further reviewed to ensure the balances are appropriate. <p>The Council has to address these points in 2018/19.</p> |

Value for Money conclusion

Key Value for Money Risks (continued)

| Risks identified in our audit plan | Findings | Conclusion |
|---|---|--|
| <p>Financial governance and Internal Control</p> <p>During 2015/16, and the early part of 2016/17, financial reporting to full Council was inadequate. In addition we reported in 2015/16 that the general control environment was weak. A weak control environment and inadequate financial reporting leaves the council open to fraud and can also lead to decisions being made using incorrect information.</p> <p>We will review the progress made by the Council in terms of financial governance and improving the control environment. This will closely link with our work on reviewing the inter authority agreement.</p> | <p>Financial reporting was much improved in 2017/18 and has further improved in 2018/19. However, the in year surplus was largely achieved through locking down spend. This is unsustainable and spend should be controlled through cultural change or the control environment.</p> <p>It was however noted, as part of our narrative report review, that there are currently no arrangements in place for monitoring and reporting non-financial information and risk.</p> <p>During 2017/18 monthly control reconciliations were not being routinely completed, although management have asserted that this is now the case in 2018/19. We have not assessed this as our assessment only covers 2017/18.</p> <p>Internal Audit gave limited assurance in relation to budgetary control.</p> | <p>Based on the arrangements in place during 2016/17 we concluded that there were weaknesses in the Councils arrangements for financial reporting and maintaining a sound system of internal control and providing reliable and timely financial reporting that supports the delivery of strategic priorities.</p> <p>This conclusion is underpinned by the S24 recommendations that were made in 2015/16. Key to addressing these recommendations are:</p> <ul style="list-style-type: none"> • The Council have to review capacity across the Council to ensure adequate resource is available to achieve the Council's strategy. • The Council should start to monitor and report against key non financial KPI's as well as key strategic risks. • The Council should continue to perform key monthly control account reconciliations including cash, purchase and sales ledgers. |

Value for Money conclusion

Key Value for Money Risks (continued)

| Risks identified in our audit plan | Findings | Conclusion |
|---|---|--|
| <p>Partnership working</p> <p>The Council have entered into an inter authority agreement with Cornwall Council. This remains a key partnership that underpins leadership, capacity, infrastructure, internal control and financial monitoring and reporting.</p> <p>As part of 'shaping our future' the Council are starting the journey towards integrated strategic commissioning.</p> <p>We will review progress with the inter authority agreement in relation to achieving its primary objectives. We will also review arrangements in place for monitoring performance against the agreement.</p> <p>We will also update our understanding of the arrangements in place for delivering integrated strategic commissioning.</p> | <p>Although the inter authority agreement has had teething issues it appears to be progressing well.</p> <p>Financial reporting and budget monitoring are improving as have capacity and capability within the finance team. Whilst there has been improvement within finance capacity in other service areas remains stretched.</p> <p>With all large collaborations time will be needed to fully embed and resolve emerging issues.</p> <p>It is crucial that the Council monitor progress and performance against the inter authority agreement. During 2017/18 the Council started the process of putting in place these arrangements. These will be monitored by the Sponsorship Board and Steering Group. We will continue to maintain a watching brief in this area.</p> <p>The Council have started the journey towards Strategic Commissioning. Although it is very early days there is evidence that the CIOS have arrangements in place for working with partners in this very important area of policy.</p> | <p>We concluded that arrangements in place are adequate. We will maintain a watching brief in both of these areas.</p> |

A. Reports issued and fees

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

Reports issued

| Report | Date issued |
|-----------------------|---------------|
| Audit Plan | August 2018 |
| Audit Findings Report | December 2018 |
| Annual Audit Letter | March 2019 |

Fees for non-audit services

| Service | Fees £ |
|------------------------------------|--------|
| Audit related services | |
| - Teachers' Pensions certification | 3,200 |

Fees

| | Planned £ | Actual fees £ | 2016/17 fees £ |
|-------------------------------------|---------------|------------------|-------------------|
| Statutory Council audit | 27,128 | TBC | £53,128 |
| Housing Benefit Grant Certification | 4,520 | 4,520 | 4,478 |
| Total fees | 31,648 | TBC | 57,606 |

The planned fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA). The actual fee for 2016/17 of £53,128 includes a fee variation of £26,000 in relation to the additional work required to complete the 2016/17 audit. This is still subject to PSAA approval. There will be an additional charge for the 2017/18 audit due to the additional work required as a result of the change of financial system. This is still to be agreed with management and subsequently PSAA.

Our fees for grant certification cover only housing benefit subsidy certification, which falls under the remit of Public Sector Audit Appointments Limited. Fees in respect of other grant work, such as reasonable assurance reports, are shown under 'Fees for other services'.

Follow up of prior year recommendations

We identified the following issues in the audit of Council's 2016/17 financial statements, which resulted in nine recommendations being reported in our 2016/17 Audit Findings report. We have followed up on the implementation of our recommendations and note three are still to be completed/in-progress:

| Assessment | Issue and risk previously communicated | Update on actions taken to address the issue |
|------------|---|--|
| X | We recommend that the Council reviews its procedures for recognising grant income. All grants should be recognised in line with the accounting policies. Further more all grants should be recorded on a grants register and this should document their subsequent treatment. Supporting documentation setting out conditions should be retained in support of grants received. | The recognition of grant income has been controlled as part of the financial statements production process, however, the system and controls that underpin this process need to be fully re-assessed in order to systematically prevent the potential incorrect recognition of grant income. |
| X | Savings plans (or income generation schemes) should be further developed to ensure the budget shortfall is addressed over the medium term. Schemes should be supported by detailed plans that are deliverable. | This is ongoing and will be addressed as part of the medium term financial plan refresh during 2018/19. |
| ✓ | It is recommended that the Council monitor progress against each individual savings scheme. This ensures transparency of reporting and mitigates the risk of potential unforeseen impact on front line services. | We have noted that during 2018/19 the Council do have quarterly reporting which includes progress against individual savings schemes. |
| ✓ | We recommend that the Council reviews its year end creditors and accruals processes to ensure that all staff are aware of the year end requirements and that income and expenditure is recorded in the correct financial year. The Council should also review its de-minus levels at which an accrual is made. | Our audit has found no issues with accrued income or expenditure. We have however re-iterated the recommendation relating to the need for an accounting policy that sets a de-minimus level; above which accruals are made. |
| ✓ | We recommend that Porthcressa is included in the 2017/18 programme of formal revaluations. | The Council revalued its entire asset base during 2017/18. |

Assessment

- ✓ Action completed
- X Not yet addressed

Follow up of prior year recommendations (cont)

| Assessment | Issue and risk previously communicated | Update on actions taken to address the issue |
|------------|--|--|
| ✓ | The Council should review the processes and controls by which partnerships are assessed, developed and monitored. This will ensure that the purpose of each partnership is clear and achievement against the stated objectives are monitored. | The Council have put in place procedures to monitor the performance of the inter authority agreement. We will revisit this further as part of 2018/19 work. |
| ✓ | We recommend that the cash flow forecasting tool be refined to show all actual and expected transactions. This will improve the transparency of the tool and will also ensure that the Council can accurately forecast its financing requirements. | Cash flow forecasting continues to be undertaken as part of Treasury Management activities. |
| X | We recommend that the Council review its KPI that is included in the narrative report to ensure they they are appropriate and fully reflective of the Councils vision. | The Councils narrative report does not include non-financial performance and risk reporting. We have seen no evidence of monitoring and reporting during the financial year. This has formed part of our VFM conclusion for 2017/18. |
| ✓ | We recommend that access rights to post journals for this member of staff be removed to prevent potential unauthorised postings. | Under the new system access rights have been revisited. |

Assessment

- ✓ Action completed
- X Not yet addressed

Action plan

We identified ten recommendations for the Council as a result of issues identified during the course of our audit. We agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2018/19 audit. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

| Assessment | Issue and risk | Recommendations |
|--------------|---|---|
| ● (Amber) | Alignment of Information Security Policies and Procedures - IT delivery, system and application management is now being co-sourced by Cornwall Council and hence changes have been made in year to the IT arrangements and processes in place at the Council for the Isles of Scilly (COIS). During this period of change it is essential to establish that appropriate security arrangements are in place and that staff are fully aware of any changes in policies they need to abide by. Where policies have not been aligned there is a risk that staff breach organisational, legislative or regulatory requirements by not understanding what their responsibilities are. Also, that staff who do breach security requirements cannot be held accountable through lack of enforceable arrangements to inform them of the responsibilities by Council management. | <p>Management should confirm arrangements to inform staff of IT security requirements at the Council and ensure that all Council for the Isles of Scilly policies are aligned with the security standards in place at Cornwall Council.</p> <p>A mandatory training programme should be considered to ensure all Council staff are aware of their IT security responsibilities, which should be monitored to ensure compliance and be held on an annual basis. Induction processes should include IT security training.</p> <p>All staff should be required to regularly agree to abide by the policies, either on-line or signature.</p> <p>Policies should be reviewed annually and refreshed at least every three years or when significant changes to the IT environment or legislation have occurred and be reissued.</p> <p>Management response</p> <p>Agreed – The Isles of Scilly Council will work with Cornwall Council to ensure that policies and security arrangements are aligned and will investigate using Cornwall Council's approach to deliver the training required.</p> |
| ● (Amber) | IT Risk Management - During any co-sourcing or shared service arrangement, IT risks should still be reviewed by the individual organisations involved and monitored on a regular basis. The failure to identify, monitor and manage risk could give rise to unexpected system disruption arising from a threat that was not properly assessed and mitigated. | <p>The Council for the Isles of Scilly management team should ensure that they identify and monitor any risks to the IT services that could potentially cause any system disruption that would impact their IT systems and hence the business functions they support.</p> <p>Management response</p> <p>Agreed – will form part of a wider risk management review.</p> |
| ● (Amber) | Monitoring Service Levels - To ensure an effective co-sourcing or shared service arrangement, management should monitor defined service levels to ensure that the services provided do meet their organisation's needs and ensure satisfactory system performance. These should be monitored on a regular basis. The failure to monitor service levels could mean that system performance is not reviewed for adequacy and anticipated benefits arising from the co-sourcing or shared service arrangements may not be fully realised. | <p>Management should monitor expected service levels to ensure that the services provided to meet their needs on a regular basis. This could be supported by the examination of system performance data (e.g. via critical audit logs on each system) that could be reviewed on a periodic basis for any anomalies that undermine system performance.</p> <p>Management response</p> <p>Agreed – already identified as a requirement by the Council's Scrutiny Committee and Sponsor Board. Initial work has been commenced in this regard.</p> |

Action plan (cont)

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

| Assessment | Issue and risk | Recommendations |
|--------------|--|---|
| ● (Amber) | The Council does not currently have an accounting policy which sets a de-minimis level under which amounts are not required to accrued. | The Council should consider implementing a de-minimis policy as this will ensure decisions not to accrue expenditure are fully documented. Management response Agreed – we propose a de minimis level of £1,000 for accruals in future. |
| ● (Red) | In previous years we have identified issues with the incorrect recognition of grants. We have made a recommendation in 2016/17 for the Council to review the procedures in this area. The Council have better controlled grants in terms of producing the financial statements, however the underlying processes and controls remain unchanged. There is a risk of grant income being inappropriately recognised. | We recommend that the Council reviews its procedures for recognising grant income. All grants should be recognised in line with the accounting policies. Further more all grants should be recorded on a grants register and this should document their subsequent treatment. Supporting documentation setting out conditions should be retained in support of grants received. Management response Agreed – all specific grants are now recorded on a central register. Grant notifications and supporting documentation are now forwarded to the Finance team. |
| ● (Red) | The Council's current interim medium term financial plan is not fully developed. There is a risk that assumptions are not appropriate and therefore budget gaps are larger than expected. There is also a risk that it is not fully aligned with the Council's strategy. | The Council should develop a robust medium term financial plan that supports the Council's strategy. All assumptions and budget gaps should be fully supported and monitored to ensure that they stay relevant, accurate and in line with the Council's strategy. Management response Agreed – a medium term financial plan will be developed. |
| ● (Red) | General Fund Reserves are currently below the required level of £1m. With the forecast under delivery of savings targets in 2018/19 there is a risk that General Fund Balances could be required to support the financial position. | Reserve balances should be further reviewed to ensure the balances are appropriate. Management response Agreed – reserves will be reviewed as part of the 2019/20 budget setting process. |
| ● (Red) | Capacity and capability within the finance team has improved however capacity in other service areas remains stretched. | The Council should review capacity across the Council to ensure adequate resource is available to achieve the Council's strategy. Management response The Council will review its capacity to deliver the updated corporate strategy to feed in to the report in February. |

Action plan (cont)

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

| Assessment | Issue and risk | Recommendations |
|------------|--|---|
| ● (Red) | The Council does not currently monitor or report for non-financial performance and key strategic risks. | <p>The Council should start to monitor and report against key non financial KPI's as well as key strategic risks.</p> <p>Management response</p> <p>Agreed – initial work has been focussed on introducing financial performance and risk reporting as a priority. As this becomes embedded work will commence on looking at non-financial risk and performance reporting.</p> |
| ● (Red) | During 2017/18 key control account reconciliations were not routinely performed. This heightens the risk of undetected errors or frauds. | <p>The Council should continue to perform key monthly control account reconciliations including cash, purchase and sales ledgers.</p> <p>Management response</p> <p>Agreed – all key reconciliations are now undertaken on the ERP system on a monthly basis since the system went live on March 1st 2018.</p> |



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