



# Audit Completion Report

Durham County Council

Year ending 31 March 2019

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July 2019

Dear Audit Committee Members

### **Audit Completion Report – Year ended 31 March 2019**

We are pleased to present our Audit Completion Report for the year ended 31 March 2019. The purpose of this document is to summarise our audit conclusions.

The scope of our work, including identified significant audit risks and other areas of management judgement, was outlined in our Audit Strategy Memorandum which we presented on 26 February 2019. We have reviewed our Audit Strategy Memorandum and concluded that the original significant audit risks and other areas of management judgement remain appropriate.

We would like to express our thanks for the assistance of your team during our audit.

If you would like to discuss any matters in more detail then please do not hesitate to contact me on 0191 383 6300.

Yours faithfully

Signed:   
Mark Kirkham (Jul 22, 2019)

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# 1. EXECUTIVE SUMMARY

## Purpose of this report and principal conclusions

The Audit Completion Report sets out the findings from our audit of Durham County Council ('the Council') for the year ended 31 March 2019, and forms the basis for discussion at the Audit Committee meeting on 31 July 2019.

The detailed scope of our work as your appointed auditor for 2018/19 is set out in the National Audit Office's (NAO) Code of Audit Practice. Our responsibilities and powers are derived from the Local Audit and Accountability Act 2014 and, as outlined in our Audit Strategy Memorandum, our audit has been conducted in accordance with International Standards of Auditing (UK) and means we focus on audit risks that we have assessed as resulting in a higher risk of material misstatement.

Sections 2 and 5 of this report outline the detailed findings from our work on the financial statements and our conclusion on the Council's arrangements to achieve economy, efficiency and effectiveness in its use of resources. Section 2 also includes our conclusions on the audit risks and areas of management judgement in our Audit Strategy Memorandum, which include:

- management override of control;
- revenue recognition;
- property valuation; and
- defined benefit liability valuation.

## Status of our work

As we outline on the following page, our work is substantially complete. Subject to the satisfactory completion of the outstanding work, at the time of issuing this report we have the following conclusions:

### Opinion on the financial statements

We anticipate issuing an unqualified opinion, without modification, on the financial statements. Our proposed audit opinion is included in the draft auditor's report in Appendix B.

### Value for money conclusion

We anticipate concluding that the Council had proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources. Our draft auditor's report, including proposed conclusion, is provided in Appendix B.

### Whole of Government Accounts (WGA)

We anticipate completing our work on your WGA submission, in line with the group instructions issued by the NAO, by the deadline of 31 August 2019. We anticipate reporting that the WGA submission is consistent with the audited financial statements.

### Wider powers

The 2014 Act requires us to give an elector, or any representative of the elector, the opportunity to question us about the accounting records of the Council and to consider any objection made to the accounts. We have received no objections or questions from local electors.

Executive summary

Significant findings

Internal control recommendations

Summary of misstatements

Value for money conclusion

Appendices

# 1. EXECUTIVE SUMMARY

## Status of our audit work

We have substantially completed our work on the financial statements and Value for Money conclusion for the year ended 31 March 2019. At the time of preparing this report the following matters remain outstanding:

Audit area	Status	Description of outstanding matters
Cash and bank	●	We are awaiting evidence of one school bank balance.
File closure procedures	●	Our standard closure procedures, including review of the final amended accounts.

### Status

- Likely to result in material adjustment or significant change to disclosures within the financial statements
- Potential to result in material adjustment or significant change to disclosures within the financial statements
- Not considered likely to result in material adjustment or change to disclosures within the financial statements

We will provide the Audit Committee with an update in relation to these outstanding matters in a follow-up letter, prior to signing the auditor's report.

## Our audit approach

We provided details of our intended audit approach in our Audit Strategy Memorandum in February 2019. We have not made any changes to our audit approach since we presented our Audit Strategy Memorandum.

## Materiality

We set materiality at the planning stage of the audit at £26.071m using a benchmark of 2% gross expenditure at the surplus or deficit on provision of services level. Our final assessment of materiality, based on the final financial statements and qualitative factors is £26.786m using the same benchmark. We set our trivial threshold (the level under which individual errors are not communicated to the Audit Committee, at £0.804m based on 3% of overall materiality.

## Misstatements and internal control recommendations

Section 3 sets out the internal control recommendations that we make, together with an update on any prior year recommendations.

Section 4 outlines the misstatements noted as part of our audit as at the time of issuing this report. If any additional misstatements are noted on completion of the outstanding work, these will be reported to the Audit Committee in a follow-up letter.

## 2. SIGNIFICANT FINDINGS

Set out below are the significant findings from our audit. These findings include:

- our audit conclusions regarding significant risks and key areas of management judgement outlined in the Audit Strategy Memorandum;
- our comments in respect of the accounting policies and disclosures that you have adopted in the financial statements. On page 9 we have concluded whether the financial statements have been prepared in accordance with the financial reporting framework and commented on any significant accounting policy changes that have been made during the year;
- any further significant matters discussed with management; and
- any significant difficulties we experienced during the audit.

### Significant risks and key areas of management judgement

As part of our planning procedures we considered the risks of material misstatement in the Council's financial statements that required special audit consideration. Although we report identified significant risks at the planning stage of the audit in our Audit Strategy Memorandum, our risk assessment is a continuous process and we regularly consider whether new significant risks have arisen and how we intend to respond to these risks. No new risks have been identified since we issued our Audit Strategy Memorandum.

#### Significant risk

Management override of controls

#### Description of the risk

In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Because of the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.

#### How we addressed this risk

We addressed this risk by carrying out audit work in the following areas:

- accounting estimates impacting on amounts included in the financial statements;
- consideration of any significant transactions outside the normal course of business;
- consideration of the selection and application of accounting policies; and
- journals recorded in the general ledger and other adjustments made in preparation of the financial statements.

#### Audit conclusion

Our work has provided the required assurance.

## 2. SIGNIFICANT FINDINGS (CONTINUED)

### Significant risk

### Description of the risk

Revenue recognition

In accordance with ISA 240 we presume there is a risk of fraud in respect of the recognition of revenue because of the potential for inappropriate recording of transactions in the wrong period. ISA 240 allows the presumption to be rebutted but, given the Council's range of revenue sources, we have concluded that there are insufficient grounds for rebuttal for all income streams in 2018/19. We have identified income from fees and charges as the key areas for audit testing.

This does not imply that we suspect actual or intended manipulation but that we continue to deliver our audit work with appropriate professional scepticism.

### How we addressed this risk

We addressed this risk by performing the following audit work:

- testing no grant revenue items recorded around year end to ensure they had been recognised in the appropriate financial year;
- testing year end receivables;
- testing adjustment journals, including material revenue journals; and
- obtaining direct confirmations of year-end bank balances and testing the reconciliations to the ledger.

### Audit conclusion

Our work has provided the required assurance.

### Significant risk

### Description of the risk

Property, plant and equipment valuations

The financial statements contain material entries on the Balance Sheet as well as material disclosure notes in relation to the Council's holding of property.

Although the Council employs an internal valuation expert to provide information on valuations, there remains a high degree of estimation uncertainty associated with the revaluation of property, plant and equipment (PPE) due to the significant judgements and number of variables involved in providing revaluations. We have therefore identified the revaluation of PPE to be an area of risk.

### How we addressed this risk

- we critically assessed the Council's arrangements for ensuring that PPE valuations are reasonable;
- we critically assessed, the reasonableness of the valuations provided by the Council's valuer using other sources of data;
- we considered the competence, skills and experience of the valuer and the instructions issued to the valuer; and;
- performed further audit procedures on individual assets to ensure the basis of valuations was appropriate.

### Audit conclusion

Our work has provided the required assurance.

## 2. SIGNIFICANT FINDINGS (CONTINUED)

<b>Significant risk</b>	<b>Description of the risk</b>
Defined benefit liability valuation	The financial statements contain material pension entries in respect of the retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. This results in an increased risk of material misstatement.
	<b>How we addressed this risk</b>
	<ul style="list-style-type: none"><li>we critically evaluated the Council's arrangements (including relevant controls) for making estimates in relation to pension entries within the financial statements; and</li><li>we challenged the reasonableness of the actuary's assumptions that underpin the relevant entries made in the financial statements, through the use of an expert commissioned by the National Audit Office.</li></ul>
	<b>Audit conclusion</b>
	Following the changes to the accounts in respect of the McCloud and GMP judgments we have obtained the assurance required.

### Areas of management judgement

<b>Management judgement</b>	<b>Description of the management judgement</b>
Unquoted equity investment valuations	The Council has to make judgements in respect of the fair value measurements of unquoted equity investments it holds, including those in Newcastle Airport and several others.  The underlying accounting requirements are subject to change in 2018/19, which increases the risk in respect of these valuation judgements, therefore they have been assessed as enhanced risks.
	<b>How our audit addressed this area of management judgement</b>
	<ul style="list-style-type: none"><li>we critically assessed the basis of valuation for the Council's unquoted equity investments. This included the valuation of Newcastle airport and Durham County Cricket Club; and</li><li>we assessed whether disclosures are in line with the Code of Practice on Local Authority Accounting (the Code).</li></ul>
	<b>Audit conclusion</b>
	Our review identified several matters which resulted in amendments the classification of some equity investments. These amendments are reflected in note 17, financial instruments. Subject to the amendments to the financial statements we have obtained the assurance sought.

## 2. SIGNIFICANT FINDINGS (CONTINUED)

### Management judgement

Debtors impairment allowance

#### Description of the management judgement

The Council has disclosed its impairment of debtors allowance as an area of estimation uncertainty.

The underlying accounting requirements are subject to change in 2018/19, which increases the risk in respect of the assumptions and uncertainties relevant to this area, therefore they have been assessed as enhanced risks.

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#### How our audit addressed this area of management judgement:

- we critically reviewed the Council's calculation of its impairment of debtors allowance; and
- we assessed whether disclosures were in line with the Code of Audit Practice, including any exemptions relevant to non-contractual debt.

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#### Audit conclusion

Our work has provided the required assurance.

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## 2. SIGNIFICANT FINDINGS (CONTINUED)

### Qualitative aspects of the Council's accounting practices

We have reviewed the Council's accounting policies and disclosures and concluded they comply with the requirements of the Code of Practice on Local Authority Accounting (the Code), appropriately tailored to the Council's circumstances.

Draft accounts were received from the Council on 31 May 2019 and were of a good quality. Working papers were provided in a timely manner and officers have responded to our questions promptly. This is essential in delivering the audit to the July deadline. We would like to thank officers for their support.

### Significant matters discussed with management

#### Pensions

As discussed at the June 2019 Audit Committee, a number of significant issues have arisen this year relating to accounting for pensions. These issues are not specific to the Council, but are national issues impacting on all local government and related bodies. There have been three issues, but the most significant issue is the impact of what is known as the McCloud judgment.

The nature and impact of the McCloud judgment was originally referenced in the draft financial statements as a contingent liability. It relates to claims of discrimination in respect of protections offered to some, but not all, pension scheme members as part of reforms to public sector pensions. In December 2018, the Court of Appeal ruled in a test case that this did amount to unlawful discrimination. At the time the draft financial statements were produced, the Government intended to appeal to the Supreme Court and the outcome was uncertain.

During the audit period, the Government was denied leave to appeal, requiring the estimated impact to be reflected in the pension disclosures in the financial statements, subject to materiality considerations. The Council commissioned the actuary to provide an updated estimate of the pension liability considering the impact of McCloud. Following receipt of the actuary's report, the Council's pension liability has been increased by £41.67m.

The other two issues are:

- Guaranteed Minimum Pension (GMP) indexation and equalisation, which relates to the move to a single-tier new State Pension and equalisation of the GMP benefits between males and females, which has been accounted for to varying degrees by each actuary. Management considered whether the impact of GMP equalisation suggested a material risk to their estimate of the pension liability. The actuary has provided the Council with an updated report showing the impact on the pension liability is not material. Management have, however, decided to amend for the increase in the liability of £7.46m.
- Asset values – the issue is whether the estimation of assets by the actuary using asset values at the end of December 2018 / end of January 2019 was accurate, given higher than expected returns in the final quarter of 2018/19. Management requested further information from the actuary who estimated an increase of £4.01m to the assets value was appropriate. The pension disclosures have been adjusted to reflect this movement.

For each of these issues, our approach was to suggest that engagement with the actuary of each scheme was needed to assess the potential impact of these issues to see whether the impact is material, and, if so, to make amendments to the financial statements.

None of these issues impact on the Council's General Fund balance but both McCloud and GMP will place upward pressure on employers' pension contributions.



## 2. SIGNIFICANT FINDINGS (CONTINUED)

### Significant matters discussed with management (continued)

#### NDR Appeals provision

The NDR appeal provision includes an amount associated with NHS Trust appeals for charitable fund status. We are satisfied, based on review of legal evidence, that the Durham County Council share of the provision is not materially misstated and that the Council has shown prudence in recognising a provision for the appeal.

#### Depreciation of buildings

As part of our testing of building depreciation we recalculated a sample of depreciation charges made in 2018/19. We based our calculation on Gross Book Value brought forward divided by useful asset life assessed by the Council's valuer. For two of the three building assets tested we noted that the Council's calculation was based on Net Book Value. Officers confirmed this was a result of the methodology built into the Council's Fixed Assets System. We estimated the overall potential impact to be £1.3m additional depreciation for the 2018/19 financial year. This, therefore, does not indicate a risk of material misstatement in the estimate. It is noted that whilst depreciation is charged to the cost of services, it is written out under statutory adjustments meaning there is no impact on the Council's General Fund balance.

#### Group Accounts

The Code of Practice on Local Authority Accounting, paragraph 9.1.1.6 states:

'Authorities with interests in subsidiaries, associates and/or joint ventures shall prepare Group Accounts in addition to their single entity financial statements, unless their interest is considered not material.'

The Council has assessed its subsidiaries, associates and joint ventures and considers them to be not material either qualitatively or quantitatively. We have considered management's judgement and are satisfied that the accounts are not materially misstated as a result of this judgement. In the coming years the Council will need to ensure it reviews this assessment and updates it for any significant changes.

#### Earmarked Reserves

The Council is currently showing a negative balance for the 'DSG reserve' (Note 10). This, in our view is not appropriate as a Council can't set aside amounts that are not available. This means a negative earmarked reserve is not appropriate unless derived from a statutory authority. We are not aware of any such authority being granted. The current position may reflect the funding position, i.e., the deficit position will be funded from another source but this is different to the financial reporting position. Management's view is the disclosure reflects the reality of the Council's position and they are not proposing to amend.

### Significant difficulties during the audit

During the course of the audit we did not encounter any significant difficulties and we have had the full co-operation of management.



## 2. SIGNIFICANT FINDINGS (CONTINUED)

### Wider responsibilities

Our powers and responsibilities under the 2014 Act are broad and include the ability to:

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

We have not exercised any of these powers as part of our 2018/19 audit.

The 2014 Act also gives rights to local electors and other parties, such as the right to ask questions of the auditor and the right to make an objection to an item of account. We received no questions or objections from local electors and other parties.



### 3. INTERNAL CONTROL RECOMMENDATIONS

The purpose of our audit is to express an opinion on the financial statements. As part of our audit we have considered the internal controls in place relevant to the preparation of the financial statements. We do this in order to design audit procedures to allow us to express an opinion on the financial statement and not for the purpose of expressing an opinion on the effectiveness of internal control, nor to identify any significant deficiencies in their design or operation.

The matters reported are limited to those deficiencies and other control recommendations that we have identified during our normal audit procedures and that we consider to be of sufficient importance to merit being reported. If we had performed more extensive procedures on internal control we might have identified more deficiencies to be reported or concluded that some of the reported deficiencies need not in fact have been reported. Our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.

Our findings and recommendations are set out below. We have assigned priority rankings to each of them to reflect the importance that we consider each poses to your organisation and, hence, our recommendation in terms of the urgency of required action. In summary, the matters arising fall into the following categories:

Priority ranking	Description	Number of issues
<b>1 (high)</b>	In our view, there is potential for financial loss, damage to reputation or loss of information. This may have implications for the achievement of business strategic objectives. The recommendation should be taken into consideration by management immediately.	0
<b>2 (medium)</b>	In our view, there is a need to strengthen internal control or enhance business efficiency. The recommendations should be actioned in the near future.	0
<b>3 (low)</b>	In our view, internal control should be strengthened in these additional areas when practicable.	1

### 3. INTERNAL CONTROL RECOMMENDATIONS (CONTINUED)

#### Other recommendations on internal control – Level 3

##### Description of deficiency

Our testing of IT general controls noted the following matters:

- There was no specific periodic review of active directory accounts. We were informed by ICT Management that a recent review of old active directory accounts (i.e. older than 12 months) has been undertaken but this was undertaken outside of the audit period (i.e. post 31st March 2019).
- Resource Link (payroll system) password parameters, such as minimum character length, were not in line with the policy requirements.

Compensating control are in place and we neither matter affected our audit approach.

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##### Potential effects

The is inappropriate access to the Council's financial systems.

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##### Recommendation

The Council should ensure policies are complied with.

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##### Management response

ICT are notified of all leavers via an electronic alert from the HR system and immediately deactivate the user account, however on rare occasions, when the user is an agency worker, ICT are not always informed when the user leaves. HR are to remind managers to report agency workers as leavers through the HR system and with immediate effect will run weekly reports out of the Agency Worker system in order that ICT are notified automatically to deactivate these users.

Resourcelink can only be accessed once the user is logged into the council's network and Pulse Secure is required to access systems outside of the council network, using dual authentication and a random token number. Signing in to the Resourcelink system also requires knowledge of the user's personal employee number and the answer to a secondary personalised security question. Going forward ICT are working towards single sign on to access the council's network and are to increase the security of devices when users work outside of the council's network using 'mobile device management' software.

ICT are also reviewing the current password policy.

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##### Follow up of previous internal control points

The only internal control point raised in the prior year was a in relation to IT leaver access deficiency wherein three leavers (from 25 tested) still had access to Council IT systems after their leaving date.

We carried out similar testing for our 2018/19 audit and there were no unexplained cases where employees still had access to IT systems after their leaving date.

## 4. SUMMARY OF MISSTATEMENTS

We set out below the misstatements identified for adjustment during the course of the audit, above the level of trivial threshold of £0.804m.

The first table outlines the misstatements that were identified during the course of our audit which management has assessed as not being material, either individually or in aggregate, to the financial statements and does not currently plan to adjust.

The second table outlines the misstatements that have been adjusted by management during the course of the audit.

### Unadjusted misstatements 2018/19

	Comprehensive Income and Expenditure Statement		Balance Sheet	
	Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
1 Dr: Other long term liabilities - Pensions Cr: Unusable Reserves: Pensions Reserve			5,000	5,000
<p>As reported in our 2017/18 Audit Completion Report the since the last triennial valuation schools have transferred to academy status. In total 12 schools have converted to Academies. When a school converts to an Academy the Council is no longer responsible for the employees and as such the Academy takes on the associated pension liability. The Council has commissioned the actuary to reflect the transfer of the four largest schools in the Council's Pension Liability. However the transfer of the smaller schools has not been reflected meaning the Councils position at the 31 March 2019 includes liabilities associated with academies.</p> <p>The Council and actuary determined that the conversion of these 8 schools would not be material, and have elected to wait till the next triennial valuation to remove these scheme members. The actuary has estimated that the impact of these members remaining in the Councils pension figures means the Pension Liability is overstated by between £3m-£5m which is approximately 0 - 0.4% of the total liability. The figure in the table therefore reflects the higher estimated impact.</p>				
<b>Total unadjusted misstatements</b>			<b>£5,000</b>	<b>£5,000</b>

**Note 1, Accounting policy 21 PPE:** As reported in previous years a de-minimis level for accounting for PPE has not been included in the Accounting Policy disclosures as required by Code (4.1.4.1).

**Note 43, Leases:** Our testing of operating leases noted an error in one leases calculation of future minimum lease payments was overstated by £0.793m. We extrapolated this error across the population tested and estimated the potential error to be an overstatement of future minimum lease payments of £1.32m. This is a disclosure error only as future minimum operating lease payments are not reflected in the Council's balance sheet.

## 4. SUMMARY OF MISSTATEMENTS (CONTINUED)

### Adjusted misstatements 2018/19

	Comprehensive Income and Expenditure Statement		Balance Sheet	
	Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
1				
Dr: CIES: Corporate Costs	49,130			
Dr: Balance Sheet - Pension Reserve			45,120	
Cr: CIES Other Comprehensive I&E		4,010		
Cr: Movement in Reserves		45,120		
Cr: Balance Sheet - Pension Liability				45,120

The Council updated the pension liability to reflect three matters:

1) The nature and impact of the McCloud judgment was recorded in the Council's draft financial statements as a contingent liability. In December 2018, the Court of Appeal ruled in a test case that this did amount to unlawful discrimination. At the time the Council's draft financial statements were prepared, the Government intended to appeal to the Supreme Court and the outcome was uncertain. In late June, however, the Government was denied leave to appeal. As a result local authorities and others affected by the judgment needed to recognise the constructive obligation to account for estimated impact on pension liabilities as at 31 March 2019. The Council's actuary estimated the impact on the pension liability as £41.67m

2) Guaranteed Minimum Pension (GMP) indexation and equalisation, which relate to the move to a single-tier new State Pension and equalisation of the GMP benefits between males and females, was initially accounted for to varying degrees by actuaries. Management considered whether the impact of GMP equalisation suggested a material risk to their estimate of the pension liability. The actuary has provided the Council with an updated report showing the impact on the pension liability is not material. Management, however, amended for the increase of £7.46m.

3) Asset values – this issue relates to the Local Government Pension Scheme (which is funded). The issue is whether the estimation of assets by the actuary using asset values at the end of December 2018 / end of January 2019 was accurate, given higher than expected returns in the final quarter of 2018/19. Management requested further information from the actuary. This resulted in an increase in pension assets of £4.01m

The figures in the table are the net position for these adjustments.

The above also impacted on the cash flow statement and supporting cash flow disclosures.

- 2 The cash flow statement was amended for the pension changes detailed above which impacted on the 2018/19 'non cash movements' (£49.130m). There were also some further adjustments to 'other non cash movements' with amounts reclassified as 'financing activities' (£4.602m). Prior year figures were restated to ensure consistency of classification

The Council also restated some prior year figures. This was to ensure a consistent approach to the classification of 'non cash movements' and 'investing activities'. The largest adjustment was associated with capital grants which instead of being treated as 'non cash movements' have been reclassified as 'investing activities' (£45.324m). This adjustment means classification is in line with the Code requirements. Some further adjustments were made to 'non cash movements' including changes to ensure consistency in recognition of increases and decreases in debtors, creditors and other non-cash items (net impact £1.820m). Overall 'non cash movements' decreased by £43.504m with corresponding increase in 'financing' and 'investing' activities.

## 4. SUMMARY OF MISSTATEMENTS (CONTINUED)

### Adjusted misstatements 2018/19 (Continued)

	Comprehensive Income and Expenditure Statement		Balance Sheet	
	Dr (£'000)	Cr (£'000)	Dr (£'000)	Cr (£'000)
3 Dr: Balance Sheet: Long Term Investments			5,081	
Cr: Balance Sheet - Financial Instrument Adjustment Account				5,081

Following a review of the valuation calculation the Council's investment in Newcastle Airport increased by £5.081m to £10.657m. In the draft accounts a decrease in valuation of £5.081m had been recognised through other comprehensive income and expenditure.

### Disclosure amendments

**Note 4, Assumptions made about the future and other major sources of estimation uncertainty:** Some adjustments were made to this disclosure.

**Note 17 and 18, Financial Instruments;** The notes were amended for several errors. This included amending the classification of assets incorrectly disclosed as 'non financial instrument balances'. The majority of these assets were reclassified as held at 'amortised cost'. The narrative was amended to reflect the new classification under IFRS 9.

**Note 21, Debtors for Local Taxation;** note was removed as the Council deemed it none material given the expanded note 20 (Short Term Debtors).

**Note 24, Short Term Creditors:** The 'Other entities and individuals' line was disaggregated in line with the Code (paragraph 3.4.2.63). Additional lines added were Accumulated Absences (£10.6m), Short term finance lease and PFI liabilities (£5.5m), Collection Fund prepayments (£4.1m) Section 106 agreements (£7.1m), Pension Fund (£7.1m) and Other (£41.8m).

**Note 25, Provisions:** The note narrative was expanded to provide more detail on the nature of the obligations, the expected timing and resulting cash flows (subject to commercial sensitivity), where uncertainty exists and any assumptions applied in estimating the provision.

**Notes 28- 32, Cash Flow Statement:** The draft cash flow disclosure notes were amended for the pension adjustments detailed above plus some other presentational changes. The changes also impacted on several of the prior year figures which were consequently restated to ensure consistency – see previous page.

**Note 38, External Audit Costs:** The note was updated as current year certification of grant claims and returns by the appointed auditor for PSAA is no longer applicable. The audit fee was also adjusted to ensure it was consistent with the fee set by PSAA.

**Note 41, Related parties:** Some amendments to the disclosure were made.

**Note 42 Capital financing and expenditure:** Note was updated to reflect prior year the assets being acquired under finance leases rather than the increase in underlying need to borrow.

The Statement of Accounts was also adjusted for minor spelling, grammatical and consistency errors.

## 5. VALUE FOR MONEY CONCLUSION

### Our audit approach

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

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

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

Commentary against each of the sub-criteria, and an indication of whether arrangements are in place, is provided below.

Sub-criteria	Commentary	Arrangements in place?
Informed decision making	<p>A Council Constitution is in place which is reviewed, as a minimum, annually. This sets out the governance structure of the Council which has remained unchanged in 2018/19. The Audit Committee met regularly during the year. The Audit Committee monitors the Council's system of internal control and, where it deems necessary, challenges officers where weaknesses are identified. The Internal Audit plan has been delivered for the year and Internal Audit report directly to the Audit Committee. Internal Audit recommendations are closely monitored to ensure they are implemented and this is in a timely manner. An Annual Governance Statement has been prepared and approved by the Audit Committee.</p> <p>A Corporate Risk Management Group is in place highlighting the strategic risks facing the Council. Performance and financial reporting is embedded in the Council and there has been regular reporting to the Cabinet using a consistent methodology which allows any over or under delivery to be identified. The year end financial position reported to Cabinet in July 2019 was not significantly different to the position forecast during the year. Financial reporting provides detailed analysis of under and over spends of income and expenditure, for example, the 2018/19 reports have highlighted at an early stage the pressures in Children and Young People's Services. Performance reports include staff indicators, such as sickness levels.</p> <p>A Medium Term Financial Plan (MTFP) (8) was in place for the year ended 31 March 2019. Performance against the plan was reported regularly to the Cabinet. MTFP (9) covering the period 2019/20 – 2022/23 was approved by the Council in February 2019. This set a balanced budget for the 2019/20 financial year, including fully identified savings of £10m. Cabinet have received regular updates on the Council's arrangements to address school deficit budgets for 2019/20.</p>	Yes

## 5. VALUE FOR MONEY CONCLUSION

Sub-criteria	Commentary	Arrangements in place?
Sustainable resource deployment	<p>MTFP (9) was approved by full Council in February 2019. The plan sets out the pressures faced by the Council in the coming year including demand and funding pressures. The Net Budget Requirement for 2019/20 is £400.031. This requires savings of £15.8m of which £5.5m will be covered by use of the Budget Support Reserve (Balance at 31 March 2019 is £30m) and £10m by savings. The savings have been fully identified and are detailed in appendix 3 of the MTFP. Over the life of the MTFP (9) the Council estimates savings of £39.5m will be necessary to ensure a balanced budget (£23.24m for the period 20/21-22/23). The Council has a good record of delivering savings since 2011/12. It recognises that delivery of savings in coming years will be more challenging. The Budget Support Reserve is intended to support the budget in later years and is forecast to have a balance of £24.2m at 31 March 2020.</p> <p>The 2018/19 outturn shows that overall the Council delivered a surplus against the set budget. The outturn report reflects the pressures faced by the Council in particular children's social services and high needs DSG. Additional General Fund support has been reflected in the 2019/20 budget. The MTFP recognises that this is not sustainable and the council is working locally and nationally to mitigate the pressures and secure additional central government funding. Other pressures include maintained schools budgets. Several schools have set deficit budgets for 2019/20. Others have set budgets which include the use of reserves to balance the 19/20 budget. Consequently school reserves are forecast to decrease by £10.231m to £7.459m at 31 March 2020. Where appropriate the Corporate Director for Resources is working with individual schools and monitoring the overall position of schools budgets. The position has been reported to Cabinet.</p> <p>Earmarked reserves increased by £1.98m and the General Fund increased by £0.6m. The means overall useable reserves as at 31 March 2019 are £251.53m. Although as noted above some individual reserves, such as Dedicated Schools Grant Reserve, have been utilised more than planned. The MTFP (9) is based on the General Fund reserve being maintained within the Council's approved range of 5-7.5% of Net Budget Requirement.</p> <p>Overall capital expenditure was lower than planned in the year by £12.561m which is 12% of total budget. The underspend has been carried into the 2019/20 budget. MTFP (9) includes a financed capital programme. Future investments such as the Milburngate development have been approved by the Cabinet.</p> <p>As detailed in the Annual Governance Statement an EU Exit Working Task &amp; Finish Group has been established. This is chaired by the Director of Transformation and Partnerships with representatives from all service groupings, reporting to Corporate Management Team. The group, Chaired by the Director of Transformation and Partnerships, monitored the emerging impact to identify and minimise the risks on council services and service users.</p>	Yes

# 5. VALUE FOR MONEY CONCLUSION

Sub-criteria	Commentary	Arrangements in place?
Working with partners and other third parties	<p>The Council's Constitution details the arrangements for contracting with third parties. The Council has written procedures for procuring products and services, which are within its constitution.</p> <p>Significant partnerships such as the Better Care Fund are balanced with no one party able to disproportionately direct the culture and outcomes of the partnership. The Health and Well-being Board is responsible for the Durham Better Care Fund plan. Financial and health outcome performance of the plan is monitored.</p> <p>Where appropriate partnerships are monitored through Council performance reporting arrangements. Area Action Partnerships are intended to give local residents a voice in how services are provided locally. Consultation with partners feeds into the Council's MTFP development.</p> <p>The County Durham Partnership is in place bringing together key partners in the County. This is leading the development of the County Durham Vision for where the Council aims to be by 2035.</p>	Yes



## 5. VALUE FOR MONEY CONCLUSION (CONTINUED)

### Significant audit risks

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

Risk	Work undertaken	Conclusion
<p><b>Sustainable resource deployment</b></p> <p>The Council has a good track record of delivering to budget. Reduced funding means the Council continues to require significant levels of savings in the coming years. The medium term financial plan (MTFP) is in place to meet these pressures. To ensure our conclusion is correct we need to update our understanding of the Council's MTFP arrangements and how it monitors the planned delivery of savings.</p>	<ul style="list-style-type: none"> <li>We reviewed the Council's arrangements for developing the MTFP (9).</li> <li>We considered the delivery of 2018/19 savings against plans, including testing the outcome of a small sample of schemes.</li> <li>We reviewed the arrangements for future savings, including reviewing the robustness of identified plans for 2019/20 and beyond. This includes testing a sample of 2019/20 schemes.</li> <li>We reviewed the arrangements for the Transformation Programme.</li> </ul>	<p>Our work provided sufficient assurance. We have no matters to report.</p>

### Our overall value for money conclusion

Our draft auditor's report included in Appendix B states that we intend to issue an unqualified conclusion for the 2018/19 financial year.



# APPENDIX A

## DRAFT MANAGEMENT REPRESENTATION LETTER

Durham County Council  
County Hall  
Durham  
DH1 5UZ

July 2019

Dear Mark

### **Durham County Council - audit for year ended 31 March 2019**

This representation letter is provided in connection with your audit of the financial statements of Durham County Council (the Council) for the year ended 31 March 2019 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 (the Code) and applicable law.

I confirm that the following representations are made on the basis of enquiries of management and staff with relevant knowledge and experience (and, where appropriate, inspection of supporting documentation) sufficient to satisfy ourselves that I can properly make each of the following representations to you.

#### **My responsibility for the financial statements and accounting information**

I believe that I have fulfilled my responsibilities for the true and fair presentation and preparation of the financial statements in accordance with the Code and applicable law.

#### **My responsibility to provide and disclose relevant information**

I have provided you with:

- access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other material;
- additional information that you have requested from us for the purpose of the audit; and
- unrestricted access to individuals within the Council you determined it was necessary to contact in order to obtain audit evidence.

I confirm as Corporate Director of Resources that I have taken all the necessary steps to make me aware of any relevant audit information and to establish that you, as auditors, are aware of this information.

As far as I am aware there is no relevant audit information of which you, as auditors, are unaware.

#### **Accounting records**

I confirm that all transactions that have a material effect on the financial statements have been recorded in the accounting records and are reflected in the financial statements. All other records and related information, including minutes of all Council and committee meetings, have been made available to you.

#### **Accounting policies**

I confirm that I have reviewed the accounting policies applied during the year in accordance with Code and International Accounting Standard 8 and consider these policies to faithfully represent the effects of transactions, other events or conditions on the Council's financial position, financial performance and cash flows.

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# APPENDIX A

## DRAFT MANAGEMENT REPRESENTATION LETTER (CONTINUED)

### Accounting estimates, including those measured at fair value

I confirm that any significant assumptions used by the Council in making accounting estimates, including those measured at current or fair value, are reasonable.

### Contingencies

There are no material contingent losses including pending or potential litigation that should be accrued where: information presently available indicates that it is probable that an asset has been impaired or a liability had been incurred at the balance sheet date; and the amount of the loss can be reasonably estimated.

There are no material contingent losses that should be disclosed where, although either or both the conditions specified above are not met, there is a reasonable possibility that a loss, or a loss greater than that accrued, may have been incurred at the balance sheet date.

- There are no contingent gains which should be disclosed.
- All material matters, including unasserted claims, that may result in litigation against the Council have been brought to your attention. All known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to you and accounted for and disclosed in accordance with the Code and applicable law.

### Laws and regulations

I confirm that I have disclosed to you all those events of which I am aware which involve known or suspected non-compliance with laws and regulations, together with the actual or contingent consequences which may arise therefrom.

The Council has complied with all aspects of contractual agreements that would have a material effect on the accounts in the event of non-compliance.

### Fraud and error

I acknowledge my responsibility as Corporate Director of Resources for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

I have disclosed to you:

- all the results of my assessment of the risk that the financial statements may be materially misstated as a result of fraud;
- all knowledge of fraud or suspected fraud affecting the Council involving:
  - management and those charged with governance;
  - employees who have significant roles in internal control; and
  - others where fraud could have a material effect on the financial statements.

I have disclosed to you all information in relation to any allegations of fraud, or suspected fraud, affecting the Council's financial statements communicated by employees, former employees, analysts, regulators or others.

### Related party transactions

I confirm that all related party relationships, transactions and balances, have been appropriately accounted for and disclosed in accordance with the requirements of the Code and applicable law.

I have disclosed to you the identity of the Council's related parties and all related party relationships and transactions of which I am aware.

### Impairment review

To the best of my knowledge, there is nothing to indicate that there is a permanent reduction in the recoverable amount of the property, plant and equipment below their carrying value at the balance sheet date. An impairment review is therefore not considered necessary.

# APPENDIX A

## DRAFT MANAGEMENT REPRESENTATION LETTER

### (CONTINUED)

#### Future commitments

I am not aware of any plans, intentions or commitments that may materially affect the carrying value or classification of assets and liabilities or give rise to additional liabilities.

#### Service Concession Arrangements

I am not aware of any material contract variations, payment deductions or additional service charges in 2018/19 in relation to the Council's PFI schemes that you have not been made aware of.

#### Subsequent events

I confirm all events subsequent to the date of the financial statements and for which the Code and applicable law, require adjustment or disclosure have been adjusted or disclosed.

Should further material events occur after the date of this letter which may necessitate revision of the figures included in the financial statements or inclusion of a note thereto, I will advise you accordingly.

#### Going concern

To the best of my knowledge there is nothing to indicate that the Council will not continue as a going concern in the foreseeable future. The period to which I have paid particular attention in assessing the appropriateness of the going concern basis is not less than twelve months from the date of approval of the accounts.

#### Unadjusted misstatements

I confirm that the effects of the uncorrected misstatements are immaterial, both individually and in aggregate, to the financial statements as a whole. *Please make sure the appendix is attached to the letter and not cross-referenced to the appendix in the ACR.*

Yours faithfully

Corporate Director of Resources: .....

Date: .....

# APPENDIX B

## DRAFT AUDITOR'S REPORT

### Opinion on the financial statements of Durham County Council

We have audited the financial statements of Durham County Council ('the Council') for the year ended 31 March 2019, which comprise the Comprehensive Income and Expenditure Statement, the Movement in Reserves Statement, the Balance Sheet, the Cash Flow Statement, and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

In our opinion, the financial statements:

- give a true and fair view of the financial position of Durham County Council as at 31<sup>st</sup> March 2019 and of its expenditure and income for the year then ended; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

### Opinion on the financial statements of Durham County Council Pension Fund

We have audited the financial statements of Durham County Council Pension Fund ('the Pension Fund') for the year ended 31 March 2019, which comprise the Fund Account, the Net Assets Statement, and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

In our opinion the financial statements:

- give a true and fair view of the financial transactions of Durham County Council Pension Fund during the year ended 31 March 2019, and the amount and disposition of the Pension Fund's assets and liabilities as at 31 March 2019; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

### Basis for opinions

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities section of our report. We are independent of the Council and the Pension Fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applicable to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinions.

### Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the Corporate Director of Resources use of the going concern basis of accounting in the preparation of the Council's and the Pension Fund's financial statements is not appropriate; or
- the Corporate Director of Resources has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Council's or the Pension Fund's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

### Other information

The Corporate Director of Resources is responsible for the other information. The other information comprises the Annual Governance Statement and information included in the Statement of Accounts, other than the financial statements and our auditor's report thereon. Our opinions on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

# APPENDIX B

## DRAFT AUDITOR'S REPORT (CONTINUED)

### Responsibilities of the Corporate Director of Resources for the financial statements

As explained more fully in the statement of the Corporate Director of Resources' Responsibilities, the Corporate Director of Resources is responsible for the preparation of the Statement of Accounts, which includes the Council's and Pension Fund's financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19, and for being satisfied that they give a true and fair view. The Corporate Director of Resources is also responsible for such internal control as the Corporate Director of Resources determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Corporate Director of Resources is required to comply with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 and prepare the financial statements on a going concern basis, unless the Council is informed of the intention for dissolution without transfer of services or function to another entity. The Corporate Director of Resources is responsible for assessing each year whether or not it is appropriate for the Council and the Pension Fund to prepare the accounts on the going concern basis and disclosing, as applicable, matters related to going concern.

### Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the Council's and Pension Fund's financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities). This description forms part of our auditor's report.

### Matters on which we are required to report by exception under the Code of Audit Practice

We are required by the Code of Audit Practice to report to you if:

- we issue a report in the public interest under section 24 of the Local Audit and Accountability Act 2014;
- we make a recommendation under section 24 of the Local Audit and Accountability Act 2014; or
- we exercise any other special powers of the auditor under sections 28, 29 or 31 of the Local Audit and Accountability Act 2014.

We have nothing to report in these respects.

### Conclusion on Durham County Council's arrangements for securing economy, efficiency and effectiveness in the use of resources

#### Conclusion

On the basis of our work, having regard to the guidance on the specified criterion issued by the Comptroller and Auditor General in November 2017, we are satisfied that, in all significant respects, Durham County Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

#### Basis for conclusion

We have undertaken our review in accordance with the Code of Audit Practice issued by the Comptroller and Auditor General, having regard to the guidance on the specified criterion issued in November 2017, as to whether the Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. The Comptroller and Auditor General determined this criterion as that necessary for us to consider in satisfying ourselves whether the Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

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

#### Responsibilities of the Council

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

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# APPENDIX B

## DRAFT AUDITOR'S REPORT (CONTINUED)

### Auditor's responsibilities for the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

We are required under section 20(1)(c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice requires us to report to you our conclusion relating to proper arrangements. We are not required to consider, nor have we considered, whether all aspects of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

### Use of the audit report

This report is made solely to the members of Durham County Council, as a body, in accordance with part 5 of the Local Audit and Accountability Act 2014 and as set out in paragraph 44 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our audit work has been undertaken so that we might state to the members of the Council those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the members of the Council, as a body, for our audit work, for this report, or for the opinions we have formed.

### Certificate

We certify that we have completed the audit of Durham County Council in accordance with the requirements of the Local Audit and Accountability Act 2014 and the Code of Audit Practice.

[Signature]

Mark Kirkham  
For and on behalf of Mazars LLP  
Salvus House  
Aykley Heads  
Durham  
DH1 5TS  
31 July 2019

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# APPENDIX C INDEPENDENCE

As part of our ongoing risk assessment we monitor our relationships with you to identify any new actual or perceived threats to our independence within the regulatory or professional requirements governing us as your auditors.

We can confirm that no new threats to independence have been identified since issuing the Audit Strategy Memorandum and therefore we remain independent.



## CONTACT

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