



# **Peterborough City Council Audit Planning Report**

**Year ended 31 March 2019**

**30 January 2019**



Audit Committee  
Peterborough City Council

30 January 2019

Dear Committee Members

### 2018/19 Audit Plan

We are pleased to attach the Final Audit Plan for the 2018/19 audit following completion of our risk assessment procedures. The main changes to the Outline Audit Plan we presented to the 19 November 2018 meeting are in relation to the risks we have identified. We include a summary of these changes on the next page and provide more detailed explanations in Sections 01 and 02.

The Plan sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the Audit Committee with a basis to review our proposed audit approach and scope for the 2018/19 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This plan summarises our assessment of the key risks driving the development of an effective audit for the Council, and outlines our planned audit strategy in response to those risks.

This report is intended solely for the information and use of the Audit Committee and management, and is not intended to be and should not be used by anyone other than these specified parties.

We welcome the opportunity to discuss this report with you on 11 February 2019 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Suresh Patel

For and on behalf of Ernst & Young LLP

## Summary of changes to the risks identified for 2018/19

	<b>Risk / area of focus</b>	<b>Outline Plan</b>	<b>Final Plan</b>	<b>Reason for change</b>
1	Risk of fraud in revenue and expenditure recognition	Fraud risk	Not included	We have rebutted the risk
2	Misstatements due to fraud or error - management override	Fraud risk	Fraud risk	n/a
3	Valuation and impairment of Property, Plant and Equipment (PPE) and Investment Property (IP)	Inherent risk	Inherent risk	n/a
4	Pension liability and assets	Inherent risk	Inherent risk	n/a
5	Assessment of Group Boundary	Other risk	Not included	No significant developments impacting the group boundary
6	PFI Accounting	Inherent risk	Significant risk	We have not reviewed in detail the Schools PFI accounting since 2015/16
7	New accounting standards	Other risk	Other risk	n/a
8	Misstatements due to fraud or error - the incorrect capitalisation of revenue expenditure and REFCUS	Not included	Fraud risk	Focused consideration of management override of controls
9	Misstatements due to fraud or error - incorrect application of capital grants	Not included	Fraud risk	
10	Valuation of property, plant and equipment assets under depreciated replacement cost model	Linked to item 3	Significant risk	Specific risk in relation to specialist assets

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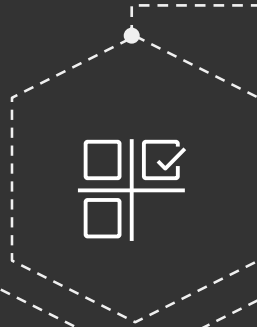
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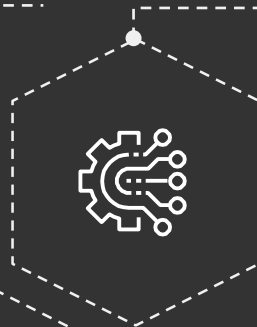
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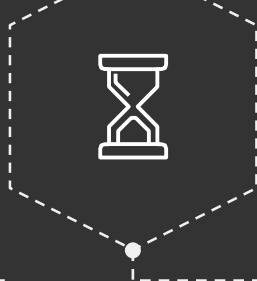
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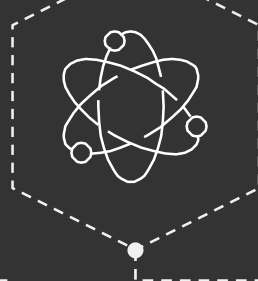
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In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued "Statement of responsibilities of auditors and audited bodies". It is available from the via the PSAA website ([www.PSAA.co.uk](http://www.PSAA.co.uk)). The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas. The "Terms of Appointment (updated February 2017)" issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature. This report is made solely to the Audit Committee and management of Peterborough City Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee, and management of Peterborough City Council those matters we are required to state to them in this 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 Audit Committee and management of Peterborough City Council for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.



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01

# Overview of our 2018/19 audit strategy



## Overview of our 2018/19 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

### Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively.
Misstatements due to fraud or error - the incorrect capitalisation of revenue expenditure and REFCUS	Fraud risk	New area of focus	<p>The Council is under financial pressure to achieve budget and maintain reserve balances above the minimum approved levels. Manipulating expenditure is a key way to achieve these targets and one way management override (as outlined above) can manifest.</p> <p>We consider the risk applies to capitalisation of revenue expenditure and revenue expenditure funded from capital under statute (REFCUS). Management could manipulate revenue expenditure by incorrectly capitalising expenditure which is revenue in nature and should be charge to the comprehensive income and expenditure account.</p>
Misstatements due to fraud or error - incorrect application of capital grants	Fraud risk	New area of focus	<p>The Council is under financial pressure to achieve its revenue budget and maintain reserve balances above the minimum approved levels. Manipulating expenditure is a key way of achieving these targets and another way management override (as outlined above) can manifest.</p> <p>The adjustments between accounting basis and funding basis under regulation changes the amounts charged to General Fund balances. Regulations are varied and complex, resulting in a risk that management misstatement accounting adjustments to manipulate the General Fund balance. We have identified the risk to be highest for adjustments concerning the application of capital grants.</p>
PFI Accounting	Significant risk	Change in focus	The Council has a material PFI arrangement. The complexity of PFI accounting represents an inherent risk. We last reviewed in depth the Council's arrangements in 2016 and will need to draw on our PFI experts to carry out a review including any changes made by the Council.

## Overview of our 2018/19 audit strategy

### Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Valuation of property, plant and equipment assets under depreciated replacement cost model	Significant risk	New area of focus	<p>Property, plant and equipment (PPE) represents a significant balance in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges.</p> <p>Material judgemental inputs and estimation techniques are required to calculate the year-end PPE balances held in the balance sheet. For assets valued using depreciated replacement cost (DRC) this risk is heightened due to the specialised nature of the assets and insufficient availability of market-based evidence to assist the valuation.</p> <p>As the Council's DRC asset base is significant, and the outputs from the valuer are subject to estimation, there is a significant risk PPE may be under/overstated or the associated accounting entries incorrectly posted. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of experts and assumptions underlying fair value estimates.</p>
Valuation of other Land and Buildings and Investment Properties	Inherent risk	No change in risk or focus	<p>The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges.</p> <p>Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.</p>
Pension Liability Valuation & Pensions Assets	Inherent risk	No change in risk or focus	<p>The Council makes extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Cambridgeshire County Council. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2018 this totalled £271 million. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf.</p>
New accounting standards	Other risk	New area of focus	<p>For 2018/19 the Council needs to consider the new accounting standards relating to financial instruments (IFRS 9) and revenue from contracts (IFRS 15). The Council needs to assess and evaluate the implications of these new standards on the 2018/19 accounts.</p>

# Overview of our 2018/19 audit strategy

## Materiality

Planning  
materiality  
**£10.0m**

In light of changes across the audit profession we have reduced the top of our range for materiality from 2% to 1.8% of the forecast gross expenditure (based on the PY outturn) of the Council. Our planning materiality has decreased from £10.5 million in the prior year.

Performance  
materiality  
**£7.5m**

We have set performance materiality at £7.5 million, which represents 75% of materiality and is the top of our range.

Audit  
differences  
**£500k**

We will report all uncorrected misstatements relating to the primary statements (comprehensive income and expenditure statement, balance sheet, movement in reserves statement and cash flow statement) greater than £0.5 million. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

We also identify areas where misstatement at a lower level than our overall materiality level might influence the reader and develop an audit strategy specific to these areas, including:

- ▶ Remuneration disclosures including councillor allowances: we will agree all disclosures back to source data, and councillor allowances to the agreed and approved amounts.
- ▶ Related party transactions we will test the completeness of related party disclosures and the accuracy of all disclosures by checking back to supporting evidence.



# Overview of our 2018/19 audit strategy

## Audit scope

This Audit Plan covers the work that we plan to perform to provide you with:

- Our audit opinion on whether the financial statements of Peterborough City Council give a true and fair view of the financial position as at 31 March 2019 and of the income and expenditure for the year then ended; and
- Our conclusion on the Council's arrangements to secure economy, efficiency and effectiveness.

We will also review and report to the National Audit Office (NAO), to the extent and in the form required by them, on the Council's Whole of Government Accounts return.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

- Strategic, operational and financial risks relevant to the financial statements;
- Developments in financial reporting and auditing standards;
- The quality of systems and processes;
- Changes in the business and regulatory environment; and,
- Management's views on all of the above.

By considering these inputs, our audit is focused on the areas that matter and our feedback is more likely to be relevant to the Council.

## Audit team

We have made two changes to your audit team, bringing in Dan Cooke as Audit Manager and Bach Pham as lead executive. Both Dan and Bach have good experience and knowledge of local government in the East of England. Suresh Patel will continue to be your Engagement Lead.



# 02 Audit risks



## Our response to significant risks

We have set out the significant risks (including fraud risks denoted by\*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

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### Misstatements due to fraud or error \*

#### What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

As part of our work to identify fraud risks during the planning stages, we have identified those areas of the accounts that involve management estimates and judgements as the key areas at risk of manipulation.

These are set out on the following pages.

#### What will we do?

- ▶ Identifying fraud risks during the planning stages.
- ▶ Inquiry of management about risks of fraud and the controls put in place to address those risks.
- ▶ Understanding the oversight given by those charged with governance of management's processes over fraud.
- ▶ Consideration of the effectiveness of management's controls designed to address the risk of fraud.
- ▶ Determining an appropriate strategy to address those identified risks of fraud.
- ▶ Performing mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments in the preparation of the financial statements.

To address the residual risk of management override we perform specific procedures which include:

- ▶ Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements, for example using our journal tool to focus our testing on specific journals such as those created at unusual times or by staff members not usually involved in journal processing;
- ▶ Assessing key accounting estimates for evidence of management bias; and
- ▶ Evaluating the business rationale for significant unusual transactions

## Our response to significant risks (continued)

**Misstatements due to fraud or error - the incorrect capitalisation of revenue expenditure and REFCUS \***

**Financial statement impact**

We have identified a risk of expenditure misstatements due to fraud or error that could affect the income and expenditure accounts.

We consider the risk applies to capitalisation of revenue expenditure and REFCUS and could result in a misstatement of cost of services reported in the comprehensive income and expenditure statement.

**What is the risk?**

The Council is under financial pressure to achieve budget and maintain reserve balances above the minimum approved levels. Manipulating expenditure is a key way to achieve these targets.

We consider the risk applies to capitalisation of revenue expenditure and revenue expenditure funded from capital under statute (REFCUS). Management could manipulate revenue expenditure by incorrectly capitalising expenditure which is revenue in nature and should be charge to the comprehensive income and expenditure account.

In 2017/18 the Council incurred £80.3 million capital expenditure (of which REFCUS represented £23.4 million).

**What will we do?**

**Our approach will focus on:**

- Sample testing additions to property, plant and equipment to ensure that they have been correctly classified as capital and included at the correct value in order to identify any revenue items that have been inappropriately capitalised;
- Sample testing REFCUS transactions to ensure they have been correctly classified and the expenditure meets the definition of allowable expenditure, or is incurred under direction from the secretary of state; and
- Using our data analytics tool to identify and test journal entries that move expenditure into capital codes.

## Our response to significant risks (continued)

**Misstatements due to fraud or error - incorrect application of capital grants \***

### What is the risk?

The Council is under financial pressure to achieve its revenue budget and maintain reserve balances above the minimum approved levels. Manipulating expenditure is a key way of achieving these targets.

We consider the risk applies to the application of capital grants in the financial statements.

The adjustments between accounting basis and funding basis under regulation changes the amounts charged to General Fund balances. Regulations are varied and complex, resulting in a risk that management misstatement accounting adjustments to manipulate the General Fund balance. We have identified the risk to be highest for adjustments concerning the application of capital grants.

In 2017/18 the Council applied £36.5 million of capital grants and contributions.

### What will we do?

**Our approach will focus on:**

- Sample testing the application of capital grants to ensure they meet the definition of capital expenditure;
- Sample testing capital grants received in advance to ensure any conditions have been correctly applied; and
- Using our data analytics tool to identify and test journal entries adjustments that impact capital grant accounts.

### Financial statement impact

We have identified a specific risk of misstatements due to fraud or error that could affect the income and expenditure accounts and the balance sheet.

We consider the risk applies to the application of capital grants in the comprehensive income and expenditure statement (CIES) and balance sheet.

## Our response to significant risks (continued)

**Valuation of property, plant and equipment assets under depreciated replacement cost model**

**Financial statement impact**

We have identified a specific risk of misstatements due to fraud or error that could affect the balance sheet.

We consider the risk applies to the valuation of property, plant and equipment using the depreciated replacement cost method in the balance sheet.

**What is the risk?**

Property, plant and equipment (PPE) represents a significant balance in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges.

Material judgemental inputs and estimation techniques are required to calculate the year-end PPE balances held in the balance sheet. For assets valued using depreciated replacement cost (DRC) this risk is heightened due to the specialised nature of the assets and insufficient availability of market-based evidence to assist the valuation.

As the Council's DRC asset base is significant (£319 million), and the outputs from the valuer are subject to estimation, there is a significant risk PPE may be under/overstated or the associated accounting entries incorrectly posted.

ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of experts and assumptions underlying fair value estimates.

**What will we do?**

**Our approach will focus on:**

- ▶ Consider the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work;
- ▶ Sample test key asset information used by the valuers in performing their DRC valuations (e.g. floor plans to support valuations based on price per square metre and the specialised nature of the assets);
- ▶ Consider the use of EY valuation specialists to review a sample of the underlying assumptions used to value any material specialist DRC assets;
- ▶ Review DRC assets not subject to valuation in 2018/19 to confirm that the remaining asset base is not materially misstated;
- ▶ Consider changes to useful economic lives as a result of the most recent valuation; and
- ▶ Test accounting entries have been correctly processed in the financial statements.

## Our response to significant risks (continued)

### PFI accounting

#### What is the risk?

The Council has a material PFI arrangement for three secondary schools in Peterborough. PFI accounting is a complex area. We undertook a detailed review of the arrangements in 2015/16 and concluded that the accounting disclosures were materially correct. Given the complexities involved we have identified a need to undertake a technical review of the accounting arrangements by an EY PFI specialist to ensure the arrangements are still operating effectively.

#### What will we do?

##### Our approach will focus on:

- ▶ Making enquiries to management in respect of changes to arrangements and the calculation of annual payments and the on going liability; and
- ▶ Using our PFI specialists to review the operating and accounting models for the schemes to ensure these are operating effectively and consistent with the disclosures in the financial statements.

#### Financial statement impact

We have identified a specific risk of misstatements due to fraud or error that could affect the balance sheet.

We consider the risk applies to the valuation of PFI liabilities in the balance sheet.

In 2017/18 the Council reported future PFI repayments totalling £179.4 million in the financial statements.

## Audit risks

### Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures.

#### What is the risk/area of focus?

##### **Valuation of other Land and Buildings and Investment Properties**

The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges.

Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.

#### What will we do?

We will:

- ▶ Consider the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work;
- ▶ Sample test key asset information used by the valuers in performing their valuation (e.g. floor plans to support valuations based on price per square metre);
- ▶ Consider the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code for PPE and annually for IP. We have also considered if there are any specific changes to assets that have occurred and that these have been communicated to the valuer;
- ▶ Review assets not subject to valuation in 2018/19 to confirm that the remaining asset base is not materially misstated;
- ▶ Consider changes to useful economic lives as a result of the most recent valuation; and
- ▶ Test accounting entries have been correctly processed in the financial statements.



## Audit risks

### Other areas of audit focus (continued)

#### What is the risk/area of focus?

##### **Pension Liability Valuation & Pensions Assets**

The Council makes extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Cambridgeshire County Council.

The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2018 this totalled £271 million.

The information disclosed is based on the IAS 19 report issued to the Council by the actuary to the County Council.

Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf.

We undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

#### What will we do?

We will:

- ▶ Liaise with the auditors of Cambridgeshire Pension Fund, to obtain assurances over the information supplied to the actuary in relation to Peterborough City Council;
- ▶ Assess the work of the Pension Fund actuary (Hymans Robertson) including the assumptions they have used, by relying on the work of PWC - Consulting Actuaries commissioned by the National Audit Office for all local government sector auditors, and by considering any relevant reviews by the EY actuarial team; and
- ▶ Review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS19 considering fund assets and the Council's liability.

#### What is the risk/area of focus?

##### **New accounting standards**

The Code requires the Council to comply with the requirements of two new accounting standards for 2018/19 and make preparations for another new standard for 2020/21. These standards are:

- ▶ IFRS 9 - Financial instruments
- ▶ IFRS 15 - Revenue from contracts
- ▶ IFRS 16 - Leases

There is an inherent risk in relation to implementing new accounting standards and carrying out a sufficient assessment and evaluation.

#### What will we do?

We will:

- ▶ Engage early with the Council on their assessment and evaluation of the impact of each new accounting standard. We will also provide an early view on the Council's proposed accounting and disclosures; and
- ▶ If required, undertake additional audit procedures on the Council's assessments we will discuss with the Chief Financial Officer the impact on our audit fee.



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03

## Value for Money Risks





## Background

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion. For 2018/19 this is based on the overall evaluation criterion:

"In all significant respects, the audited body 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 NAO defines proper arrangements as your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.

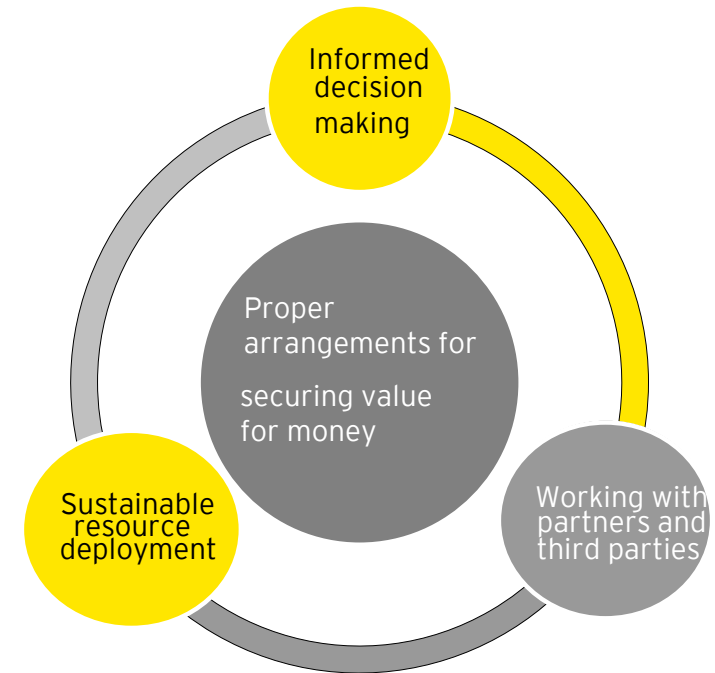
The NAO's auditor guidance includes specific reference to combined authorities, recognising their commissioning role and focus on partnership working.

In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

We are only required to determine whether there are any risks that we consider significant, which the Code of Audit Practice defines as:

"A matter is significant if, in the auditor's professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public".

Our risk assessment supports the planning of sufficient work to enable us to deliver a safe conclusion on arrangements to secure value for money and enables us to determine the nature and extent of further work that may be required. If we do not identify any significant risks there is no requirement to carry out further work. We have therefore considered both the potential financial impact of the issues we have identified, and also the likelihood that the issue will be of interest to local taxpayers, the Government and other stakeholders. Based on our initial planning considerations we have identified a significant risk noted on the following page which we view as relevant to our value for money conclusion.





## Value for Money Risks

### What is the significant value for money risk?

We reported in the previous year our views on the financial resilience of the Council and in particular the scale of the financial challenge it faces. Like most local authorities, the Council's finances continue to be stretched. There are significant gaps in the budget over the period of the Medium Term Financial Strategy. The cumulative budget gap to 2020/21 is £20.7million and this also includes the successful delivery of £72.3 million of savings up to that period. Whilst the Council is taking action to identify ways to bridge the gaps, there remains a significant risk to its financial resilience.

### What arrangements does the risk affect?

- ▶ Take informed decisions
- ▶ Deploy resources in a sustainable manner

### What will we do?

Our approach will focus on:

- ▶ Delivery of the Council's 2018/19 savings plans and linkages to delivery of longer-term transformational change;
- ▶ Review of the Council's 2019/20 financial plan; and
- ▶ Review of the Council's longer-term financial strategy in the light of the local and wider financial pressures.



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RESERVE BANK OF INDIA



# 04

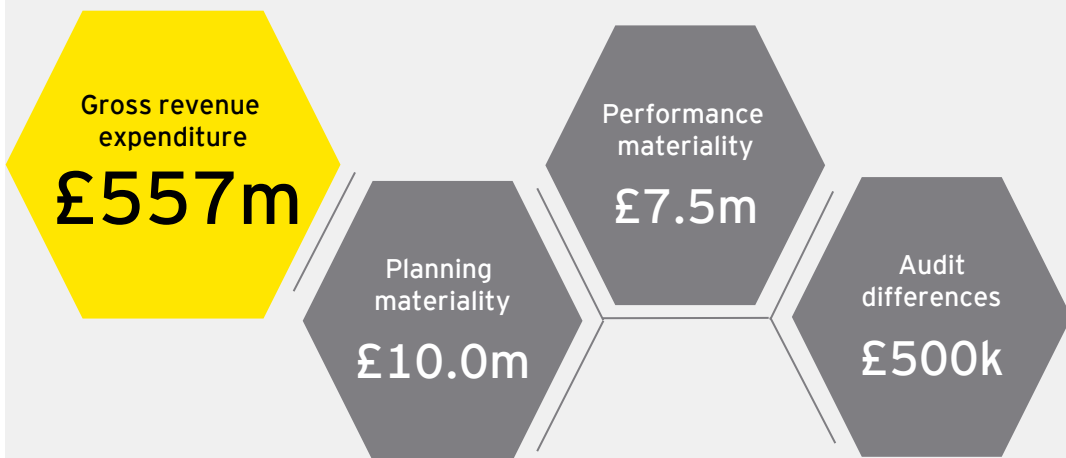
## Audit materiality



# Materiality

## Materiality

For planning purposes, materiality for 2018/19 has been set at £10.025 million. This represents 1.8% of the Council's prior year gross expenditure on provision of services (excluding NDR tariff payments and some non recurring items such as de-recognition of subsidiary assets). In the prior year we applied a threshold of 2%. We have applied a lower percentage on the basis that the Council meets the Local Audit & Accountability Act 2014 criteria for a major local audit based on its size. We have also considered its overall risk profile and public interest in comparison to other councils. We will reassess materiality throughout the audit process. It will be reassessed throughout the audit process. We have provided supplemental information about audit materiality in Appendix C.



We request that the Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

## Key definitions

**Planning materiality** - the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

**Performance materiality** - the amount we use to determine the extent of our audit procedures. We have set performance materiality at £7.519 million which represents 75% of planning materiality.

**Audit difference threshold** - we propose that misstatements identified below this threshold are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the comprehensive income and expenditure statement, balance sheet, and collection fund that have an effect on income or that relate to other comprehensive income.

Other uncorrected misstatements, such as reclassifications and misstatements in the cashflow statement and movement in reserves statement or disclosures, and corrected misstatements will be communicated to the extent that they merit the attention of the audit committee, or are important from a qualitative perspective.

**Specific materiality** - We set lower materiality levels for some disclosures e.g. remuneration disclosures, related party transactions, members' allowances and exit packages, which reflects our understanding that an amount less than our materiality would influence the economic decisions of users of the financial statements in relation to this. We will apply a £1k threshold to any errors identified as this is the rounding point in the financial statements.



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**05**

**Scope of our audit**



## Our Audit Process and Strategy

### Objective and Scope of our Audit scoping

Under the Code of Audit Practice our principal objectives are to review and report on the Council's financial statements and arrangements for securing economy, efficiency and effectiveness in its use of resources to the extent required by the relevant legislation and the requirements of the Code.

We issue an audit report that covers:

#### 1. Financial statement audit

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK and Ireland).

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

#### Procedures required by standards

- Addressing the risk of fraud and error;
- Significant disclosures included in the financial statements;
- Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- Auditor independence.

#### Procedures required by the Code

- Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance; and
- Reviewing and reporting on the Whole of Government Accounts return, in line with the instructions issued by the NAO.

#### 2. Arrangements for securing economy, efficiency and effectiveness (value for money)

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources.



## Our Audit Process and Strategy (continued)

### Audit Process Overview

Our audit involves:

- ▶ Identifying and understanding the key processes and internal controls; and
- ▶ Substantive tests of detail of transactions and amounts.

For 2018/19 we plan to follow a substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

Analytics:

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular journal entries. These tools:

- ▶ Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- ▶ Give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Audit Committee.

Internal audit:

We will regularly meet with the Head of Internal Audit, and review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit plan, where they raise issues that could have an impact on the financial statements.



06

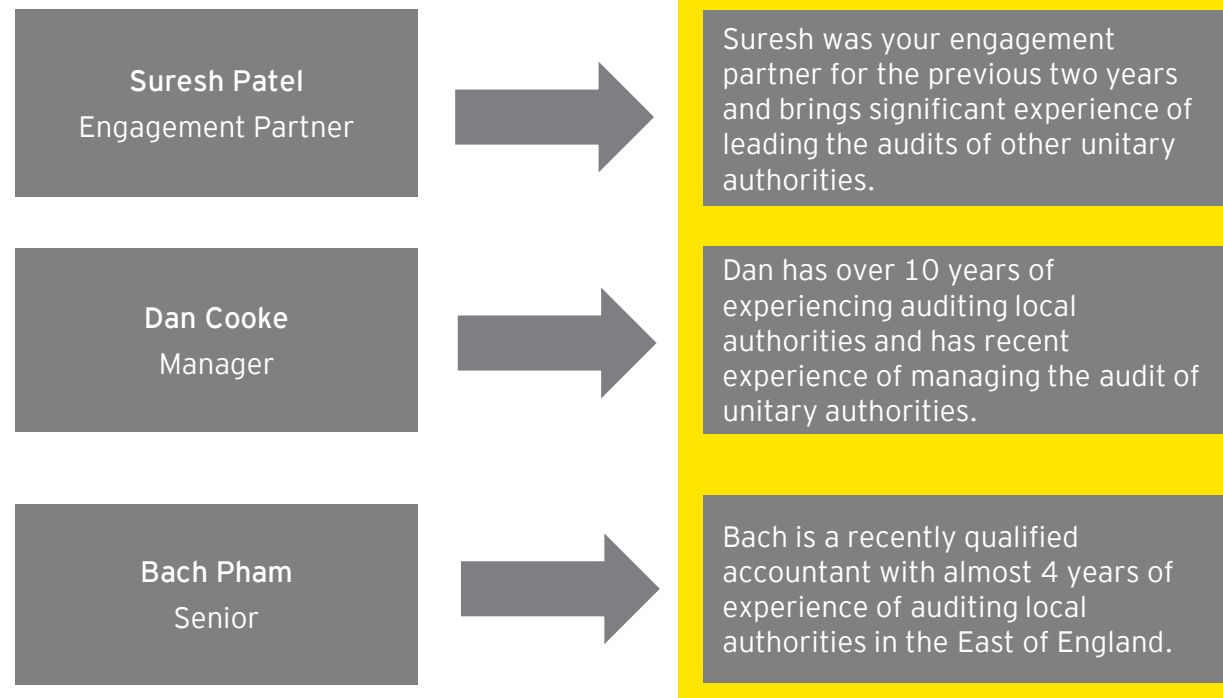
Audit team



## Audit team

### Audit team structure:

We have put together an audit team, based from our Cambridge office, with significant experience of auditing unitary authorities dealing with the same issues as the Council. They are committed to working effectively with the finance team to deliver a smooth and effective audit, adding value wherever possible.



## Audit team

# Use of specialists

Our approach to the involvement of specialists, and the use of their work:

When auditing key judgements, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where either EY or third party specialists provide input for the current year audit are:

Area	Specialists	
	EY	Council
Valuation of Land and Buildings	Real Estates team (if required)	Wilkes Head & Eve & NPS
Pensions disclosure	EY Actuaries	Hymans
PFI	PFI Specialist	N/A

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In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Council's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- ▶ Analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- ▶ Assess the reasonableness of the assumptions and methods used;
- ▶ Consider the appropriateness of the timing of when the specialist carried out the work; and
- ▶ Assess whether the substance of the specialist's findings are properly reflected in the financial statements.



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# Audit timeline





# Audit timeline

## Timetable of communication and deliverables

### Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2018/19. From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.

Audit phase	Timetable	Audit committee timetable	Deliverables
Planning: Risk assessment and setting of scopes.	November	Audit Committee	Outline Audit Plan
	December		Final Audit Plan to management
	January		
Walkthrough of key systems and processes Testing of routine processes and controls	February	Audit Committee	Final Audit Plan (presented to Committee)
	March		Interim audit update (verbal unless there are significant issues)
Interim audit testing	April		
	May/June		
Year end audit Audit Completion procedures	July	Audit Committee	Audit Results Report Audit opinions and completion certificates
	August		Annual Audit Letter

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# Independence



## Introduction

The FRC Ethical Standard and ISA (UK) 260 “Communication of audit matters with those charged with governance”, requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in June 2016, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

### Required communications

Planning stage	Final stage
<ul style="list-style-type: none"> <li>▶ The principal threats, if any, to objectivity and independence identified by Ernst &amp; Young (EY) including consideration of all relationships between the you, your affiliates and directors and us;</li> <li>▶ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review;</li> <li>▶ The overall assessment of threats and safeguards;</li> <li>▶ Information about the general policies and process within EY to maintain objectivity and independence.</li> <li>▶ Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard.</li> </ul>	<ul style="list-style-type: none"> <li>▶ In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed;</li> <li>▶ Details of non-audit services provided and the fees charged in relation thereto;</li> <li>▶ Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us;</li> <li>▶ Written confirmation that all covered persons are independent;</li> <li>▶ Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy;</li> <li>▶ Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and</li> <li>▶ An opportunity to discuss auditor independence issues.</li> </ul>

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In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services. We also provide information on any contingent fee arrangements, the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted. We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, are disclosed.



## Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non-audit services if the service has been pre-approved in accordance with your policy.

### Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Suresh Patel, your audit engagement partner, and the audit engagement team have not been compromised.

### Self interest threats

A self interest threat arises when EY has financial or other interests in the Council. Examples include where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services and we will comply with the policies that you have approved.

None of the services are prohibited under the FRC's ES or the National Audit Office's Auditor Guidance Note 01 and the services have been approved in accordance with your policy on pre-approval. The ratio of non audit fees to audits fees is not permitted to exceed 70%.

At the time of writing, the Council has not engaged us to undertake any non-audit services.

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 4.

There are no other self interest threats at the date of this report.

### Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements. There are no self review threats at the date of this report.

### Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of the Council. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work.

There are no management threats at the date of this report.

## Other communications

### EY Transparency Report 2018

Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the year ended 1 July 2018 and can be found here:

<http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2018>



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# Appendices



## Appendix A

### Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Communities and Local Government. PSAA has published a scale fee for all relevant bodies. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the NAO Code. The fee for 2018/19 reflects the year 1 of the new 5 year contract awarded by PSAA.

	Planned fee 2018/19	Scale fee 2018/19	Final Fee 2017/18
		£	£
Standard Fee - Code work	83,570	83,570	108,533
Additional code work	0	0	6,750
<b>Total audit</b>		<b>83,570</b>	<b>115,283</b>
Other non-audit services not covered above (Housing Benefits - note 1)	N/A	N/A	20,827
<b>Total other non-audit services</b>	<b>N/A</b>	<b>N/A</b>	<b>20,827</b>
<b>Total fees</b>	<b>N/A</b>	<b>83,570</b>	<b>136,110</b>

*All fees exclude VAT*

*Note 1: The Council has appointed a new provider for the 2018/19 housing benefit audit.*

The agreed fee presented is based on the following assumptions:

- ▶ The level of risk in relation to the financial statements and VFM arrangements remains the same;
- ▶ Officers meeting the agreed timetable of deliverables;
- ▶ Our accounts opinion and value for money conclusion being unqualified;
- ▶ Appropriate quality of documentation is provided by the Council; and
- ▶ The Council has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with the Council in advance.

The risks identified in sections 2 and 3 of this plan are likely to result in an audit fee variation, the level of which will be commensurate with the additional work required.



Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

## Appendix B

# Required communications with the Audit Committee





We have detailed the communications that we must provide to the Audit Committee.

### Our Reporting to you





Required communications	 What is reported?	 When and where
Terms of engagement	Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	<p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p> <p>When communicating key audit matters this includes the most significant risks of material misstatement (whether or not due to fraud) including those that have the greatest effect on the overall audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team</p>	Audit Planning Report - February 2019
Significant findings from the audit	<ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations that we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters if any, significant to the oversight of the financial reporting process</li> <li>▶ Findings and issues regarding the opening balances</li> </ul>	Audit Results Report - July 2019

## Appendix B

# Required communications with the Audit Committee (continued)





		 Our Reporting to you
Required communications	 What is reported?	  When and where
Going concern	<p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	Audit Results Report - July 2019
Misstatements	<ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ Corrected misstatements that are significant</li> <li>▶ Material misstatements corrected by management</li> </ul>	Audit Results Report - July 2019
Fraud	<ul style="list-style-type: none"> <li>▶ Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ A discussion of any other matters related to fraud</li> </ul>	Audit Results Report - July 2019
Related parties	<ul style="list-style-type: none"> <li>▶ Significant matters arising during the audit in connection with the entity's related parties including, when applicable:</li> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the entity</li> </ul>	Audit Results Report - July 2019

## Required communications with the Audit Committee (continued)

		 Our Reporting to you
<b>Required communications</b>	 <b>What is reported?</b>	  <b>When and where</b>
Independence	<p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> <li>▶ The principal threats</li> <li>▶ Safeguards adopted and their effectiveness</li> <li>▶ An overall assessment of threats and safeguards</li> <li>▶ Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul> <p>For public interest entities and listed companies, communication of minimum requirements as detailed in the FRC Revised Ethical Standard 2016:</p> <ul style="list-style-type: none"> <li>▶ Relationships between EY, the Council and senior management, its affiliates and its connected parties</li> <li>▶ Services provided by EY that may reasonably bear on the auditors' objectivity and independence</li> <li>▶ Related safeguards</li> <li>▶ Fees charged by EY analysed into appropriate categories such as statutory audit fees, tax advisory fees, other non-audit service fees</li> <li>▶ A statement of compliance with the Ethical Standard, including any non-EY firms or external experts used in the audit</li> <li>▶ Details of any inconsistencies between the Ethical Standard and Group's policy for the provision of non-audit services, and any apparent breach of that policy</li> <li>▶ Details of any contingent fee arrangements for non-audit services</li> <li>▶ Where EY has determined it is appropriate to apply more restrictive rules than permitted under the Ethical Standard</li> <li>▶ The Audit Committee should also be provided an opportunity to discuss matters affecting auditor independence</li> </ul>	<p>Audit planning report, Feb 2019 and Audit results report, July 2019</p>

## Appendix B

# Required communications with the Audit Committee (continued)

		 Our Reporting to you
Required communications	 What is reported?	  When and where
External confirmations	<ul style="list-style-type: none"> <li>▶ Management's refusal for us to request confirmations</li> <li>▶ Inability to obtain relevant and reliable audit evidence from other procedures</li> </ul>	Audit Results Report - July 2019
Consideration of laws and regulations	<ul style="list-style-type: none"> <li>▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off</li> <li>▶ Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of</li> </ul>	Audit Results Report - July 2019
Internal controls	<ul style="list-style-type: none"> <li>▶ Significant deficiencies in internal controls identified during the audit</li> </ul>	Audit Results Report - July 2019 Annual Audit Letter - August 2019
Representations	<ul style="list-style-type: none"> <li>▶ Written representations we are requesting from management and/or those charged with governance</li> </ul>	Audit Results Report - July 2019
Material inconsistencies and misstatements	<ul style="list-style-type: none"> <li>▶ Material inconsistencies or misstatements of fact identified in other information which management has refused to revise</li> </ul>	Audit Results Report - July 2019
Auditors report	<ul style="list-style-type: none"> <li>▶ Key audit matters that we will include in our auditor's report</li> <li>▶ Any circumstances identified that affect the form and content of our auditor's report</li> </ul>	Audit Results Report - July 2019
Fee Reporting	<ul style="list-style-type: none"> <li>▶ Breakdown of fee information when the audit plan is agreed</li> <li>▶ Breakdown of fee information at the completion of the audit</li> <li>▶ Any non-audit work</li> </ul>	Audit Planning Report - February 2019 Audit Results Report - July 2019

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## Additional audit information

### Other required procedures during the course of the audit

In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.

#### Our responsibilities required by auditing standards

- ▶ Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
- ▶ Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Council's internal control.
- ▶ Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Concluding on the appropriateness of management's use of the going concern basis of accounting.
- ▶ Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Council to express an opinion on the consolidated financial statements. Reading other information contained in the financial statements, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and
- ▶ Maintaining auditor independence.

## Additional audit information (continued)

### Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines:

- ▶ The locations at which we conduct audit procedures to support the opinion given on the Council's financial statements; and
- ▶ The level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

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### About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

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