



Midlothian Council

**Annual Audit Plan
Year ending 31 March 2021**



Contents

Section	Auditor Responsibility	Page
Executive Summary	Summarise the purpose and key information for the 2020/21 audit	03
Local Government developments	Provide a summary of the overall local government environment	06
Financial Statements and Accounting	Summary of audit approach, materiality, risks etc.	09
Wider Scope Audit Risks	Audit approach for reviewing the Council's compliance with the wider public audit scope areas: <ul style="list-style-type: none">▶ financial position and arrangements for securing financial sustainability▶ suitability and effectiveness of corporate governance arrangements▶ effectiveness of performance management arrangements in driving economy, efficiency and effectiveness in the use of public money and assets	20
Appendices	Undertake statutory duties, and comply with professional engagement and ethical standards: Appendix A: Code of Audit Practice: responsibilities Appendix B: Auditor Independence Appendix C: Best Value Programme of Coverage Appendix D: Required communications with the audit committee Appendix E: Timing and deliverables Appendix F: Audit fees Appendix G: Additional audit information	24

About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of Midlothian Council (the Council) for financial years 2016/17 to 2020/21. As a result of the impact of Covid-19 our appointment was extended by a further 12 months to include the financial year 2021/22. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

This report is for the benefit of the Council and is made available to the Accounts Commission, the Controller of Audit and Audit Scotland (together the Recipients). This report has not been designed to be of benefit to anyone except the Recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

Complaints

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 Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. 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, or with how your complaint has been handled, you can refer the matter to Diane McGiffen, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

1

Executive summary

Our key contacts:

Stephen Reid
Partner
sreid2@uk.ey.com

Grace Scanlin
Senior Manager
grace.scanlin@uk.ey.com

Our independence:

We confirm that we have undertaken client and engagement continuance procedures, which include our assessment of our continuing independence to act as your external auditor.

Purpose of our plan

The Accounts Commission appointed EY as the external auditor of Midlothian Council (“the Council”) for the five year period to 2020/21. As a result of the impact of Covid-19 our appointment was extended by a further 12 months to include the financial year 2021/22.

This Annual Audit Plan, prepared for the benefit of Council management and the Audit Committee, sets out our proposed audit approach for the audit of the financial year ending 31 March 2021, the fifth year of our appointment. In preparing this plan, we have updated our understanding of the Council through planning discussions with management, review of relevant documentation and committee reports, and our general understanding of the environment in which the Council is currently operating.

A key objective of our audit reporting is to add value by supporting the improvement of the use of public money. We aim to achieve this through sharing our insights from our audit work, our observations around where the Council employs best practice and where processes can be improved. We use these insights to form our audit recommendations to support the Council in improving its practices around financial management and control, as well as around key aspects of the wider scope dimensions of audit. These are highlighted throughout our reporting together with our judgements and conclusions regarding arrangements.

We are mindful that as a result of the pandemic, planning guidance from Audit Scotland or additional risks arising, may change the areas of audit focus for 2020/21. Any material changes to this plan will be reported to the Audit Committee. After consideration by the Council’s Audit Committee, the finalised plan will be provided to Audit Scotland and published on their website.

Scope and Responsibilities

We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; International Standards on Auditing (UK); relevant legislation; and other guidance issued by Audit Scotland. The Code sets out the responsibilities of both the Council and the auditor, more details of which are provided in Appendix A.

Financial statement audit

We are responsible for conducting an audit of the Council's financial statements. We provide an opinion as to:

- ▶ whether they give a true and fair view in accordance with applicable law and the 2020/21 Code of the state of affairs of the Council and its group as at 31 March 2021, and of the income and expenditure of the Council and its group for the year then ended;
- ▶ whether they have been properly prepared in accordance with the IFRSs, as interpreted and adapted by the 2020/21 Code; and
- ▶ whether they have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

We also review and report on the consistency of the other information prepared and published along with the financial statements.

Materiality

Materiality levels have been set at the planning stage of the audit as follows:

Planning Materiality	Tolerable Error	Nominal amount
£6.8 million	£ 5.1 million	£250,000
2% of the Council's gross expenditure	Materiality at an individual account level	Level that we will report to committee

Based on considerations around the expectations of financial statement users and qualitative factors, we apply a lower materiality level to the audited section of the Remuneration Report. We also apply professional judgement to consider the materiality of Related Party Transactions to both parties.

Wider Scope audit

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on the four dimensions of wider-scope public audit, as well as an assessment around the Council's arrangements for securing Best Value. The Code requires auditors to provide judgements and conclusions on the four dimensions of wider scope public audit:

- ▶ Financial management;
- ▶ Financial sustainability;
- ▶ Governance and transparency; and
- ▶ Value for money

Our audit work over the wider scope audit dimensions complements our financial statements audit. We have updated our understanding of the risks impacting the Council through discussions with management, review of relevant committee reports, and our knowledge of the local government environment.

Audit Risk Dashboard

Key Financial Statement Risks

<p>Significant Risk: Risk of fraud in revenue and expenditure recognition</p>	<p>Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. During 2020/21, we will consider the impact of additional Covid-19 grant income streams that the Council has managed to support the response to the pandemic, including those administered by the City of Edinburgh on the Council's behalf.</p>
<p>Fraud Risk: Misstatement due to fraud or error</p>	<p>As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud due to the ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively.</p>
<p>Inherent risk: Valuation of property, plant and equipment</p>	<p>The fair value of property, plant and equipment (PPE) represent significant balances in the Council's financial statements. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.</p>
<p>Valuation of pension assets and liabilities</p>	<p>Accounting for the Local Government Pension Scheme involves significant estimation and judgement and management engages an actuary to undertake the calculations on their behalf. The Lothian Pension Fund triennial valuation was completed as at 31 March and will therefore inform the valuation as at 31 March 2021. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts, the assumptions underlying fair value estimates, and the valuation of the Council's share of scheme assets and liabilities at the year end.</p>

Wider Scope Risks

<p>Financial Sustainability: Impact of the pandemic on medium term financial planning</p>	<p>As in previous years, the Council was unable to fully achieve its savings target in 2019/20, and the impact of the global pandemic means that planned savings could not be delivered in 2020/21 as the Council focused on responding to the pandemic. The Council estimates that the net impact of the pandemic is a cost of £2.26 million, resulting in a projected general reserve balance of £3.5 million, only marginally above the Council's minimum reserves level.</p>
<p>Financial Management: Treasury Management</p>	<p>Treasury Management and the application of the Prudential Code are areas of increased focus in local government. In 2020, members of the Audit Committee raised specific concerns which has led to our consideration of treasury management as an area of increased focus as part of our wider scope audit procedures in 2020/21.</p>

Local Government developments

Introduction

In accordance with the principles of the Code, our audit work considers key developments in the sector. We obtain an understanding of the strategic environment in which the Council operates to inform our audit approach.

Scrutiny

The LAN is content that no additional scrutiny requirements are necessary in 2021/22.

A National Scrutiny Plan (NSP) was most recently published by the Accounts Commission (on behalf of the Strategic Scrutiny Group) in September 2019. The NSP summarises all planned and announced strategic scrutiny activity from September 2019 in each of Scotland's 32 councils. The plan was based on a shared risk assessment undertaken by a local area network (LAN), comprising representatives of all the scrutiny bodies who engage with the various councils.

As the appointed auditor of the Council, we act as the LAN lead for Midlothian Council shared risk assessment process. The LAN met on 1 March 2021 to discuss the 2021/22 shared risk assessment. The LAN concluded that no additional scrutiny requirements were identified and that no local scrutiny plan would be published.

Political uncertainty

Continuing uncertainty exists around a number of factors in the foreseeable future including:

- ▶ **Covid-19 Pandemic:** : the impact of the pandemic has dominated the political environment for the last financial year and will, in all likelihood, continue to do so throughout 2021.
- ▶ **EU withdrawal:** the UK formally exited the EU on 31 January 2020, following a transition period until 31 December 2020, its relationship with the EU is now fully under new arrangements.
- ▶ **Scottish Parliament Elections:** Scottish elections are due to be held on 6 May 2021.
- ▶ **Scottish Local Government Elections:** Due to be held in May 2022
- ▶ **Scotland Independence Referendum:** there is continued uncertainty regarding whether a Scottish independence referendum will be held.

We will continue to monitor how the Council prepares for, and responds to, the implications of political factors throughout the audit year.

Accounts Commission Overview

The Accounts Commission (“the Commission”) published their Local Government in Scotland: Financial overview 2019/20 report in January 2021. This report provides an overview of the financial performance of councils in 2019/20.

Key messages highlighted by this report included:

- ▶ There was an increase in Scottish Government funding for the sector of £0.5 billion, with nearly half of the increase intended to fund the expansion in early learning and childcare.
- ▶ Funding in 2019/20 improved relative to other areas of the Scottish budget but a historic difference continues to exist, meaning that reductions over the last seven years are larger than in other areas of the Scottish Government budget.
- ▶ The financial cost of Covid-19 to local government in Scotland in 2020/21 is estimated to be £767 million, with just over half due to lost income.

The report also drew attention to two councils (Fife and Aberdeenshire) now being at risk of running down their general fund balance within four to five years if their current trend of use of reserves continues.

Fiscal flexibilities

A package of financial flexibilities has been developed, with conclusion expected soon, between the Scottish Government and the Convention of Scottish Local Authorities to address the funding pressures faced by local government due to Covid-19.

The flexibilities are intended to be available in 2020/21 and/or 2021/22, and include the use of capital receipts to meet the costs of the pandemic. Additionally, there is continued work to seek to provide the ability to charge depreciation for leases and service concession arrangements to the General Fund over the life of relevant assets, rather than over the contract period and deferment of loans funds repayments. We will consider the Council's assessment and use of flexibilities as part of our wider scope work on Financial Sustainability.

Budget setting process 2021/22

The Scottish Budget for 2021/22 was published on 28 January 2021. This announcement focused on key priorities, including the response to the global pandemic.

Due to delays in the Scottish Budget announcement, many councils delayed agreeing their 2021/22 budget. Midlothian Council met to agree its budget on 23 February 2021. The Council agreed to freeze council tax levels, along with fees and charges, to recognise the unique pressures created by the pandemic and to help protect household incomes. A planned rent increase was delayed for the same reasons. The Council has also agreed a significant capital programme to help support the area's economic recovery and which reflects the level of infrastructure investment needed to meet the needs of rapid population growth. We will consider the Council's approach to budget setting as part of our wider scope work on Financial Management.

Financial statements: Our approach and significant risks identified

Introduction to section

The Council's Annual Accounts enables the Council to demonstrate accountability for, and its performance in the use of its resources. They are prepared in accordance with proper accounting practice, which is represented by the 2020/21 Code of Practice on Local Authority Accounting in the United Kingdom.

Audit Opinion

We are responsible for conducting an audit of the financial statements of the Council. We will provide an opinion on the financial statements as to:

- ▶ whether they give a true and fair view in accordance with applicable law and the 2020/21 Code of the state of affairs of the Council and its group as at 31 March 2021, and of the income and expenditure of the Council and its group for the year then ended;
- ▶ whether they have been properly prepared in accordance with the IFRSs as adopted by the European Union, as interpreted and adapted by the 2020/21 Code. Note that public bodies will continue to use EU-adopted IFRS for 2020/21 and will move to UK-adopted IFRS in 2021/22; and
- ▶ whether they have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

We also review and report on the consistency of the other information prepared and published by the Council along with its financial statements. We noted that the management commentary and narrative reporting significantly improved in 2019/20 and we will therefore continue to support the Council to improve and refine disclosures, where required.

Audit Approach

We determine which accounts, disclosures and relevant assertions could contain risks of material misstatement. Our audit involves:

- ▶ Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud, error or design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
- ▶ Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Council's internal control.
- ▶ Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Concluding on the appropriateness of management's use of the going concern basis of accounting.
- ▶ Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Council to express an opinion on the consolidated financial statements.
- ▶ Reading other information contained in the financial statements, including that the annual report is fair, balanced and understandable, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements.
- ▶ Maintaining auditor independence.
- ▶ Substantive tests of detail of transactions and amounts. For 2020/21 we plan to follow a predominantly substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

Materiality

For the purposes of determining whether the financial statements are free from material error, in accordance with ISA (UK) 320 we define materiality as the magnitude of an omission or misstatement that, individually or in aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements.

Materiality Level

Rationale

<p>Planning Materiality £6.8 million</p>	<p>Planning materiality (PM) - the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.</p> <p>For planning purposes, materiality for 2020/21 has been set at £6.8 million (2019/20: £6.8 million). This represents 2% of the Council's prior year gross expenditure on provision of services, excluding IJB gross-up of income and expenditure. We have derived this figure following our assessment of risk factors impacting the Council in 2020/21.</p>
<p>Tolerable Error £5.1 million</p>	<p>Tolerable error (TE) - materiality at an individual account balance, which is set so as to reduce to an acceptably low level that the aggregate of uncorrected and undetected misstatements exceeds PM. We have set it at £5.1 million (2018/19: £3.4 million) which represents 75% of planning materiality. This level reflects our prior year audit experience in the preparation of the 2019/20 financial statements.</p>
<p>Summary of Audit Differences £250,000</p>	<p>Summary of Audit Differences (SAD) Nominal amount - the amount below which misstatements whether individually or accumulated with other misstatements, would not have a material effect on the financial statements.</p>

Our evaluation requires professional judgement and so takes into account qualitative as well as quantitative considerations implied in the definition. Factors which we consider include the perspectives and expectations of users of the financial statements as well as our risk assessment as to the likelihood of material misstatements arising in the financial statements.

The amount we consider material at the end of the audit may differ from our initial determination. At the end of the audit we will form, and report to you, our final opinion by reference to all matters that could be significant to users of the financial statements, including the total effect of any audit misstatements, and our evaluation of materiality at that date.

We consider all accounts and disclosures within the financial statements individually to ensure an appropriate materiality is used. In determining their materiality, we consider both the quantitative and qualitative factors that could drive materiality for the users of the financial statements. Accordingly we determine it is appropriate to use lower levels of materiality for some areas of the financial statements, including:

- ▶ Remuneration report - given the sensitivity around the disclosure of senior staff remuneration we apply a lower materiality threshold to our audit consideration around the remuneration report and related disclosures.
- ▶ Related party transactions - which are considered material when they are material to either party in the transaction. We do not apply a specific materiality but consider each transaction individually.

Covid-19 Pandemic - Impact on Financial Statements

We outlined in our reporting in 2019/20 how the impact of Covid-19 has changed expectations about required disclosures in the financial statements.

- ▶ In line with 2019/20, the governance statement should capture how the control environment has changed during the period of the pandemic, and steps being taken by the Council to maintain a robust control environment during the disruption. This includes consideration of how key governance functions are continuing to operate, such as key committee meetings and the delivery of internal audit's programme of work.
- ▶ The Council's management commentary should clearly summarise the performance of the Council in the year, including the impact of Covid-19 on both its financial performance and future planning, and its impact of key statutory performance indicators.
- ▶ Significant events after the balance sheet date require to be disclosed within the financial statements, either through the post balance sheet events note or in specific accounting notes or the management commentary and governance statement, as appropriate. The detail required in the disclosures will reflect the specific circumstances of the Council.

Accounting policies

While the impact of Covid-19 has been felt for almost a year now, 2020/21 is the first financial year where the full impact on day to day accounting transactions will be seen in the financial statements. Covid-19 will continue to have a potentially material impact on the financial statements, including how the Council accounts for significant income and expenditure. Any specific government support may qualify as a new transaction stream and require development of new accounting policies.

Impact on Audit Process

The deadline for audits has not yet been set, reflecting the ongoing and severe impact that the pandemic has had on both Council finance teams and audit timescales.

Following the impact of Covid-19 on the financial statement preparation and audit process in 2020, Audit Scotland has provisionally set its reporting deadline for local government bodies at 31 October 2021, a month later than the traditional timeframe but earlier than the 2020 revised deadlines. These deadlines will continue to be reviewed through the year as circumstances change, however the FRC and Audit Scotland have made clear that any deadlines are secondary to the primacy of audit quality and ensuring completeness of work regardless of the environment in which audit takes place.

We have outlined the planned timing for the key deliverables of the audit process in Appendix E. These reflect initial discussions with management and the agreed intention to maintain planned reporting dates in line with previous timeframes. We will continue to work closely with management to review timeframes and logistics for the completion of the audit in 2020/21.

We will aim to take a pragmatic and flexible approach in the current environment, while also recognising that strong financial management and good governance are more important than ever at this time.

Significant Risks

We set out below the significant risks identified for 2020/21, along with the rationale and expected audit approach. The risks identified may change to reflect any significant findings or subsequent issues we identify during the audit.

1. Risk of fraud in expenditure recognition, including through management override of control

Under ISA 240 there is a presumed risk that income may be misstated due to improper recognition of income. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which means we also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

Significant risks identified in the audit relate to the risk of fraud in income and expenditure recognition. We also perform procedures in all audits to respond to the risk of misstatement due to fraud or error caused by management override of controls. We will report our findings in these areas within our 2020/21 Annual Audit Report.

We consider there to be a specific risk around income and expenditure recognition through:

- ▶ Incorrect income and expenditure cut-off recognition to alter the Council's financial position around the financial year end.
- ▶ Incorrect recognition applied to grant income with performance conditions.
- ▶ Incorrect capitalisation of revenue expenditure.

In line with auditing standards, we rebut the risk around income and expenditure where appropriate depending on the nature of the account.

Accordingly, we have rebutted the risk of improper recognition of income in respect of core grant funding from the Scottish Government, as well as in respect of council tax and non-domestic rate income. With regards to expenditure we have rebutted the risk of improper recognition of

Work we will perform:

- ▶ Identifying fraud risks during the planning stages.
- ▶ Inquiry of management about risks of fraud and the controls put in place to address those risks.
- ▶ Understanding the oversight given by those charged with governance of management's processes over fraud and consideration of the effectiveness of controls designed to address the risk of fraud.
- ▶ Determining an appropriate strategy to address those identified risks of fraud.
- ▶ Review and challenge management on any accounting estimates on income or expenditure recognition for evidence of bias.
- ▶ Review Covid-19 related income streams; challenge the judgements of whether to account for schemes as 'agent' or 'principal' and whether income recognition criteria are satisfied.
- ▶ Focused and extended substantive testing of related income and expenditure transactions where we have identified a significant risk.
- ▶ Testing of income and expenditure cut-off treatment around the year end.
- ▶ Review a sample of expenditure transactions recorded in the ledger and payments made from bank accounts post year-end and confirm that the associated expenditure has been recorded in the correct period.
- ▶ Assess and challenge manual adjustments / journal entries by management around the year end for evidence of management bias and evaluation of business rationale and supporting evidence.
- ▶ Develop a testing strategy to test material revenue and expenditure streams, including testing revenue and capital expenditure to ensure it has been correctly classified.

2. Misstatement due to 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.

In prior years we identified some audit adjustments which were material to the financial statements in relation to the Council's areas of estimate and judgement. These include the accounting for the Council's property, plant and equipment balances. The nature of the adjustments means we did not identify a specific attempt to alter the financial position of the Council, and through our planning procedures we have not identified a specific account where the risk of management override is higher than generally throughout the financial statements.

Work we will perform:

- ▶ Identifying fraud risks during the planning stages.
- ▶ Inquiry of management about risks of fraud and the controls put in place to address those risks.
- ▶ Understanding the oversight given by those charged with governance of management's processes over fraud.
- ▶ Consideration of the effectiveness of management's controls designed to address the risk of fraud, including any controls in place to manage the awarding of Covid-19 related grants and reliefs.
- ▶ Determining an appropriate strategy to address those identified risks of fraud.
- ▶ Performing mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments in the preparation of the financial statements.
- ▶ Specific focus on the accounting for any identified key areas of judgement and estimates in the financial statements.

Other areas of focus: Inherent risks

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures and therefore may be key audit matters we will include in our audit report.

1. Valuation of Property, Plant and Equipment

The fair value of PPE represents a significant balance in the Council's financial statements (2019/20 PPE totalled £891 million) and is subject to valuation changes, impairment reviews and depreciation charges.

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

In previous years we identified errors in the Council's valuations. While we noted continued improvement in 2019/20, we noted that this continues to be an area of disproportionate audit effort.

During 2020/21, the Council's valuers will review the primary education school estate. Work we will perform:

- ▶ Assess the work performed by the Council's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work.
- ▶ Involve EY internal specialists to challenge the work performed by the Council's valuers, where appropriate.
- ▶ Sample test key asset information used by the valuers in performing their valuation (e.g. floor plans to support valuations based on price per square metre).
- ▶ Review the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code for PPE and annually for investment properties. We will also consider if there are any specific changes to assets that have occurred and that these have been communicated to the valuer.
- ▶ Test assets not subject to valuation in 2020/21 to confirm that the remaining asset base is not materially misstated.
- ▶ Examine changes to useful economic lives as a result of the most recent valuation.
- ▶ Test accounting entries have been correctly processed in the financial statements.

2. Valuation of pension assets and liabilities

The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Lothian Pension Fund.

The information disclosed is based on the IAS 19 report issued by the Council's actuary.

Triennial valuations of Scottish Local Government Pension Funds are due to be completed in March 2021. This will identify the funding level in each scheme and inform future funding and investment strategies as well as determining the level of employer and employee contribution rates from 2021/22 onwards.

Accounting for this scheme involves significant estimation and judgement, including financial and demographic assumptions. The Council engages an actuary to undertake the calculations on their behalf.

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

Work we will perform:

- ▶ Liaise with the auditor of Lothian Pension Fund to obtain assurances over the information supplied to the actuary in relation to the Council and confirm joint assurances in respect of employer and employee contributions in the year.
- ▶ Engage our actuarial specialists to assess the work of the actuary (Hyman Robertson), including the assumptions they have used and their assessment of the liability due to recent legal rulings for McCloud and Goodwin.
- ▶ Relying on the work of PWC, appointed to consider actuarial assumptions used at the year end for all local government sector bodies.
- ▶ Review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS19.
- ▶ Require an updated IAS19 report in July to ensure that there have been no material movement in the value of pension fund assets between the initial IAS19 report, and the signing of the financial statements.

Other audit considerations

We also plan and perform certain general audit procedures on every audit which may not be directly related to financial statement account assertions. Examples of such procedures includes compliance with applicable laws and regulations, litigation and claims and related parties.

Changes to Auditing Standards

A revised ISA (UK) 701 applies from 2020/21 and aims to secure enhancements to auditor reporting. Our Annual Audit Report will therefore include:

- ▶ a description of the most significant assessed risks of material misstatement that were identified by the auditor which had the greatest effect on the overall audit strategy, the allocation of resources in the audit, and directing the efforts of the audit team;
- ▶ how each of the above significant risks of material misstatement was addressed including, as a new requirement of the ISA, significant judgements made with respect to each one;
- ▶ specifying the materiality threshold for the financial statements as a whole and, as new requirements, specifying performance materiality and providing an explanation of the significant judgments in determining these amounts; and
- ▶ an overview of the scope of the audit, including an explanation of how it addressed each of the significant assessed risks of material misstatement and how it was influenced by the auditor's application of materiality.

ISA(UK) 540 on accounting estimated was issues in December 2019. Guidance on inherent risk factors relevant to the public sector includes examples to be considered such as:

- ▶ a very high degree of estimation uncertainty caused by the need to project forecasts far into the future, such as liabilities relating to defined benefit pension schemes
- ▶ areas where there may be a lack of available comparators for estimates that are unique to the public sector, such as the valuation of important public assets
- ▶ the existence of possible constructive obligations created by political statements or past practice of carrying out actions that may be expected of public authorities but are not required by law; and
- ▶ political uncertainty and the possibility of future changes in public policy having an impact on the assumptions used to prepare accounting estimates.

Updates to the CIPFA/LAASAC Code for 2020/21

Changes have been made to the guidance notes issued by CIPFA/LAASAC on the Accounting Code for 2020/21;

- ▶ Amendments to reflect changes to the definition of material which now makes reference to the concept of obscuring information.
- ▶ Implementation of amendments to IAS 19 in respect of a pension scheme amendment, curtailment or settlement occurring during the year.
- ▶ Amendments to the disclosure requirements for pension funds in respect of pooled investment vehicles.
- ▶ Clarifications in respect of aspects of financial instruments.

We do not currently consider that the above would result in a material impact to the Council. However, it is important that the Council ensures that it performs its own assessment of the impact in advance of preparation of the 2020/21 financial statements. We will assess management's implementation of this guidance as part of the 2020/21 audit.

Revised practice note on auditing public bodies

A revised version of Practice Note 10 *Audit of Financial Statements and Regularity of Public Sector Bodies in the UK (PN 10)* was issued in November 2020.

A significant aspect of PN 10 is the guidance on applying ISA (UK) 570 Going Concern to the public sector.

Going Concern

Under the revised standard, ISA 570, we are required to undertake greater challenge of management's assessment of going concern, including testing of the adequacy of the supporting evidence we obtained. PN 10 has been extensively revised to clarify the importance of the applicable financial reporting framework in determining the extent of the auditor's procedures. As in prior years, due to the anticipated continuation of service provision, the going concern basis of accounting will continue to be appropriate for the Council. We will review the requirements of the refreshed guidance alongside our wider scope work on Financial Sustainability.

Use of specialists

When auditing key judgements, such as the valuation of property, plant and equipment, defined benefit pension scheme assets and liabilities, or certain assets and liabilities, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

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

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

Internal audit

We will review the internal audit plan and the results of internal audit's work, including the discussion of audit findings at the Audit Committee and management's response to findings. We will reflect the findings from internal audit reports, together with reports from any other work completed in the year, in our plan for the audit, where they raise issues that could have an impact on the financial statements or our wider responsibilities.

Data analytics

Where possible and appropriate, we will use our bespoke data analysers to enable us to capture whole populations of your financial data, in particular covering journal entries and payroll transactions. These analysers help identify specific exceptions and anomalies within populations of data to focus substantive audit tests more effectively than traditional audit sampling.

We will obtain the financial data from both the general ledger and payroll system for 2020/21 as part of our testing strategy. We will report the findings of our work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Audit Committee through the yearend audit reporting process.

Group financial statements

The Council has a number of non-consolidated interests in other entities. For the purposes of consolidation and incorporation within the Group financial statements the Council recognises subsidiaries including trusts, bequests, common good and trust funds as well as Pacific Shelf 826 Ltd. These entities are below the materiality threshold.

Management has assessed that it exerts significant influence but not control over Lothian Valuation Joint Board, therefore this interest is deemed to be an associate.

The Midlothian Integration Joint Board (IJB) is identified as a joint venture and consolidated in accordance with the requirements of the Code. We have been appointed as auditor to the Midlothian Integration Joint Board and will report separately on our audit of that entity.

The only significant component by size is the Council, which accounts for 99% of consolidated gross expenditure. There have been no specific risks identified that may indicate a component is significant by risk, as the IJB does not affect the transactions as such, only the nominal funding agreement in and out of the IJB.

We will also discuss with management their updated assessment in respect of other entities where the Council has a relationship, but at this stage, it has been assessed that consolidation has not been required.

Other assurance activity

Under the terms of our appointment we are required to undertake a number of other areas of audit activity. These include certifying authorities Whole of Government Accounts returns and certifying any applicable grant claims and returns such as the non-domestic rates return and housing benefits subsidy claim.

Anti-money laundering

The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 came into force on 26 June 2017 and replace The Money Laundering Regulations 2007. The regulations impose an obligation on the Auditor General to inform the National Crime Agency if she knows or suspects that any person has engaged in money laundering or terrorist financing. As appointed auditor we will consider arrangements in place for the Council to identify and report any instances of money laundering in line with Audit Scotland reporting arrangements.

4

Wider Scope Dimensions: Risk assessment and approach

Our wider scope audit work, and the judgements and conclusions reached in these areas, contribute to the overall assessment and assurance on the achievement of Best Value.

The Code sets out the four dimension that comprise the wider scope audit for public sector in Scotland. These are: financial sustainability, financial management, governance and transparency, and value for money. The Accounts Commission has also set five strategic Audit Priorities in its 2019-24 strategy. In 2020/21 auditors are not specifically asked to consider and report on these through our audit work, however we will continue to consider them as part of our wider scope work through the year.

As part of our risk assessment procedures, we have reviewed each dimension to assess potential areas of risk. We set out our areas of focus, along with specific significant risks relating to each dimension below.

Our wider scope audit work, and the judgements and conclusions reached in these areas, contribute to the overall assessment of and assurance over the achievement of Best Value.

Best Value audit approach

Our wider scope audit work, and the judgements and conclusions reached in these areas, contribute to the overall assessment and assurance on the achievement of Best Value. The Accounts Commission published the Best Value Assurance Report (BVAR) for Midlothian Council in July 2019.

In August 2019, the Council considered and implemented an action plan to respond to the recommendations within the BVAR. In 2020/21 and beyond, our work will include a follow-up on the findings from the Best Value report and monitoring of the implementation of the improvement actions that the Council identified. Our Annual Audit Report will consider how the Council has demonstrated improvement against the recommendations included within the 2019 Best Value report, while reflecting the severe impact of the pandemic on capacity and priorities.

As a result of the impact of the pandemic and lockdown arrangements in 2020, we postponed our work on Best Value in 2019/20 and have reassessed our overall Best Value programme, in agreement with Audit Scotland. Our updated plan of Best Value coverage is attached at Appendix C.

Financial Sustainability

Financial sustainability considers the medium and longer term outlook for the Council to determine if planning is effective to support service delivery. We focus on the arrangements to develop viable and sustainable financial plans.

In our 2019/20 Annual Audit Report, we noted that the adoption of the Medium Term Financial Strategy and supporting governance arrangements meant that savings proposals were well advanced prior to the impact of Covid-19. Early work to develop Midlothian's local route map through and out of the crisis provides clear and coherent focus on priorities, including economic recovery for the community, and will therefore support the development of future financial plans.

Continuing financial pressures

The Council's most recent projections note a net impact of £2.2 million as a result of the response to the global pandemic in 2020/21. The Council also faces an ongoing challenge to deliver savings in light of the level of risks and uncertainty that are outside the Council's control, including Covid-19 factors and decisions on funding allocations. While the short term risk may be mitigated by fiscal flexibilities, there is a need for continued member and officer focus to safeguard financial sustainability.

The Council has a shared route map through and out of the Covid-19 crisis which aims to secure transformation and support recovery. Our work in this area in 2020/21 will include:

- ▶ Consideration of the Council's updated medium term financial plans, including the risk assessment of savings options;
- ▶ Assessment of the Council's plans to use fiscal flexibilities to ensure the plans are in accordance with Scottish Government guidance; and
- ▶ Progress with embedding the medium term financial strategy, including the revenue consequences of the Council's capital planning.

Financial management

The financial management dimension considers the effectiveness of financial management arrangements, including whether there is sufficient financial capacity and resources, sound budgetary processes and whether the control environment and internal controls are operating effectively.

Other financial management work in 2020/21 will encompass:

- ▶ Assessment of the control framework with a focus on the prevention of fraud and irregularity, including in procurement;
- ▶ The Council's self-assessment of compliance against the CIPFA Financial Management Code;
- ▶ A focus on controls to mitigate the risk of fraudulent claims processed by, or on behalf of, the Council in relation to Covid-19 related support for communities and businesses; and
- ▶ Continuing monitoring of the Council's participation in the National Fraud Initiative, including notification of any failure to investigate matches by September 2021.

Treasury Management and the application of the Prudential Code are areas of increased focus in local government. In response to the recommendation of the UK Parliament's Public Accounts Committee and the substantial increase in commercial investment, CIPFA proposes to strengthen the provisions within both the existing Prudential and Treasury Management Codes. The closing date for responses to consultations is set for 12 April 2021. The intention is for the revised codes to be published towards the end of the calendar year for 2021/22 implementation.

In December 2020, the Council received media attention due to their fixed-term deposit of funds placed on 3 April 2020 with the London Borough of Croydon Council, which had issued a statutory section 114 notice on 11 November 2020. The increased attention and scrutiny of treasury management and the application of the prudential code within local government, along with specific concerns expressed by members of the Audit Committee, has led to our consideration of treasury management as an area of increased focus as part of our wider scope audit procedures in 2020/21.

Focus on Treasury Management

The effectiveness and appropriateness of the Council's arrangements for Treasury Management will be an area of focus for the 2020/21 audit. Specifically, our wider scope consideration will assess:

- ▶ Whether the Council's Treasury Management and Investment Strategy is in line with the principles of the Prudential and Treasury Management Codes.
- ▶ Whether the Council can demonstrate that strategies have been applied in practice through the consideration of a sample of transactions in year. This will consider whether the appropriate due diligence has been taken in advance of borrowing and investments decisions.
- ▶ The Council's process for appointing their current Treasury Management advisers and reviewing and considering the advice received.
- ▶ The quality and completeness of treasury management reporting to management, Audit Committee and Council.

In light of the level of concern expressed by the Audit Committee in relation to this area, it is our current intention to complete this work early in the audit cycle to allow us to report findings to the May meeting of the Audit Committee.

Governance and Transparency

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.

In our 2019/20 Annual Audit Report we concluded that the key features of good governance are in place and operating effectively. No significant risks have been identified in relation to this dimension.

Our work for the year will consider:

- ▶ Progress against recommendations from both internal and external audit alongside the Best Value Report, including the Council's arrangements for ensuring these are monitored and reported on a routine basis;
- ▶ Internal audit arrangements during 2020/21, including significant findings identified and the work done to address issues identified;
- ▶ The quality of reporting and information provided to key decision makers, and evidence of effective challenge and scrutiny;
- ▶ Following the public pound arrangements;
- ▶ Implementation of the revised governance arrangements to respond the second national lockdown, ensuring appropriate transition arrangements were in place; and
- ▶ Progress in developing a revised programme of member training and support.

Value for money

We consider whether value for money can be demonstrated in the use of resources. This includes the extent to which there is an alignment between spend, outputs and outcomes delivered and that there is a clear focus on improvement. As part of its Best Value improvement plan, the Council has introduced revised performance management arrangements to further support elected member scrutiny.

We have not identified a specific significant risk in relation to value for money but we note that the Council is required to meet the requirements of the revised Statutory Performance Information Direction.

5 Appendices

A - Code of Audit Practice: responsibilities

B - Independence and audit quality

C - Best Value Programme of Coverage

D - Required communications with the Audit Committee

E - Timing and deliverables of the audit

F - Audit fees

G - Additional audit information

Appendix A: Code of Audit Practice Responsibilities

Audited Body's Responsibilities

<p>Corporate Governance</p>	<p>Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.</p>
<p>Financial Statements and related reports</p>	<p>Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:</p> <ul style="list-style-type: none"> ▶ preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation. ▶ maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures. ▶ ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority. ▶ maintaining proper accounting records. ▶ preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body. ▶ Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework. <p>Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.</p>
<p>Standards of conduct / prevention and detection of fraud and error</p>	<p>Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.</p>
<p>Standards of conduct / prevention and detection of fraud and error</p>	<p>Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:</p> <ul style="list-style-type: none"> ▶ such financial monitoring and reporting arrangements as may be specified ▶ compliance with any statutory financial requirements and achievement of financial targets ▶ balances and reserves, including strategies about levels and their future use ▶ how they plan to deal with uncertainty in the medium and longer term ▶ the impact of planned future policies and foreseeable developments on their financial position.
<p>Best Value</p>	<p>Local authority bodies have a statutory duty, under the Local Government (Scotland) Act 1973 and associated statutory guidance, to make arrangements to secure best value through the continuous improvement in the performance of their functions.</p>

Appendix B: Independence Report

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

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

We confirm that we have undertaken client and engagement continuance procedures, which include our assessment of our continuing independence to act as your external auditor.

Appendix C: Best Value Programme of Coverage

The annual audit will continue to focus on specific aspects of Best Value over the course of our audit appointment. Our updated plan of coverage is outlined below.

Best Value Audit Coverage						
	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Vision and Leadership						
Sound Governance and Accountability						
Effective Use of Resources						
Partnership and collaborative working						
Community responsiveness						
Sustainability						
Fairness and equality						
Performance outcomes and improvement						

Appendix D: Required Communications

Required communication	Our reporting to you
<p>Terms of engagement / Our responsibilities</p> <p>Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.</p> <p>Our responsibilities are as set out in our engagement letter.</p>	<p>Audit Scotland Terms of Appointment letter - audit to be undertaken in accordance with the Code of Audit Practice</p>
<p>Planning and audit approach</p> <p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p>	<p>Annual Audit Plan</p>
<p>Significant findings from the audit</p> <ul style="list-style-type: none"> ▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▶ Significant difficulties, if any, encountered during the audit ▶ Significant matters, if any, arising from the audit that were discussed with management ▶ Written representations that we are seeking ▶ Expected modifications to the audit report ▶ Other matters if any, significant to the oversight of the financial reporting process 	<p>Annual Audit Plan Annual Audit Report</p>
<p>Going concern</p> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> ▶ Whether the events or conditions constitute a material uncertainty ▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▶ The adequacy of related disclosures in the financial statements 	<p>Annual Audit Report</p>
<p>Misstatements</p> <ul style="list-style-type: none"> ▶ Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation ▶ The effect of uncorrected misstatements related to prior periods ▶ A request that any uncorrected misstatement be corrected ▶ Corrected misstatements that are significant ▶ Material misstatements corrected by management 	<p>Annual Audit Report</p>
<p>Fraud</p> <ul style="list-style-type: none"> ▶ Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity ▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist ▶ A discussion of any other matters related to fraud 	<p>Annual Audit Report</p>
<p>Consideration of laws and regulations</p> <ul style="list-style-type: none"> ▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ▶ Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of 	<p>Annual Audit Report or as occurring if material.</p>

Required communication	Our reporting to you
<p>Related parties</p> <p>Significant matters arising during the audit in connection with the entity's related parties including, when applicable:</p> <ul style="list-style-type: none"> ▶ Non-disclosure by management ▶ Inappropriate authorisation and approval of transactions ▶ Disagreement over disclosures ▶ Non-compliance with laws and regulations ▶ Difficulty in identifying the party that ultimately controls the entity 	<p>No significant matters have been identified.</p> <p>Annual Audit Report or as occurring if material.</p>
<p>Independence</p> <p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> ▶ The principal threats ▶ Safeguards adopted and their effectiveness ▶ An overall assessment of threats and safeguards ▶ Information about the general policies and process within the firm to maintain objectivity and independence 	<p>Annual Audit Plan</p> <p>Annual Audit Report</p>
<p>Internal controls</p> <p>Significant deficiencies in internal controls identified during the audit</p>	<p>Annual Audit Report</p>
<p>Group audits</p> <ul style="list-style-type: none"> ▶ An overview of the type of work to be performed on the financial information of the components ▶ An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components ▶ Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work ▶ Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted ▶ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements 	<p>Annual Audit Plan</p> <p>Annual Audit Report</p>
<p>Representations</p> <p>We will request written representations from those charged with governance.</p>	<p>Annual Audit Report</p>
<p>Subsequent events</p> <p>Where appropriate, asking the audit committee whether any subsequent events have occurred that might affect the financial statements.</p>	<p>Annual Audit Report</p>
<p>Material inconsistencies</p> <p>Material inconsistencies or misstatements of fact identified in other information which management has refused to revise</p>	<p>Annual Audit Report</p>
<p>Fee Reporting</p> <ul style="list-style-type: none"> ▶ Breakdown of fee information when the audit plan is agreed ▶ Breakdown of fee information at the completion of the audit ▶ Any non-audit work 	<p>Annual Audit Plan</p> <p>Annual Audit Report</p>

Appendix E: Timing and deliverables of the audit

We deliver our audit in accordance with the timeline set by the Council, in accordance with guidance from Audit Scotland. Below is a timetable showing the key stages of the audit and the deliverables through the 2020/21 audit cycle.

JAN	Audit Activity	Deliverable	Timing
FEB	<ul style="list-style-type: none"> Onsite fieldwork, documentation and walkthrough of key accounting processes 	Annual Audit Plan	Finalised by April 2021
MAR	<ul style="list-style-type: none"> Scoping of wider scope work for year 		
APR	<ul style="list-style-type: none"> Review of current issues impacting the Council 	Quarterly current issue return submission	Quarterly
	<ul style="list-style-type: none"> Review of reported frauds 	Quarterly fraud return submission	Quarterly
MAY	<ul style="list-style-type: none"> Education Maintenance Allowance (EMA) grant claim testing 	Certified EMA return	TBD: Guidance in May
JUN	<ul style="list-style-type: none"> Submit minimum dataset return to Audit Scotland 	Return for financial overview	TBD: Guidance in May
JUL	<ul style="list-style-type: none"> Review progress of NFI exercise 	Submit NFI Questionnaire	Notified of progress September 2021
AUG	<ul style="list-style-type: none"> Year-end substantive audit fieldwork on unaudited financial statements 	Whole of Government Accounts assurance statement to NAO (as required)	
SEP	<ul style="list-style-type: none"> Conclude on results of audit procedures 	Certify Annual Financial Statements	Provisionally set at 30 October 2021
OCT	<ul style="list-style-type: none"> Issue opinion on the Council's financial statements 	Issue Annual Audit Report	
		Submit minimum dataset return to Audit Scotland	
NOV	<ul style="list-style-type: none"> Completion of Non-Domestic Rates return testing 	Certified Non-Domestic Rates return	TBD: Guidance in May
DEC	<ul style="list-style-type: none"> Completion of Housing Benefits claim testing 	Certified Housing Benefit subsidy claim	TBD: Guidance in May

Appendix F: Audit fees

The audit fee is determined in line with Audit Scotland's fee setting arrangements, set out in recent communications to all audited bodies in line with their publication on 'Our Approach to setting audit fees' (http://www.audit-scotland.gov.uk/uploads/docs/um/audit_fee_approach.pdf).

Audit Fees (including VAT)	2020/21	2019/20
Component of fee:		
Auditor remuneration - expected fee	£148,890	£144,550
Additional audit procedures (note 1)	£TBD	£45,110
Audit Scotland fixed charges:		
Pooled costs	£14,160	£14,140
Performance audit and best value	£66,860	£64,560
Audit support costs	£8,190	£8,740
Total fee	£TBD	£277,100

The expected fee for each body, set by Audit Scotland, assumes that it has sound governance arrangements in place and operating effectively throughout the year, prepares comprehensive and accurate draft financial statements and meets the agreed timetable for the audit. It also assumes there is no major change in respect of the scope of work in the year. Fees can be agreed between the auditor and audited body by varying the auditor remuneration by up to 10% above the level set, for example, where significant local issues require additional work to be undertaken.

Note 1

We have outlined through areas of additional audit focus this year which are likely to have an impact on the expected fee, including the Council's Treasury Management process, arrangements for administering Covid-19 grants, the implications of changes to auditing standards and our follow up of findings within the Best Value Assurance Report.

Where further additional work is required, fees will be agreed with management and reported to the Audit Committee in our 2020/21 Annual Audit Report.

Factors Likely to Impact Future Audit Fees

While responsibility for setting the audit fee on an annual basis rests with the Audit Scotland, there are a number of factors that we anticipate will continue to impact audit fees that we would bring to the attention of the Audit Committee:

Regulatory Factors: Recent high profile corporate failures have weakened public trust and confidence in both the auditing profession and business at large. Multiple ongoing regulatory reviews continue to reshape the corporate reporting environment and raise fundamental questions about the purpose, product and role of an external audit, as well as the accountability of auditors and those charged with governance.

Status of sector: Financial reporting and decision making in local government has become increasingly complex, for example from the growth in commercialisation and investments. This has also brought increasing risk about the financial sustainability of councils.

Audit of estimates: There has been a significant increase in the focus on areas of the financial statements where judgemental estimates are made. This is to address regulatory expectations on the extent of audit procedures performed in areas such as the valuation of land and buildings and pension assets and liabilities.

Resourcing: Across the sector, auditing has become less attractive as a profession, especially due to regulatory pressure and greater compliance requirements. This has contributed to higher attrition rates in our profession over the past year and we face intense competition for the best people, with appropriate public sector skills, as a result of a shrinking resource pool. While local authorities also facing challenges to recruit and retain staff with the necessary financial reporting skills and capabilities.

To respond to these factors we have to:

- ▶ Increase our sample sizes, seek higher levels of corroborative evidence and engage with our internal specialists on a wider array of matters;
- ▶ Increase our investment in data analytics tools to allow us to test more transactions to a greater level of detail and enhance audit quality; and
- ▶ Invest in our audit quality infrastructure, as a firm our compliance costs have doubled as a proportion of revenue over the past five years.

Appendix G: Additional audit information

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

Our responsibilities required by auditing standards

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

Purpose and evaluation of materiality

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

Materiality determines the locations at which we conduct audit procedures and the level of work performed on individual account balances and financial statement disclosures.

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

Audit Quality Framework / Annual Audit Quality Report

Audit Scotland are responsible for applying the Audit Quality Framework across all audits. This covers the quality of audit work undertaken by Audit Scotland staff and appointed firms. The team responsible are independent of audit delivery and provide assurance on audit quality to the Auditor General and the Accounts Commission.

We support reporting on audit quality by providing additional information including the results of internal quality reviews undertaken on our public sector audits. The most recent audit quality report can be found at: <https://www.audit-scotland.gov.uk/report/quality-of-public-audit-in-scotland-annual-report-201920>.

EY has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained. Details can be found in our annual Transparency Report:

https://www.ey.com/en_uk/who-we-are/transparency-report-2020

EY | Assurance | Tax | Transactions | Advisory

About EY

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

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

Ernst & Young LLP

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

© 2021 Ernst & Young LLP. Published in the UK.
All Rights Reserved.

ey.com