



## **North Ayrshire Council**

Report to the Audit and Scrutiny Committee, Members of the  
Council and the Controller of Audit on the 2019/20 audit

Issued on 14 September for the meeting on 29 September 2020

# Contents

---

## 01 Our report

Introduction	3
--------------	---

### ***Financial statements audit***

Quality indicators	8
--------------------	---

Our audit explained	9
---------------------	---

Significant risks	10
-------------------	----

Other areas of audit focus	14
----------------------------	----

Other significant findings	18
----------------------------	----

COVID-19 outbreak	20
-------------------	----

Our audit report	21
------------------	----

Your annual report	22
--------------------	----

---

## 02 Appendices

Purpose of our report and responsibility statement	24
--	----

Action plan	25
-------------	----

Our other responsibilities explained	26
--------------------------------------	----

Independence and fees	27
-----------------------	----

Quality of public audit in Scotland	28
-------------------------------------	----

# Introduction

## The key messages in this report

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

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

I have pleasure in presenting our final report to the Audit and Scrutiny Committee ("the Committee") of North Ayrshire Council ("the Council") for the year ending 31 March 2020 audit. The scope of our audit was set out within our planning report presented to the Committee in January 2020.

This audit was carried out under unusual circumstances, being a remote audit conducted during the national lockdown in response to COVID-19. We recognise the extra pressure faced by Council staff in preparing the annual report and in preparing for the audit. We engaged early with management on the potential implications of COVID-19 for the preparation of the annual report as well as the audit, and management confirmed their desire to work to the original timetable. While the shift to remote working placed pressure on the original timetable for preparation of the annual report and completion of the audit, we have worked closely with management to mitigate this whilst maintaining audit quality as our number one focus.

This report summarises our findings and conclusions in relation to:

- The audit of the **financial statements**; and
- Consideration of the **four audit dimensions** that frame the wider scope of public sector audit requirements as illustrated in the following diagram. This includes our consideration of the Accountable Officers' duty to secure best value.



# Introduction (continued)

## The key messages in this report (continued)

I would like to draw your attention to the key messages of this paper:

### **Conclusions from our testing**

Based on our audit work completed to date we expect to issue an unmodified audit opinion.

The impact of COVID-19 has led to a material uncertainty being identified by the Council's property valuers in relation to the valuation of the Council's estate. As a result, we expect to include an 'Emphasis of Matter' paragraph within our audit report.

The management commentary and annual governance statement comply with the statutory guidance and proper practice and are consistent with the financial statements and our knowledge of the Council.

The auditable parts of the remuneration report have been prepared in accordance with the relevant regulation.

A summary of our work on the significant risks is provided in the dashboard on page 10.

No uncorrected misstatements in excess of our reporting threshold of £250,000 or material disclosure deficiencies have been identified up to the date of this report.

### **Status of the financial statements audit**

Our audit work is complete.

### **Conclusions on audit dimensions**

As set out on page 3, our audit work covered the four audit dimensions. This incorporated the specific risks highlighted by Audit Scotland.

Our separate detailed report is presented along with this paper and sets out our findings and conclusions on each dimension. In accordance with the Code of Audit Practice, we have included our overall conclusions within this report.

The outbreak of COVID-19 has brought unprecedented challenges to organisations around the country. It is not yet known what long-term impacts these will have on populations and on the delivery of public services, but they will be significant and could continue for some time. While our reports makes reference to COVID-19 where relevant in each of the dimensions, we have not considered the full impact of COVID-19 on the Council at this stage.

# Introduction (continued)

## The key messages in this report (continued)

### Conclusions on audit dimensions (continued)

**Financial Management** - The Council has strong financial management arrangements. The General Fund and HRA ended the year with an in-year surplus and savings targets were largely achieved. The financial position and variances were transparently reported to Cabinet throughout the year. The change to Section 95 Officer role from 1 April 2020 has transitioned smoothly.

**Financial sustainability** - The Council achieved short-term financial balance in 2019/20 and has set a balanced budget for 2020/21. The current reserves held are at an acceptable level. It is also positive to note that the Council is actively assessing the financial impact of COVID-19. There does, however, remain a risk, therefore it is important that the position is closely monitored.

As reported through the BVAR, the Council has made good progress with its transformation agenda, however, it still faces a significant shortfall and detailed plans are not yet in place. The Council has a coordinated approach to workforce planning and is developing workforce plans to support transformational change.

The full development of workforce plans and arrangements to monitor and report the benefits from its transformation plans needs to be progressed as a matter of priority.

**Governance and transparency** - The Council continues to have strong leadership in place and robust governance and scrutiny arrangements in place. Appropriate arrangements have been put in place in response to the COVID-19 pandemic.

The Council continues to be open and transparent. It also continues to embrace the principles of Community Empowerment and has a clear focus on improving equality outcomes.

The IJB has made some good progress during the year, particularly in its approach to transformation, however, the financial position of the IJB continues to be challenging. This is being actively monitored by the Council.

**Value for money** - The Council continues to have a clear and robust performance management framework in place. It also has a robust and long-standing arrangements in place to comply with the new SPI Direction including its public performance reporting requirements.

The performance of the Council is showing evidence of improvements in a number of areas. We recognise that the COVID-19 pandemic has had a significant impact on a number of services. It is important that the Council take any lessons learned as it moves into the recovery phase to consider alternative approaches to service delivery.

**Best Value** - The Council has robust arrangements in place to secure best value and has a clear understanding of areas which require further development.

# Introduction (continued)

## The key messages in this report (continued)

### **Next steps**

An agreed Action Plan is included as an Appendix on page 30 of this report in relation to the financial statements audit where we have followed up previous years actions. A separate Action Plan on the findings of the audit dimensions work is included in our separate report. We will consider progress with the agreed actions as part of our 2020/21 audit.

### **Added value**

Our aim is to add value to the Council by providing insight into, and offering foresight on, financial sustainability, risk and performance by identifying areas for improvement and recommending and encouraging good practice. In so doing, we aim to help the Council promote improved standards of governance, better management and decision making, and more effective use of resources.

This is provided throughout both of our reports. In addition, as information emerges as a result of the COVID-19 pandemic, we have shared guidance with management on areas to consider in relation to internal controls, fraud risks and annual reporting. In addition, invites have been issued to our weekly webinar "Responding to COVID-19: Updates and practical steps" which are open to anyone to join.

**Pat Kenny**  
**Audit Director**

# Financial statements audit





# Quality indicators

## Impact on the execution of our audit

Management and those charged with governance are in a position to influence the effectiveness of our audit, through timely formulation of judgements, provision of accurate information, and responsiveness to issues identified in the course of the audit. This slide summarises some key metrics related to your control environment which can significantly impact the execution of the audit. We consider these metrics important in assessing the reliability of your financial reporting and provide context for other messages in this report.

Area	Grading	Reason
Timing of key accounting judgements	●	Management demonstrated a clear understanding of key accounting judgements and estimates made in the preparation of the Annual Report and Accounts and provided sufficient appropriate evidence of good quality to support these.
Adherence to deliverables timetable	●	Key deliverables were provided in a timely manner, in advance of agreed timelines. Any follow-up requests during the audit were quickly actioned.
Access to finance team and other key personnel	●	Deloitte and the Council have worked together to facilitate remote communication during the audit. This has included effective use of such technologies as Microsoft Team and Deloitte Connect.
Quality and accuracy of management accounting papers	●	On the whole documentation provided has been a good standard. This included documentation that reconciled to the draft financial statements.
Quality of draft financial statements	●	A full draft of the annual report and accounts was received for audit on 29 June 2020. The draft was of a high standard with limited changes required.
Response to control deficiencies identified	●	We have not identified any significant control deficiencies during the course of our audit.
Volume and magnitude of identified errors	●	We have not identified any significant financial adjustments to date.



Lagging



Developing

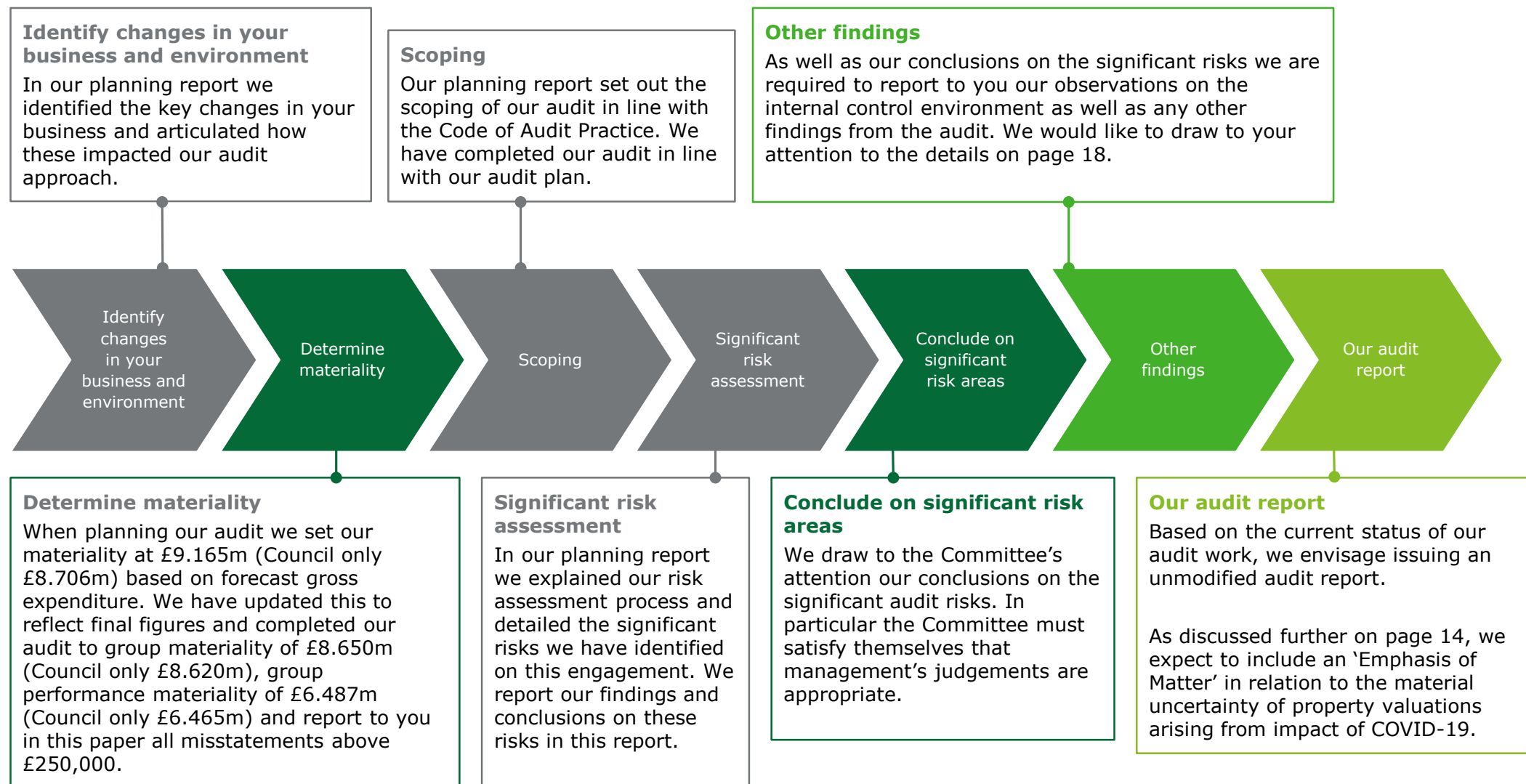


Mature









# Our audit explained

We tailor our audit to your business and your strategy



# Significant risks Dashboard

Risk	Material	Fraud risk	Planned approach to controls testing	Consistency of judgements with Deloitte's expectations	Comments	Slide no.
Recognition of grant income			D+I		Satisfactory	11
Management override of controls			D+I		Satisfactory	12

Overly prudent, likely to lead to future credit      Overly optimistic, likely to lead to future debit.

**D+I:** Testing of the design and implementation of key controls

# Significant risks (continued)

## Risk 1 - Recognition of grant income

### Risk identified

ISA 240 states that when identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such risks.

Key components of income for the Council are summarised in the table below. The General Revenue Grant and Non-Domestic Rates income which are directed by the Scottish Government and not considered a significant risk as the process for receipt of this income is not complex and can be verified 100% to third party evidence therefore there is little scope for manipulation. Similarly, the income from the IJB relates to services Commissioned from the Council and can be verified 100%. Council tax and housing rent income are set through the annual budget process with no management judgement and therefore have a low risk of fraud. Similarly, other Service Income includes fees and charges across all Services, which are set through formal approval processes, with no history of fraud or error. Finally, we perform detailed assurance work on housing benefits and therefore are satisfied that these amounts are not a significant risk area.

The significant risk is pinpointed to the recognition of grant income, comprising capital grants and contributions and service specific grants.

### Key judgements and our challenge of them



Grant income is a significant risk due to:

- management judgement in determining if there are any conditions attached to a grant and if so whether the conditions have been met; and
- complex accounting for grant income as the basis for revenue recognition in the accounts will depend on the scheme rules for each grant.

### Deloitte response



We have performed the following:

- assessed management's controls around recognition of grant income; and
- tested a sample of capital grants and grants credited to services to confirm these have been recognised in accordance with any conditions applicable and applicable accounting standards.

Type of income	2019/20 (£m)	Significant risk
<b><u>Taxation and Non-Specific Grant Income</u></b>		
Council tax income	57.0	
Non domestic rates	41.1	
General revenue grant	233.6	
<i>Capital Grants and Contributions</i>	39.1	✓
<b><u>Service Income</u></b>		
<i>Service Specific Grant Income</i>	31.7	✓
Housing Benefit Subsidy	41.9	
Housing Revenue Account	49.5	
IJB commission income	122.1	
Other Service Income	40.3	
<b>Total Service Income</b>	<b>285.5</b>	

### Deloitte view

We have concluded that grant income has been correctly recognised in accordance with the requirements of the Code of Practice on Local Authority Accounting.

# Significant risks (continued)

## Risk 2 - Management override of controls

### Risk identified

In accordance with ISA 240 (UK) management override is a significant risk. This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Council's controls for specific transactions.



### Deloitte response

We have considered the overall sensitivity of judgements made in preparation of the financial statements, and note that:

- the Council's results throughout the year were projecting underspends in the year. This was closely monitored with a good understanding of the reasons for the variances; and
- senior management's remuneration is not tied to particular financial results.

We have considered these factors and other potential sensitivities in evaluating the judgements made in the preparation of the financial statements.

### Significant and unusual transactions

We did not identify any significant transactions outside the normal course of business or any transactions where the business rationale was not clear.

### Journals

We have performed design and implementation testing of the controls in place for journal approval.

We have used Spotlight data analytics to risk assess journals and select items for detailed follow up testing. The journal entries were selected using computer-assisted profiling based on areas which we consider to be of increased interest.

We have tested the appropriateness of journal entries recorded in the general ledger, and other adjustments made in the preparation of financial reporting. No issues were noted.

### Accounting estimates and judgements (see next page)

We have performed design and implementation testing of the controls over key accounting estimates and judgements.

We reviewed accounting estimates for biases that could result in material misstatements due to fraud, as set out in the summary on the following page. We concluded that overall the changes to estimates in the period were balanced and did not indicate a bias to achieve a particular result.

We tested accounting estimates and judgements including the pension liability, valuation of property assets, and provisions focusing on the areas of greatest judgement and value. Our procedures included comparing amounts recorded or inputs to estimates to relevant supporting information from third party sources.

### Deloitte view

We have not identified any significant bias in the key judgements made by management based on work performed.

We have not identified any instances of management override of controls in relation to the specific transactions tested based on work performed to date.

# Significant risks (continued)

## Risk 2 - Management override of controls (continued)

### Key judgements

The key judgement in the financial statements are those which we have selected to be the significant audit risks around the recognition of grant income (page 11). While not considered to be significant audit risks, we have considered the assumptions used to calculate the pension liability (page 15), the valuation methodology for property valuations (page 14), and the recognition of expenditure (page 17). In the table below, we set out our challenge of the assumptions used in the determination of provisions. As part of our work on this risk, we reviewed and challenge management's key estimates and judgements including:

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Provisions	<p>The total provisions held within the Council's balance is immaterial, at £2.699m. This comprises provisions a number of individually immaterial provisions, including:</p> <ul style="list-style-type: none"> <li>• £0.885m in relation to estimated abnormal development costs in relation to Council House development sites.</li> <li>• £0.695m in relation to the Council's landfill site at Shewalton in Irvine.</li> <li>• £0.545m in relation to employee retiral commitments the Council had in place at 31 March 2020.</li> <li>• Other smaller provision in relation to equal pay, employee costs of paid absences, teachers maternity pay and potential liabilities to meet expenditure incurred in respect of the former Cunninghame District Council and Strathclyde Regional Council.</li> </ul>	<p>We examined the rationale for each provision, including a retrospective review of amounts provided in 2018/19. We have consulted with the Council's legal experts to confirm completeness of the provisions.</p> <p>In relation to the provision for equal pay, we have challenged the completeness of the provisions made through review and discussion with the Council's legal advisors and benchmarked with our industry knowledge.</p> <p>We concluded that the provisions made were reasonable.</p>

# Other areas of audit focus

## Property valuations

### Risk identified

The Council is required to hold property assets within Property, Plant and Equipment at a modern equivalent use valuation. The valuations are, by nature, significant estimates based on specialist and management assumptions and which can be subject to material changes in value. We did not identify this as a significant risk in our Audit Plan as our property specialists, Deloitte Real Estate, reviewed the methodology applied by the Council's valuer in previous years and concluded it was robust.

The Council has had an independent valuation carried out at 31 March 2020 for the purposes of the 2019/20 financial statements as part of its five-year rolling programme. The Council's also engaged the District Valuer to carry out a full valuation of HRA property assets during the year. The impact of COVID-19 has led to a material uncertainty being identified by the Council's property valuer regarding the valuation of properties. Although our overall assessment of the risk level regarding the Council's property valuation, has not increased to 'significant', we expect to include an 'Emphasis of Matter' in our Independent Audit Report.



### Key judgements

The valuation method has not changed from the prior year and is in line with International Financial Reporting Standards, with a full revaluation being carried out in line with previous years. The Council's revaluation has resulted in a net downward revaluation to property values of 9.008m.

Both the District Valuer and internal valuer identified a material uncertainty due to the impact of COVID-19 on individual markets, this is in line with RICS guidance published on 18 March 2020, as follows:

*"The outbreak of the Novel Coronavirus (COVID-19) declared by the World Health Organisation as a "Global Pandemic" on 11 March 2020, has impacted global financial markets. Travel restrictions have been implemented by many countries.*

*Market activity is being impacted in many sectors. As at the valuation date, we consider that we can attach less weight to previous market evidence for comparison purposes, to inform opinions of value. Indeed, the current response to COVID-19 means that we are faced with an unprecedented set of circumstances on which to base a judgement.*

*Our valuations are therefore reported on the basis of 'material valuation uncertainty' as per VPS3 and VPGA 10 of the RICS Red Book Global. Consequently, less certainty – and a higher degree of caution – should be attached to our valuation than would normally be the case. Given the unknown future impact that COVID-19 might have on the real estate market, we recommend that you keep the valuation of these properties under frequent review".*



### Deloitte response

- We have engaged our property specialists in relation to the impact of COVID-19 as well as reviewing the methodology and assumptions in the HRA valuation;
- We have assessed the presentation of revaluation movements and impairments, taking into account revaluation reserves for individual assets, and the disclosures included in the financial statements.
- We have reviewed both the District Valuer and internal valuer's reports and assessed managements disclosure of the key source of estimation uncertainty.
- We have assessed managements disclosure of the key source of estimation uncertainty.

### Deloitte view

Based on the audit evidence obtained, we are satisfied that the valuation of the Council's estate is appropriate. However, we expect to include an 'Emphasis of Matter' in our Independent Audit Report due to the material uncertainty identified by the valuers concerning valuations at 31 March 2020 due to the impact of COVID-19 on the property market.

This has been appropriately disclosed in the notes to the financial statements.

# Other areas of audit focus (continued)

## Defined benefits pension scheme

### Background

The Council participates in two defined benefits schemes:

- Scottish Teachers' Superannuation Scheme, administered by the Scottish Government; and
- The Strathclyde Pension Fund, administered by Glasgow City Council.

The net pension liability has decreased from £198.942m in 2018/19 to £122.116m in 2019/20. The decrease is as a result in changes in assumptions, specifically driven by reduced inflation assumptions, resulting in a reduction in the value of pension liabilities, partly offset by a reduction in the return on Scheme assets, resulting in the change in the value of the pension assets.

The Council's pension liability continues to be affected by the McCloud legal case in respect of potential discrimination in the implementation of transitional protections following changes in public sector pension schemes in 2015. Following recent consultation published by the SPPA, the actuary has amended its estimate of the impact of McCloud to only include members that were in service before 1 April 2012. This has resulted in a reduction of £6.701m to the liability disclosed in the draft accounts which has been updated in the final accounts. The actuary has made this adjustment to past service costs, but has not made any allowance within the current service costs for the impact of McCloud, therefore does not fully represent the cost of the benefits accruing for current service. The Council's actuary has estimated that the potential impact of this is an £561,000 understatement of the liability. This is an estimate and the actual cost could be different. This has also been updated for in the final accounts.

In the current year there was an additional legal case - the Goodwin judgement - that has an impact on the scheme. The judgement is in respect of a Teacher's Pension case where there was deemed to be discrimination in spousal transfer on death of the member (where a male widower was deemed to be discriminated against through receiving a different level of benefits than a female widow). The actuary has amended its estimates to take into account this case, which has resulted in an increase in liability of £0.778m to the liability disclosed in the draft accounts which have been updated in the final accounts.



### Deloitte response

- We assessed the independence and expertise of the actuary supporting the basis of reliance upon their work.
- We reviewed and challenged the assumptions made by Hymans Robertson, including benchmarking as shown the table below.
- We have requested assurance from the auditor of the pension fund over the controls for providing accurate data to the actuary.
- we assessed the reasonableness of the Council's share of the total assets of the scheme with the Pension Fund financial statements.
- we have reviewed and challenged the calculation of the impact of the McCloud and Goodwin cases on pension liabilities.
- we reviewed the disclosures within the accounts against the Code.

	Council	Comments
Discount rate (% p.a.)	2.3%	Prudent and reasonable
Retail Price Index (RPI) Inflation rate (% p.a.)	2.7%	Prudent end of reasonable range
Consumer Price Index (CPI) Inflation rate (% p.a.)	1.9%	Prudent end of reasonable range
Pension increase in payment (% p.a.)	1.9%	Reasonable
Pension increase in deferment (% p.a.)	1.9%	Reasonable
Salary increases	3%	Real salary increases 1.1% above CPI inflation
Mortality assumptions	Various	Prudent

### Deloitte view

Following receipt of the updated accounts to reflect the changes to the liability for both McCloud and Goodwin (net impact was a reduction in liability of £5.362m), we are satisfied that the net pension liability disclosed in the accounts is materially correct.



# Other areas of audit focus (continued)

## Expenditure recognition

### Risk identified

In accordance with Practice Note 10 (*Audit of financial statements of public sector bodies in the United Kingdom*), in addition to the presumed risk of fraud in revenue recognition set out in ISA (UK) 240, as discussed further on page 12, auditors of public sector bodies should also consider the risk of fraud and error on expenditure. This is on the basis that most public bodies are net spending bodies, therefore the risk of material misstatement due to fraud related to expenditure may be greater than the risk of material misstatement due to fraud related to revenue recognition.

We have considered this risk for the Council and concluded that we are satisfied that the control environment is strong and there is no history of errors or audit adjustments. This was therefore not been assessed as a significant risk area, but continued to be an area of audit focus.



### Deloitte response

We performed the following procedures to address the above risk:

- A review of the number and median value of invoices processed in the year. As illustrated in table opposite, based on the medium amount, the Council would need to omit over 37,361 invoices at year-end to result in a material error. We noted that in the month following the year-end, a total of 8,216 invoices were processed. We therefore concluded that a risk of material misstatement was remote.
- An analytical review to test the completeness and accuracy of year-end creditor balances was carried out. We are satisfied that the amount recorded is reasonable.

	Invoice Analysis
Median invoice amount	£230.72
Average number of invoices processed per month	4,834
Number of invoices that would need to be unrecorded to cause a material misstatement	37,361
Total invoices processed in April 2020 (one month after year-end)	8,216 (total value £33.3m)

### Deloitte view

We have concluded that expenditure has been correctly recognised in accordance with the requirements of the Code of Practice on Local Authority Accounting.

# Other areas of audit focus (continued)

## Charitable trusts

### Risk identified

From 2013/14, all Scottish Councils who act as sole trustees for any registered charities have to fully comply with the Charities Accounts Regulations. This requires Charities SORP compliant accounts to be prepared for each charity, and a separate audit of each. North Ayrshire Council administers eight such registered charities, disclosed in a single set of annual accounts. This is in accordance with the connected charities rules.

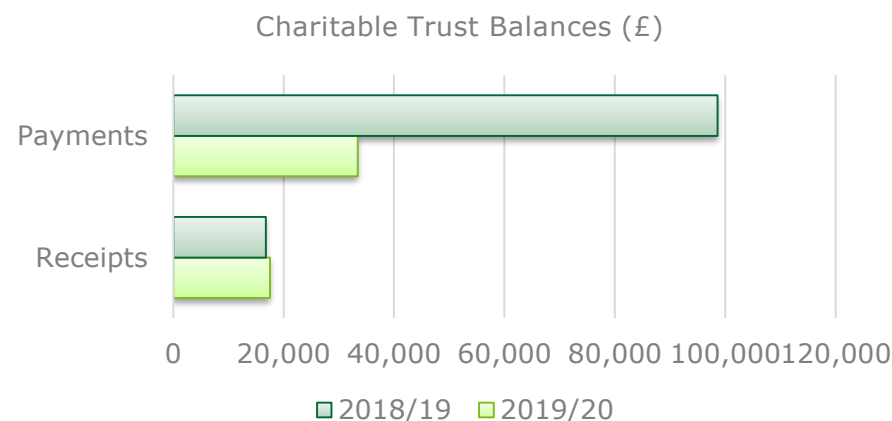
As the gross income of each of the Trusts is less than £100,000, the Council has opted to prepare the charitable trust accounts on a receipts and payments basis in accordance with The Charities Accounts (Scotland) Regulation 2006. Fully compliant Charities SORP accounts are therefore not required and disclosure is limited to that specified in the Regulations.



### Deloitte response

We have assessed that the Statement of Receipts and Payments and the Statement of Balances to ensure these have been prepared in accordance with the Charities Accounts (Scotland) Regulations 2006.

A summary is provided in the table adjacent. From an initial review of draft annual accounts we note that there has been a large movement in payments which have dropped from £98k in 2018/19 to £33k in 2019/20. The biggest decline was reported in payments for Kilwinning Trust which dropped by £61k (78%) as a result of Council's policy in prior year to encourage the utilisation of funds in support of suitable projects within the relevant communities.




### Deloitte view

Our testing of the charitable trusts is complete and no issues noted. We anticipate issuing an unmodified opinion.

# Other significant findings

## Internal control and risk management

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

Area	Observation	Priority
IT Systems	During the IT review of Council’s system there were two control deficiencies identified by IT specialists which have been communicated to the management. Management have considered these and confirmed that compensating controls are in place to mitigate the risk associated with these deficiencies. There has been no impact on the audit from these deficiencies as no control reliance is placed on IT controls during our audit.	

The purpose of the audit was for us to express an opinion on the financial statements. The audit included consideration of internal control relevant to the preparation of the financial statements 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 internal control. The matters being reported are limited to those deficiencies that we have identified during the audit and that we have concluded are of sufficient importance to merit being reported to you.

Low Priority

Medium Priority

High Priority

# Other significant findings (continued)

## Financial reporting findings

Below are the findings from our audit surrounding your financial reporting process.

### Qualitative aspects of your accounting practices:

The Council's accounts have been prepared in accordance with the Local Authority Code of Practice (the Code). The accounting policies adopted are in line with the Code.

We identified areas some areas where disclosures could be improved in line with accounting standards and best practice which management have agreed to change in the final accounts.

### Significant matters discussed with management:

Significant matters discussed with management related primarily to the impact of COVID-19 on the organisation, including the impact of the material valuation uncertainty on PPE valuations.

### Other matters relevant to financial reporting:

We have not identified other matters arising from the audit that, in the auditor's professional judgement, are significant to the oversight of the financial reporting process.

We received an objection to the Council's accounts in accordance with section 101 of the Local Government (Scotland) Act 1973 in relation to the Common Good and Trust Funds. We have provided an initial response and currently considering the detail. Any significant matters arising will be reported to the Audit and Scrutiny Committee prior to the approval of the accounts.

We will obtain written representations from the Council on matters material to the financial statements when other sufficient appropriate audit evidence cannot reasonably be expected to exist. A copy of the draft representations letter has been circulated separately.

# Coronavirus (Covid-19) outbreak

## Impact on the annual report and audit

The current crisis is unprecedented in recent times. The NHS and care sector is most directly exposed to the practical challenges and tragedies of the pandemic, and is undergoing major, rapid operational changes in response.

The uncertainties and changes to ways of working also impact upon the reporting and audit processes, and present new issues and judgements that management and the Committee need to consider. CIPFA has issued guidance relating to the impacts on the annual report to assist in making relevant disclosures. We summarise below the key impacts on reporting and audit:

Impact on Council annual report and financial statements	Impact on our audit
<p>The Council need to consider the impact of the outbreak on the annual report and financial statements including:</p> <ul style="list-style-type: none"><li>• Principal risk disclosures</li><li>• Change in the funding regime for 20/21</li><li>• Property valuation material uncertainty</li><li>• Impairment of non-current assets</li><li>• Allowance for expected credit losses</li><li>• Fair value measurements based on unobservable inputs</li><li>• Onerous contracts and any potential provisions</li><li>• Going concern</li><li>• Events after the end of the reporting period</li></ul>	<p>COVID-19 has fundamentally changed the way we have conducted our audit this year including:</p> <ul style="list-style-type: none"><li>• Teams are primarily working remotely with some challenges in accessing 'physical' documentation and with availability of some Council staff.</li><li>• The teams have had regular status updates to discuss progress and facilitate the flow of information.</li><li>• Consideration of impacts on the areas of the financial statements and annual report listed has been included as part of our audit work in the current year and comments have been included where appropriate within this report.</li><li>• In conjunction with the Council staff, we will continue to consider any developments for potential impact up to the finalisation of our work in September 2020.</li></ul>

# Our audit report

## Other matters relating to the form and content of our report

Here we discuss how the results of the audit impact on other significant sections of our audit report.



### **Our opinion on the financial statements**

Our opinion on the financial statements is expected to be unmodified.



### **Material uncertainty related to going concern**

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

While the Council is faced with financial sustainability issues (as discussed on page 5), it achieved a balanced budget in 2019/20 and has agreed a balance budget for 2020/21. There is also a general assumption set out in Practice Note 10 (Audit of financial statements of public sector bodies in the United Kingdom) that public bodies will continue in operation, therefore it is appropriate to continue as a going concern.



### **Emphasis of matter and other matter paragraphs**

As discussed on page 14, we expect to include an 'Emphasis of Matter' paragraph within our audit report in relation to the material uncertainty associated with the property valuations.

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



### **Other reporting responsibilities**

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

Our opinion on matters prescribed by the Controller of Audit are discussed further on page 22.

# Your annual report

We are required to provide an opinion on the auditable parts of the remuneration and staff report, the annual governance statement and whether the management commentaries are consistent with the disclosures in the accounts.

	Requirement	Deloitte response
Management Commentary	The management commentary comments on financial performance, strategy and performance review and targets. The commentary included both financial and non-financial KPIs and made good use of graphs and diagrams. The Council also focusses on the strategic planning context.	<p>We have assessed whether the management commentary has been prepared in accordance with the statutory guidance.</p> <p>We have also read the management commentary and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading.</p> <p>Following minor amendments made during the course of the audits, we are satisfied that the management commentary has been prepared in accordance with guidance, is consistent with our knowledge and is not otherwise misleading.</p> <p>The Council has continued to look for ways to improve the quality of management commentary including the use of graphics and charts. There is also good linkage of performance to national outcomes in line with best practice.</p>
Remuneration Report	The remuneration report has been prepared in accordance with the 2014 Regulations, disclosing the remuneration and pension benefits of Senior councillors and Senior Employees of the council.	<p>We have audited the disclosures of remuneration and pension benefits, pay bands, and exit packages.</p> <p>We can confirm that auditable parts of Remuneration report have been properly prepared in accordance with the regulations.</p>
Annual Governance Statement	The Annual Governance Statement reports that the Council governance arrangements provide assurance, are adequate and are operating effectively.	We have assessed whether the information given in the Annual Governance Statement is consistent with the financial statements and has been prepared in accordance with the accounts regulations.



# Appendices



# Purpose of our report and responsibility statement

## Our report is designed to help you meet your governance duties

### What we report

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

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

### The scope of our work

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

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

### Use of this report

This report has been prepared for the Audit and Scrutiny Committee and the Council, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose.

### What we don't report

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

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

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

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



**Pat Kenny, CPFA**

**For and on behalf of Deloitte LLP**

Glasgow | 14 September 2020

# Action plan

## Follow-up 2018/19 action plan

We have followed up the recommendations made in our 2018/19 annual report in relation to the wider scope areas and are pleased to note that one of the recommendations made have been fully implemented with the IFRS 16 point delayed due to the HM Treasury deferring the impact of this for another year.

Area	Recommendation	Management Response	Responsible person	Target Date	Priority	2019/20 Update
<i>Financial Statements – IFRS 16 Leases</i>	We recommend the Council targets completion of its IFRS 16 impact analysis during 2019/20, and to calculate an adjusted opening balance sheet position for audit following the 31 March 2020 audit. We recommend early consideration following the impact analysis of actions required to embed IFRS 16 accounting in the Council's underlying accounting systems(see page 16).	Work is ongoing to determine the full impact of the changes in accounting requirements and embed these requirements within the Council's accounting procedures.	Head of Financial and Customer Services	31 March 2020	Medium	<p><b>Partially implemented:</b></p> <p><b>Updated management response:</b> During 2019/20 the Council identified and reviewed all current leases across the Council. Management will determine the full impact and prepare a revised opening balance sheet in the 2020/21 Accounts following the delay of IFRS16 as a result of COVID-19.</p> <p><b>Updated target date:</b> 31 March 2021</p>
<i>Financial Statements – Bank Reconciliations</i>	The Council should put in place a formal procedure for investigating reconciling items to ensure that they are valid and followed up on a timely basis with appropriate action taken where necessary (see page 16).	An internal process has been implemented to investigate all outstanding bank items on a monthly basis and hold regular meetings cross service to address all reconciling items and ensure corrective action is taken.	Head of Financial and Customer Services	31 March 2020	Low	<p><b>Fully implemented</b> – reconciling items relates to 2019/20.</p>

# Our other responsibilities explained

## Fraud responsibilities and representations



### Responsibilities:

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



### Required representations:

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

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



### Audit work performed:

In our planning we identified the risk of fraud in the recognition of grant income and management override of controls as a key audit risk for your organisation.

During course of our audit, we have had discussions with management and those charged with governance.

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

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

### Concerns:

No concerns have been identified regarding fraud.



# Independence and fees



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

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Council and will reconfirm our independence and objectivity to the Audit and Scrutiny Committee for the year ending 31 March 2020 in our final report to the Audit and Scrutiny Committee.	
Fees	The audit fee for 2019/20, in line with the fee range provided by Audit Scotland, is £302,520 as analysed below:	
		£
	Auditor remuneration	184,610
	Audit Scotland fixed charges:	
	Pooled costs	18,060
	Performance Audit and Best Value	88,690
	Audit support costs	11,160
	<b>Total proposed fee</b>	<b>302,520</b>
	In addition, the audit fee for the charitable trusts audit is £1,200.	
	There are no non-audit services fees proposed for the period.	
Non-audit services	In our opinion there are no inconsistencies between the FRC's Ethical Standard and the Council's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.	
Relationships	We are required to provide written details of all relationships (including the provision of non-audit services) between us and the organisation, its board and senior management and its affiliates, including all services provided by us and the DTTL network to the audited entity, its board and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence.	
	We are not aware of any relationships which are required to be disclosed.	



# Quality of public audit in Scotland

## Annual report 2018/19

Audit Scotland published its annual assessment of audit quality carried out on the audit work delivered by Audit Scotland and appointed firms. A copy of the full report is available: <https://www.audit-scotland.gov.uk/report/quality-of-public-audit-in-scotland-annual-report-201819>

### Public audit in Scotland

Recent high-profile corporate collapses in the private sector have led to considerable scrutiny of the audit profession. The Brydon review is looking into the quality and effectiveness of the UK audit market. The Kingman review, the Competition and Markets Authority market study of the audit services market and the Business, Energy and Industrial Strategy Committee's report on the Future of Audit have all reported on structural weaknesses in the private sector audit regime. The reviews are placing a strong focus on the need for independence of auditors from the bodies they audit.

The public audit model in Scotland is fundamentally different to the private sector audit regime and is well placed to meet the challenges arising from the reviews of the auditing profession. Public audit in Scotland already operates many of the proposed features to reduce threats to auditor independence including:

- independent appointment of auditors by the Auditor General for Scotland and Accounts Commission
- rotation of auditors every five years
- independent fee-setting arrangements and limits on non-audit services
- a comprehensive Audit Quality Framework.

The Audit Scotland Audit Quality and Appointments (AQA) team will continue to develop its activities to provide the Auditor General for Scotland and Accounts Commission with assurance about audit quality. The Audit Quality Framework will be refreshed to take account of the findings from the first two years of its application and to reflect on the developments in the wider audit environment. Further development is planned over the following year to include:

- enhancing stakeholder feedback
- reviewing the structure and transparency of audit quality reporting.

### Key messages

The programme of work carried out under the Audit Quality Framework provides evidence of compliance with auditing standards and the Code of audit practice (the Code), together with good levels of qualitative performance and some scope for improvements in audit work delivered in the period 1 April 2018 to 31 March 2019.

Independent external reviews of audit quality carried out by The Institute of Chartered Accountants of Scotland (ICAS) show evidence of compliance with expected standards:

- ICAS did not identify any concerns with audit opinions
- 55 per cent of financial audit files reviewed by ICAS over the last two years were graded as limited improvement required, the remaining reviews were graded as improvement required (*100% of Deloitte files – limited improvement*)
- ICAS noted considerable improvements in the documentation of performance audits and Best Value assurance reports.

Other performance measures showing good performance include:

- 78 per cent of internal reviews of financial audits in the last two years required only limited improvements (*100% of Deloitte internal reviews graded as no improvement required*)
- all audit providers have a strong culture of support for performing high-quality audit
- stakeholder feedback shows audit work has had impact
- non-audit services (NAS) are declining in number and value and requests made complied with the Auditor General for Scotland and Accounts Commission's NAS policy.

AQA monitors progress against areas for improvement. A common area for improvement in the last two years has been the need for better documentation of audit evidence. In 2018/19 further areas for improvement were identified in:

- the use of analytical procedures
- the application of sampling.



Deloitte LLP does not accept any liability for use of or reliance on the contents of this document by any person save by the intended recipient(s) to the extent agreed in a Deloitte LLP engagement contract.

If this document contains details of an arrangement that could result in a tax or National Insurance saving, no such conditions of confidentiality apply to the details of that arrangement (for example, for the purpose of discussion with tax authorities).

Deloitte LLP is a limited liability partnership registered in England and Wales with registered number OC303675 and its registered office at 1 New Street Square, London, EC4A 3HQ, United Kingdom.

Deloitte LLP is the United Kingdom affiliate of Deloitte NSE LLP, a member firm of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"). DTTL and each of its member firms are legally separate and independent entities. DTTL and Deloitte NSE LLP do not provide services to clients. Please see [www.deloitte.com/about](http://www.deloitte.com/about) to learn more about our global network of member firms.

© 2020 Deloitte LLP. All rights reserved.