Peterborough City Council

Annual Audit Letter for the year ended 31 March 2020

May 2022

Building a better working world

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Public Sector Audit Appointments Ltd (PSAA) have issued a ‘Statement of responsibilities of auditors and audited bodies’. It is available from the Chief Executive of each audited body and via the PSAA website (www.psaa.co.uk).

This 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 April 2018)’ issued by 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 statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities / Terms and Conditions of Engagement. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Hywel Ball, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

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Section 1

Executive Summary

Executive Summary

We are required to issue an annual audit letter to Peterborough City Council (the Council) following completion of our audit procedures for the year ended 31 March 2020.

Covid-19 had an impact on a number of aspects of our 2019/20 audit. We set out these key impacts below.

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Area of impact	Commentary
Impact on the delivery of the audit	
► Changes to reporting timescales	As a result of Covid-19, new regulations, the Accounts and Audit (Coronavirus) (Amendment) Regulations 2020 No. 404, have been published and came into force on 30 April 2020. This announced a change to publication date for final, audited accounts from 31 July to 30 November 2020 for all relevant authorities. We worked with the Council to deliver our audit in line with the revised reporting timescale.
Impact on our risk assessment	
► Valuation of Property Plant and Equipment	The Royal Institute of Chartered Surveyors (RICS), the body setting the standards for property valuations, issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets might cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty have been included in the year-end valuation reports produced by the Council's external valuer. We consider that the material uncertainties disclosed by the valuer gave rise to an additional risk relating to disclosures on the valuation of property, plant and equipment.
► Disclosures on Going Concern	Financial plans for 2020/21 and medium term financial plans will need revision for Covid-19. We considered the unpredictability of the current environment gave rise to a risk that the Council would not appropriately disclose the key factors relating to going concern, underpinned by managements assessment with particular reference to Covid-19 and the Council's actual year end financial position and performance.
► Events after the balance sheet date	We identified an increased risk that further events after the balance sheet date concerning the current Covid-19 pandemic will need to be disclosed. The amount of detail required in the disclosure needed to reflect the specific circumstances of the Council.
Impact on the scope of our audit	
► Information Produced by the Entity (IPE)	We identified an increased risk around the completeness, accuracy, and appropriateness of information produced by the entity due to the inability of the audit team to verify original documents or re-run reports on-site from the Council's systems. We undertook the following to address this risk: ‣ Used the screen sharing function of Microsoft Teams to evidence re-running of reports used to generate the IPE we audited; and ‣ Agree IPE to scanned documents or other system screenshots.
► Consultation requirements	Additional EY consultation requirements concerning the impact on auditor reports. The changes to audit risks and audit approach changed the level of work we needed to perform.

Executive Summary (cont'd)

The tables below set out the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinion on the Council's:	
► Financial statements	Unqualified – the financial statements give a true and fair view of the financial position of the Council as at 31 March 2020 and of its expenditure and income for the year then ended. Our audit opinion reported: ▸ Material uncertainty relating to going concern: We draw attention to Note 44 in the financial statements, which describes the Authority's ability to continue as a going concern. As stated in Note 44, this indicates that a material uncertainty exists that may cast significant doubt on the Authority's ability to continue providing the current level of services without an increase in planned funding. Our opinion was not modified in respect of this matter. ▸ Emphasis of matter – Property, Plant and Equipment: We draw attention to Note 22 and Note 43 of the financial statements, which describe the valuation uncertainty the Authority is facing as a result of COVID-19 in relation to property valuations. Our opinion was not modified in respect of this matter.
► Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Annual Account.
► Concluding on the Council's arrangements for securing economy, efficiency and effectiveness	As a result of the procedures performed we modified our value for money conclusion and issued an adverse opinion. This is to recognise that the structural financial resilience pressures and concerns facing the Authority before and after the Covid-19 pandemic have a significant and pervasive impact on the Authority's ability to secure adequate arrangements for Value for Money in its use of resources. Financial management, decision making, partnership working; and Challenges for the next year. See Section 4 for further details.

Area of Work	Conclusion
Reports by exception:	
► Consistency of Governance Statement	The Governance Statement was consistent with our understanding of the Council.
► Public interest report	We had no matters to report in the public interest.
► Written recommendations to the Council, which should be copied to the Secretary of State	We had no matters to report.
► Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.

Executive Summary (cont'd)

Area of Work	Conclusion
Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	HM Treasury (HMT) have closed the 2019/20 data submission cycle and it is no longer possible for entities to submit their cycle 2 data. They are not putting in place alternative arrangements for 2019/20 data collection. It has been confirmed by HMT that this removes the audit responsibility to issue an assurance statement in respect of the Council's Whole of Government Accounts consolidation pack.

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 21 June 2021
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	Our certificate was issued on 16 May 2022

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Neil Harris
Associate Partner
For and on behalf of Ernst & Young LLP

Section 2

Purpose and Responsibilities

Purpose

The Purpose of this Letter

The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council.

We have already reported the detailed findings from our audit work in our 2019/20 Audit Results Report to the 21 June 2021 Audit Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.

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Responsibilities

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Responsibilities of the Appointed Auditor

Our 2019/20 audit work has been undertaken in accordance with the Audit Plan that we issued on 9 March 2020 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- Expressing an opinion:
  - On the 2019/20 financial statements; and
  - On the consistency of other information published with the financial statements.
- Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- Reporting by exception:
  - If the annual governance statement is misleading or not consistent with our understanding of the Council;
  - Any significant matters that are in the public interest;
  - Any written recommendations to the Council, which should be copied to the Secretary of State; and
  - If we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the NAO.

Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement (AGS). In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Section 3

Financial Statement Audit

Financial Statement Audit

Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health.

We audited the Council and Group's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office and issued an unqualified audit report on 21 June 2021.

Our detailed findings were reported to the 21 June 2021 Audit Committee.

The key issues identified as part of our audit were as follows:

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Significant Risk	Conclusion
Misstatements due to fraud or error 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.	Our mandatory procedures did not identify any instances of management override. As reported in our Audit Plan, our work to identify fraud risks during the planning stages identified those areas of the accounts that involve management estimates and judgements as the key areas at risk of manipulation. The identified areas were: • the incorrect capitalisation of revenue expenditure and REFCUS. • the incorrect application of MRP accounting. • inappropriate use of capital receipts. The results of our work on these specific risks are set out on the following pages.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Misstatements due to fraud or error – the incorrect capitalisation of revenue expenditure and REFCUS The Authority 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 charged to the comprehensive income and expenditure account. In 2019/20 the Authority has incurred £64.0 million capital expenditure (of which REFCUS represented £19.0 million).	Our mandatory procedures did not identify any instances of incorrect capitalisation of revenue expenditure. • Our sample testing of additions to property, plant and equipment found that they had been correctly classified as capital and included at the correct value. • Our sample testing of additions to property, plant and equipment did not identify any revenue items that were incorrectly classified. • Our sample testing of REFCUS transactions found that they had been correctly classified and the expenditure met the definition of allowable expenditure, or was incurred under direction from the secretary of state. • Our data analytical procedures did not identify any journal entries that incorrectly moved expenditure into capital codes.
Misstatements due to fraud or error – the incorrect application of MRP accounting The Authority is under significant 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 application and calculation of the minimum revenue provision. The Authority must make an annual contribution from revenue to reduce its overall borrowing requirement. This is termed the Minimum Revenue Provision (MRP). The MRP is determined prudently in accordance with statutory guidance. Over the last 18 months, the Authority's approach to MRP has been subject to media attention as well as scrutiny by Ministry of Housing, Communities & Local Government (MHCLG). Given this level of scrutiny and that MRP could be manipulated to artificially reduce expenditure we have identified the MRP calculation as a significant risk.	Our mandatory procedures did not identify any issues with the application of the MRP accounting. • Our testing confirmed that the MRP calculation met the statutory guidance. • Our re-performance of the MRP calculation did not identify any material misstatements although we did identify some trivial adjustments which would need to be applied in future periods to ensure a cumulative material error does to arise. • Our review of the MRP policy and disclosure did not identify any material audit issues. • There are some implications for MRP as a result of the Empower loan impairment but these will relate to 2020/21 and we will cover as part of that audit period.

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Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Misstatements due to fraud or error – inappropriate use of capital receipts The Authority is under significant 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 and use of capital receipts 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 higher for adjustments concerning the application of useable capital receipts and deferred capital receipts.	Our mandatory procedures did not identify any instances of inappropriate use of capital receipts. • Our sample testing of the application of capital receipts confirmed that they met the correct definition of funding sources. • Our sample testing of deferred capital receipts found that conditions had been correctly applied. • Our data analytical procedures performed to identify and test journal entries adjustments that impact capital receipts did not identify any issues.
Valuation of property, plant and equipment assets under depreciated replacement cost model Property, plant and equipment (PPE) represents a significant balance in the Authority's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Material judgemental inputs and estimation techniques are required to calculate the 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 Authority's DRC asset base is significant (£266 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 significant accounting estimates.	Our consideration of the work performed by the Authority's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work did not identify any issues. Our EY Real Estates team did not identify any material issues with the underlying assumptions used to value to DRC assets. However, they did identify some issues with some of the valuer's methodology which we have shared with management. Our review of DRC assets not subject to valuation in 2019/20 confirmed that the remaining asset base was not materially misstated. Our consideration of the useful economic lives in the most recent valuation did not identify any issues. Accounting entries had been correctly disclosed in the financial statements. Note we did identify some audit adjustments in relation to property, plant and equipment. These were reported in the Audit Results Report.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Valuation of Non-DRC PPE assets & Investment Property The Royal Institute of Chartered Surveyors (RICS), the body setting the standards for property valuations, issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets might cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty have been included in the year-end valuation reports produced by the Authority's external valuer. We consider that the material uncertainties disclosed by the valuer gave rise to an additional risk relating to disclosures on the valuation of property, plant and equipment. We therefore increased our inherent risk on valuation of Non-DRC PPE assets & Investment Property to significant. As the Authority's non-DRC and investment property asset base is significant (£119 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.	Our consideration of the work performed by the Authority's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work did not identify any issues. Our EY Real Estates team did not identify any material issues with the underlying assumptions used to value to non-DRC assets. However, they did identify some issues with some of the valuer's methodology which we have shared with management. Our review of non-DRC assets not subject to valuation in 2019/20 confirmed that the remaining asset base was not materially misstated. Our consideration of the useful economic lives in the most recent valuation did not identify any issues. Accounting entries had been correctly disclosed in the financial statements. Note we did identify some audit adjustments in relation to property, plant and equipment. These were reported in the Audit Results Report.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Other Areas of Audit Focus Findings	Conclusion
PFI accounting	Our audit testing confirmed that there were no audit issues in the calculation of the PFI annual payments or the liability held in the balance sheet. We have confirmed that the figures in the accounting models are consistent with the disclosures in the financial statements.
Pension Liability Valuation	We were informed by the Pension Fund auditor that the Peterborough City Council pension fund investment assets are understated by £2.56 million. The Authority decided not to adjust for this difference on the ground of materiality and this was reported in the Council's letter of representation to the auditor.
Recoverability of NHS Accounts Receivable Balances	Our audit testing did not identify any issues with the recoverability of the NHS accounts receivable balances.
Group Accounting	Our audit testing did not identify any issues with the group accounts or the group scoping.
Going concern disclosure	Officers carried out an assessment of the impact of Covid-19 on the Authority's income, expenditure, balances and reserves to inform reporting to the Audit Committee and other members. These assessments were used to enhance the disclosure in the financial statements around the going concern assertion. We reviewed the assessment, focusing on the reasonableness of the financial impact assessment, cash flow and liquidity forecasts, known outcomes, sensitivities, mitigating actions and key assumptions, including around reductions in fees and charges. We also considered the adequacy of the revised disclosure note and its consistency with the going concern assessment and our audit procedures. We reviewed the revised going concern disclosure and were satisfied that it adequately reflects the Authority's assessment and informs the reader of the impact of the Covid-19 pandemic on the Authority's finances. We completed our internal consultation with our Professional Practice Directorate on our audit work and assessment of the Authority's going concern disclosure. This has resulted in a material uncertainty in our audit report as the Authority's financial position casts significant doubt on their ability to continue to provide the current levels of service provision for the next 12 months and beyond.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Other Audit Findings	Conclusion
Recoverability of the Authority's £23 million loan to Empower Community Management LLP (Empower)	We reviewed the recoverability of the £23 million loan to Empower, taking account of conditions and events that took place before and after the balance sheet date. We agreed that it was appropriate for the Authority to make a post balance event adjustment and disclosure in the financial statements to recognise the conditions leading to an impairment of the loan and reclassification from short to long term debtors. We noted the judgement of the Authority that the impairment of the loan recognised in the audited 2019/2020 accounts was determined using a effective interest rate (2.1%), consistent with the Authority's weighted average cost of capital as the likely decision to bring the asset management arrangements in-house is a more representative discount rate to estimate the carrying value of the loan as at 31 March 2020. This value was within a reasonable range of estimation and uncertainty to the 2.5% terms of the long-term refinancing agreed with Empower after the balance sheet date; and the effective interest rate we believe should have been used to determine the expected credit loss on the loan under IFRS9. The Authority's disclosure in the financial statements appropriately sets out that in the unlikely event that the Authority were to seek an external provider to buy-out the finance and asset management arrangements under commercial terms, the enterprise value would be £15.4 million. Whilst the Authority had taken the appropriate steps to seek specialist legal, professional and commercial advice on the events that took place with the financing of the loan since the balance sheet date; adjusting and reporting these circumstances in the 2019/2020 accounts and in decision making papers to Cabinet on 21 June 2021, nevertheless we believe there have been significant weaknesses in the governance arrangements with Empower Community Management LLP during the 2020/2021 financial year which has exposed the Authority to financial loss. Our specialist work has determined that the re-financing of the loan after the balance sheet had aggressive assumptions on debt/equity ratios, which we note the Authority also recognised in its decision making papers. Empower had proposed additional income streams from P2P trading, however we understand from the Authority that this could not be included in the model for valuation as the contracts had not been signed. We recommend that the Authority: • Reviews any similar finance arrangements to ensure that there is not a risk of exposure to further financial loss. • Reviews the appropriateness of its Minimum Revenue Provision policy for capital loans in light of these events. • Should it decide to bring the solar panel assets and asset management arrangements in-house, obtains an up-to-date valuation of the assets as soon as practicable in order that the Authority can determine whether there are any additional indicators of impairment and the basis on which the solar panel assets are recognised for financial reporting and asset management purposes. Although we have yet to determine whether this would be an adjusting or non-adjusting event for the 2020/2021 financial statements, the Authority will need to obtain this information to make appropriate disclosures and accounting judgements in the 2020/2021 financial statements to reflect the conditions that are or are expected to be in place between now and the time when the audited accounts are authorised for issue. We will follow-up all of these matters during our audit of the 2020/2021 Authority's financial statements and in terms of arrangements for informed decision making, we will provide further reporting in our Value for Money arrangements narrative commentary as appropriate.

Financial Statement Audit (cont'd)

Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	We determined planning materiality to be £4.9 million, which is 1% of gross revenue expenditure reported in the accounts of £492 million. We consider gross revenue expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council. This results in a performance materiality, at 75% of our overall planning materiality, of £3.7 million. The performance materiality assigned for the group entity was £0.739 million.
Reporting threshold	We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.246 million across both the single and group entities.

We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include:

- Remuneration disclosures including any severance payments, exit packages, members allowances and termination benefits: We agreed disclosures back to source data and approved amounts applying a reduced materiality level of £1,000 in line with bandings disclosed in the financial statements.
- Related party transactions: We tested the completeness of related party disclosures and the accuracy of all disclosures by checking back to supporting evidence applying a reduced materiality level equal to the reporting threshold.
- Audit Fees: We agree the figures back to the agreement with officers, applying a reduced materiality level of £1,000.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.

Section 4

Value for Money

Value for Money

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness in its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

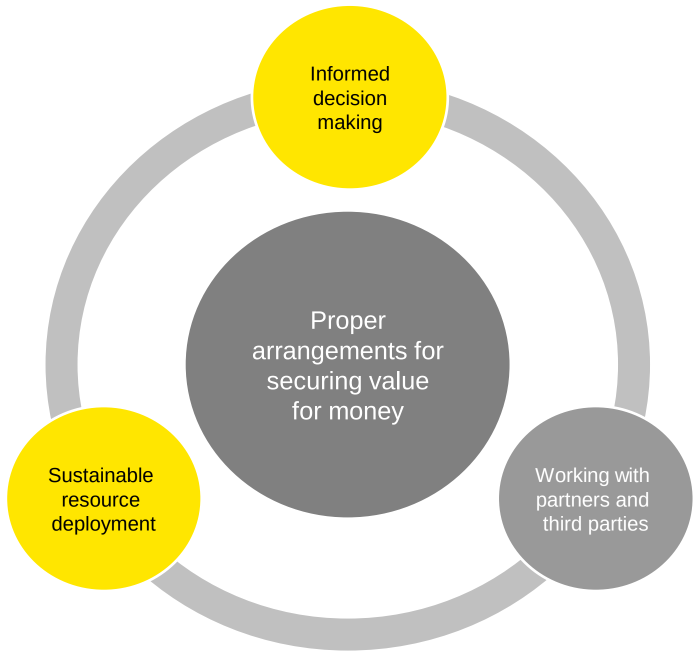
- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.

On 16 April 2020 the National Audit Office published an update to auditor guidance in relation to the 2019/20 Value for Money assessment in the light of Covid-19. This clarified that in undertaking the 2019/20 Value for Money assessment auditors should consider NHS bodies' response to Covid-19 only as far as it relates to the 2019/20 financial year; only where clear evidence comes to the auditor's attention of a significant failure in arrangements as a result of Covid-19 during the financial year, would it be appropriate to recognise a significant risk in relation to the 2019/20 VFM arrangements conclusion.

We identified one significant risk in relation to these arrangements. The tables below present the findings of our work in response to the risks identified and any other significant weaknesses or issues to bring to your attention.

We have performed the procedures outlined in our audit plan. We identified the following significant weaknesses in the Council's arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We concluded our audit procedures on your arrangements to secure economy, efficiency and effectiveness in your use of resources and modified our value for money conclusion and issued an adverse opinion. This was to recognise that the structural financial resilience pressures and concerns facing the Authority before and after the Covid-19 pandemic have a significant and pervasive impact on the Authority's ability to secure adequate arrangements for Value for Money in its use of resources.



Value for Money (cont'd)

Significant Risk	Conclusion
We reported in previous years our views on the financial resilience of the Authority and in particular the scale of the financial challenge it faces. Like most local authorities, the Authority's finances continue to be stretched. There are significant gaps in the budget over the period of the Medium Term Financial Strategy which have still not been addressed. The cumulative unmitigated budget gap to 2022/23 is £30.6 million and this also includes the successful delivery of £26.3 million of savings up to that period and some savings which are still subject to finalisation. It also includes a £10 million capitalisation direction currently with MHCLG for approval. The Chief Financial Officer has expressed concerns on the fragility of the Authority's financial position in the robustness statement presented to 25th February 2020 Cabinet supporting the 2020/2021 budget. In particular, there is a risk the Chief Financial Officer could trigger the production of a Section 114 report if the Authority could not report a balanced budget for 2020/21, where: 1. the Capitalisation Direction approval is not confirmed by 31 March 2020; or 2. realistic transformational plans, for reducing the cost of service delivery required to deliver a balanced and sustainable budget for future years, are not developed, and implementation commenced by July 2020. Whilst the Authority is taking action to identify ways to bridge the gaps, there remains a significant risk to its financial resilience.	To address this risk, we planned: Phase 1 – Financial Resilience Concerns (March to April 2020): • Robust review of the Authority's Medium Term Financial Strategy and the concerns raised by the Chief Financial Officer, including correspondence with MHCLG on the capitalisation direction application; • Developing an understanding of how the Authority identifies its budget gaps and risk mitigations; • Consideration of exercising our statutory powers at this point (by April 2020) and if appropriate issuing a statutory written recommendation under section 24 (schedule 7) of the Local Audit and Accountability Act 2014. Phase 2 – Authority's Response to Financial Resilience Concerns (April to July 2020): • Developing an understanding of how the Authority quantifies and quality assures its savings plans; • Reviewing the extent to which the Authority is addressing the future budget gaps identified within its Medium Term Financial Strategy, including the robustness of assumptions and judgements associated with savings and transformation plans. See the following slide for details of our audit procedures performed.

Value for Money (cont'd)

Conclusion

For both phases of the risk we have engaged with our Strategy and Transactions Team to provide specialist support to work with the audit team in reviewing, challenging and exercising appropriate professional scepticism on the Authority's medium-term financial strategy and proposed transformation saving plans.

We prepared a detailed scope of work for phase 1 and 2 and agreed this with officers at the Authority. We have now completed our procedures across both phases.

Phase 1 Conclusion: Our modelling suggests that the Authority's forecasts within the current financial year and over the medium-term financial strategy are both reasonable and appropriate compared with our base-case economic scenario. It is however noted that the financial challenge the Authority is facing, is forecast to be considerably more severe in our more volatile economic conditions.

The Authority's ability to deal with these challenges is significantly hindered by their reserve position, which is insufficient in dealing with the forecast financial challenge beyond the current financial year.

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The Authority's financial resilience is therefore a significant hinderance on the Authority's ability to provide value for money from public resources, as the financial uncertainty they face over the medium-term makes it difficult for the Authority to make meaningful and sustainable decisions that provide value for money. We therefore expect to modify our value for money conclusion.

Phase 2 Conclusion: Our analysis of the Authority's response to their financial resilience concerns found that for the latest development of the 2021/22 savings plan, the Authority exhibited good practice in the design principles of the plan. Given the timescales for finalising the Medium Term Financial Strategy, we found the Authority had given appropriate consideration to the budget gap, and developed the expected level of key documentation for current saving proposals. Furthermore, the allocation of these savings was appropriately distributed between departments as well as thematically.

It was also found that the Authority had comprehensive governance processes established for developing, monitoring and reporting against saving proposals. Evidence was provided that these processes are regularly conducted and receive the appropriate level of political and strategic oversight.

Nevertheless, despite the good practices that the Authority exhibits in developing well designed and governed savings proposals, the size of the current budget gap should be viewed as a significant risk in terms of delivering a balanced budget in 2021/22. The budget gap of £35.6 million in 2021/22, reflects a significant uplift in the savings target compared with previous delivery, and furthermore reflects a significant portion of service expenditure levels, which makes achievability a high risk for the Authority.

Capitalisation Direction: In October 2020 the Authority approached MHCLG to enable the further exploration of alternatives to issuing a Section 114 notice. The Authority has been engaged in regular discussions with MHCLG in respect of the Authority's finances. In February 2021 the Authority received conditional confirmation for a Capitalisation Direction of up to £4.8 million in 2020/21 and approval in principle a Capitalisation Direction of up to £20.0 million in 2021/22. This exceptional support has enabled the Authority to prepare a balanced budget for 2021/22.

Overall Conclusion: While the Authority demonstrates good development of their medium term financial strategies and exhibits a good understanding of the saving challenges they are facing the budget gap is still significant. We are therefore modifying our value for money conclusion to recognise that the structural financial resilience pressures and concerns facing the Authority before and after the Covid-19 pandemic have a significant and pervasive impact on the Authority's ability to secure adequate arrangements for Value for Money in its use of resources.

Section 5

Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

We are required to perform the procedures specified by the National Audit Office on the accuracy of the consolidation pack prepared by the Council for Whole of Government Accounts purposes.

HM Treasury (HMT) have closed the 2019/20 data submission cycle and it is no longer possible for entities to submit their cycle 2 data. They are not putting in place alternative arrangements for 2019/20 data collection. It has been confirmed by HMT that this removes the audit responsibility to issue an assurance statement in respect of the Council's Whole of Government Accounts consolidation pack.

Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and did not identify any areas of concern.

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Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Council or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.

Other Reporting Issues (cont'd)

Objections Received

We did not receive any objections to the 2019/20 financial statements from members of the public.

Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

Independence

We communicated our assessment of independence in our Audit Results Report to the Audit Committee on 21 June 2021. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

Control Themes and Observations

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

We have adopted a fully substantive audit approach and have therefore not tested the operation of controls.

We did identified one other control finding which we would like to bring to your attention:

- As part of our procedures performed in relation to the Authority's contracts register we identified two significant contracts which were not held on the register.

Recommendation: We recommend that the Authority revisit their controls covering the completeness of the contracts register and ensure that all significant contracts are recorded on the register.

Section 6

Focused on your future

Focused on your future

Implementation of IFRS 16 Leases

In previous reports to the Audit Committee, we have highlighted the issue of new accounting standards and regulatory developments. IFRS 16 introduces a number of significant changes which go beyond accounting technicalities. For example, the changes have the potential to impact on procurement processes as more information becomes available on the real cost of leases. The key accounting impact is that assets and liabilities in relation to significant lease arrangements previously accounted for as operating leases will need to be recognised on the balance sheet. IFRS 16 requires all substantial leases to be accounted for using the acquisition approach, recognising the rights acquired to use an asset. IFRS 16 does not come into effect for the Council until 1 April 2022. However, officers should be acting now to assess the Council's leasing positions and secure the required information to ensure the Councill will be fully compliance with the 2022/2023 Code. The following table summarises some key areas officers should be progressing.

IFRS 16 theme	Summary of key measures
Data collection	Management should: ▸ Put in place a robust process to identify all arrangements that convey the right to control the use of an identified asset for a period of time. The adequacy of this process should be discussed with auditors. ▸ Classify all such leases into low value; short-term; peppercorn; portfolio and individual leases ▸ Identify, collect, log and check all significant data points that affect lease accounting including: the term of the lease; reasonably certain judgements on extension or termination; dates of rent reviews; variable payments; grandfathered decisions; non-lease components; and discount rate to be applied.
Policy Choices	The Council needs to agree on certain policy choices. In particular: ▸ Whether to adopt a portfolio approach ▸ What low value threshold to set and agree with auditors ▸ Which asset classes, if any, are management adopting the practical expedient in relation to non-lease components ▸ What is managements policy in relation to discount rates to be used?
Code adaptations for the public sector	Finance teams should understand the Code adaptations for the public sector. The Code contains general adaptations, (e.g. the definition of a lease); transitional interpretations (e.g. no restatement of prior periods) and adaptations that apply post transition (e.g. use of short-term lease exemption).
Transitional accounting arrangements	Finance teams should understand the accounting required on first implementation of IFRS 16. The main impact is on former operating leases where the Council is lessee. However, there can be implications for some finance leases where the Council is lessee; and potentially for sub-leases, where the Council is a lessor, that were operating leases under the old standard.
Ongoing accounting arrangements	Finance teams need to develop models to be able to properly account for initial recognition and subsequent measurement of right of use assets and associated liabilities. This is more complex than the previous standard due to more regular remeasurements and possible modifications after certain trigger events.
Remeasurements and modifications	Finance teams need to familiarise themselves with when the 'remeasurement' or 'modification' of a lease is required and what to do under each circumstance. A modification can lead to an additional lease being recognised. It is also important to know when remeasurements require a new discount rate is to be applied to the lease.

Appendix A

Audit Fees

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Audit Fees

Our final fee for 2019/20 is in line with the fee determined by the PSAA.

Description	Final Fee 2019/20 £	Planned Fee 2019/20 £	Scale Fee 2019/20 £	Final Fee 2018/19 £
Total Audit Fee – Code work	175,549	213,271	83,570	106,334

We agreed our planned fee of £213,271 with Management and reported in our Audit Results Report to Audit Committee on 21 June 2021.

In March 2022 PSAA determined that the total fee variation for Peterborough City Council 2019/20 would be £91,979.

Total audit engagement hours for the audit exceeded 3,300 hours. A commercial benchmark for an audit of this size and complexity would be in the region of £350,000.

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ED None

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