# Staffordshire County Council

Year ending 31 March 2017

Audit Plan

February 2017

Ernst & Young LLP

Building a better working world

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Private and confidential

February 2017

Members of the Audit and Standards Committee
Staffordshire County Council
Staffordshire Place 1
Stafford
ST16 2DH

Dear Committee Members

## Reporting of the 2016-17 External Audit Plan

We are pleased to attach our Audit Planning report for the forthcoming meeting of the Audit and Standards Committee. The purpose of the report is to provide the Committee with a basis to review our proposed audit approach and scope for the 2016/17 audit, in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, standing guidance, international auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

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

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

We welcome the opportunity to discuss this Audit Plan with you on 13 March 2017 and to understand whether there are other matters which you consider may influence our audit.

Yours faithfully

**Steve Clark**
Partner
*For and behalf of Ernst & Young LLP*

*Enclosures*

# Contents



In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued ''Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website (www.psaa.co.uk).

The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The 'Terms of Appointment from 1 April 2015' issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Plan is prepared in the context of the Statement of responsibilities. It is addressed to the Audit Committee, and is prepared for the sole use of the audited body. We, as appointed auditor, take no responsibility to any third party.

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

# 1. Overview

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

- Our audit opinion on whether the financial statements of Staffordshire County Council (the Council) give a true and fair view of the financial position as at 31 March 2017 and of the income and expenditure for the year then ended.
- A statutorily required conclusion on the Council's arrangements to secure economy, efficiency and effectiveness (the Value for Money conclusion).

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

We will also give the electors the opportunity to raise questions about the accounts and consider and decide upon objections received in relation to the financial statements.

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

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

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

Our annual results report will be brought to this Committee in September 2017 to update those charged with governance on the results of our work in these areas.

# 2. Financial statement risks

We analyse the risks in your operational activities, external influences and through knowledge of the Council. We outline below our current assessment of the financial statement risks facing the Council, identified through our knowledge of the Council's operations and discussion with those charged with governance and officers.

At our meeting, we will seek to validate these with you.

## 2.1 Significant risks

Of the financial statement risks identified, we are required by Auditing Standards to consider whether any of the risks identified are 'significant' risks to our audit. Auditing standards define significant risks as those with a high likelihood of occurrence and, if they were to occur, could result in a material misstatement of the consolidated financial statements:

There are two presumed risks present in every audit:

- Risk of management override of controls*
- Risk of fraud in revenue and expenditure recognition*

** As defined by auditing standards*

| Significant risks (including fraud risks) | Our audit approach |
|---|---|
| **Risk of fraud in revenue recognition** | |
| Under ISA (UK and Ireland) 240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue.<br><br>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. | Having considered the factors for expenditure recognition, we believe the risk is focused on the year-end balance sheet and in particular the completeness and valuation of creditors and the existence and valuation of debtors. We also believe the risk is linked to the existence of capital expenditure arising from the potential to incorrectly capitalise revenue expenditure.<br><br>We will:<br>► Review and test expenditure recognition policies.<br>► Review and discuss with management any accounting estimates on expenditure recognition for evidence of bias.<br>► Test the valuation of any provisions recorded in the financial statements and perform appropriate tests to consider whether all material provisions have been recognised.<br>► Develop a testing strategy to test material debtors and creditors.<br>► Develop a testing strategy to test whether the Council has inappropriately capitalised revenue expenditure. |
| **Risk of management override** | |
| As identified in ISA (UK and Ireland) 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 | Based on the requirements of auditing standards our approach will focus on:<br>► Identifying fraud risks during the planning stages.<br>► Inquiry of management about risks of |

| | |
|---|---|
| otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement. | fraud and the controls put in place to address those risks.<br>► Understanding the oversight given by those charged with governance of management’s processes over fraud.<br>► Consideration of the effectiveness of management’s controls designed to address the risk of fraud.<br>► Determining an appropriate strategy to address those identified risks of fraud.<br>► Developing a testing approach to journal entries.<br>► Assessing accounting estimates for evidence of management bias.<br>► Evaluating the business rationale for any significant unusual transactions.<br>► Performing appropriate tests to assess whether provisions are both complete and fairly stated.<br>► Performing mandatory procedures regardless of specifically identified fraud risks.<br>► Consider whether the results of testing for incorrect revenue and expenditure recognition indicates management override of controls. |

In addition to the two mandated significant risks, we have identified two further significant risks to the 2016/17 audit.

| Significant risk | Our audit approach |
|---|---|
| **Property, Plant and Equipment Valuation** | |
| In a refresh of our approach to the audit of large local authorities, we have included a further significant risk relating to the valuation of Property, Plant and Equipment.<br>Property, Plant and Equipment accounts for a significant proportion of the Council’s (£2billion at 31 March 2016) total assets.<br>The Council carries out a rolling programme that ensures that all property, plant and equipment required to be measured at fair value is revalued at least every five years. All valuations are carried out by the Council’s own specialist valuer and must follow the methodologies and bases for estimation set out in the professional standards of the Royal Institution of Chartered Surveyors. This process incorporates significant judgements. | We will:<br>► Review each class of asset and the valuation approach adopted to assess where the risk of material misstatement is higher. We will share this risk assessment with management.<br>► Evaluate the competence, capabilities and objectivity of management’s specialist.<br>► Review any terms of engagement or instructions issued to the valuer to ensure these are consistent with accounting standards.<br>► Engage our valuation specialists to support our testing strategy and help evaluate the work of the Council’s valuer.<br>► Perform appropriate tests over the completeness and appropriateness of information provided to the valuer.<br>► Review the classification of assets and ensure the correct valuation methodology has been applied.<br>► Ensure the valuer’s conclusions have |

| Significant risk | Our audit approach |
|---|---|
| | been appropriately recorded in the accounts. |
| **Accounting for the Waste PFI** | |
| The Council has four PFI Schemes, the most significant of which is the Waste to Energy PFI Scheme and was subject to material audit adjustment in 2015/16.<br><br>Accounting for this material scheme requires the use of a complex financial model, the calculation of estimates and the application of management judgement. | We will involve our financial modelling and PFI experts to:<br>► Test the integrity of the financial model used by the Council.<br>► Test the completeness and accuracy of the inputs to the financial model and the subsequent correct application of the outputs to the financial statements. |

## 2.2 Other key areas of audit focus

We have identified other key 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.

| Other financial statement risks | Our approach |
|---|---|
| **LGPS Liability** | |
| The Council is a member of the Local Government Pension Scheme (LGPS), administered by Staffordshire Pension Fund. The net pension liability was £935million as at 31 March 2016.<br><br>The estimation of the defined benefit obligations is sensitive to a range of assumptions, such as mortality, the rate of inflation, salary increases, pension changes and discount rates. The Pension Fund separately engages an external valuation specialist, Hymans Robertson LLP, to provide these actuarial assumptions.<br><br>The extent of judgement required, and resulting significant impact this has on the value in the balance sheet, means it is an area for additional audit focus. | We will:<br>► Engage EY actuarial experts to assist our review of the key actuarial assumptions impacting the pension fund liability.<br>► Perform appropriate tests to obtain assurance over the information provided to the actuary.<br>► Write to the Pension Fund auditor to ascertain whether there are material concerns we need to be aware of for our audit.<br>► Ensure accounting entries and disclosures are consistent with the actuaries report. |
| **Financial statements presentation – Expenditure and funding analysis and Comprehensive income and expenditure statement** | |
| Amendments have been made to the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the code) this year changing the way the financial statements are presented.<br><br>The new reporting requirements impact the Comprehensive Income and Expenditure Statement (CIES) and the Movement in Reserves Statement (MiRS), and include the introduction of the new 'Expenditure and Funding Analysis' note as a result of the 'Telling the Story' review of the presentation of local authority financial statements.<br><br>The Code no longer requires statements or notes to be prepared in accordance with | Our approach will focus on:<br>► Review of the expenditure and funding analysis, CIES and new notes to ensure disclosures are in line with the code<br>► Review of the analysis of how these figures are derived, how the ledger system has been re-mapped to reflect the Council's organisational structure and how overheads are apportioned across the service areas reported.<br>► Agreement of restated comparative figures back to the Council's segmental analysis and supporting working papers. |

| Other financial statement risks | Our approach |
|---|---|
| SeRCOP. Instead the Code requires that the service analysis is based on the organisational structure under which the authority operates. We expect this to show the Council's segmental analysis.<br>This change in the code will require a new structure for the primary statements, new notes and a full retrospective restatement of impacted primary statements. The restatement of the 2015/16 comparatives will require audit review, which could potentially incur additional costs, depending on the complexity and manner in which the changes are made. | |

## 2.3 Responsibilities in respect of fraud and error

We would like to take this opportunity to remind you that management has the primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

Our responsibility is to plan and perform audits to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud. As auditors, we approach each engagement with a questioning mind that accepts the possibility that a material misstatement due to fraud could occur, and design the appropriate procedures to consider such risk.

Based on the requirements of auditing standards our approach will focus on:

- Identifying fraud risks during the planning stages;
- Enquiry of management about risks of fraud and the controls to address those risks;
- Understanding the oversight given by those charged with governance of management's processes over fraud;
- Consideration of the effectiveness of management's controls designed to address the risk of fraud;
- Determining an appropriate strategy to address any identified risks of fraud, and,
- Performing mandatory procedures regardless of specifically identified risks.

# 3. Value for money risks

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. For 2016/17 this is based on the overall evaluation criterion: "In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people."

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

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

In considering your proper arrangements, we will draw on the requirements of the local authority reporting guidance on governance statements responsibilities published by CIPFA to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

## 3.1 Significant risks

| Significant risks | Our audit approach |
|---|---|
| **Sustainable resource deployment**<br>VFM Criteria: Planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions | |
| The Council's 2016/17 and the recently updated 2017/18 Medium Term Financial Strategy (MTFS) contains a number of significant assumptions and risks to the Council's overall financial resilience.<br>Third quarter financial performance (Cabinet February 2017) shows an overspend of £9.4million mainly due to pressures from the Better Care Fund (BCF) and the Staffordshire & Stoke-on-Trent Partnership NHS Trust risk share.<br>In addition, the 2017/18 budget:<br>► Is dependent on a 4.95% increase in council tax.<br>► Requires the delivery of £47.3million savings.<br>► Identified a £6.1million budget gap in 2018/19. | We will:<br>► monitor the financial position for the remainder of 2016/17, including delivery against revenue and capital budgets;<br>► evaluate the impact of any audit findings on the reported financial position, including the risk of management override and revenue and expenditure recognition;<br>► use any work by internal audit to inform our risk assessment on the adequacy of the Council's arrangements;<br>► review the overall controls in place to manage expenditure in Adult Social Care;<br>► meet with management to discuss the arrangements for financial planning in Adult Social Care; and<br>► review the Council's approach to identify savings and bridge the spending gap for 2017/18 to 2019/20. |
| **Working with third parties effectively to deliver strategic priorities**<br>VFM Criteria: Working with third parties effectively to deliver strategic priorities | |
| The health economy across Staffordshire is significantly challenged, with substantial deficits | We will:<br>► meet with management to discuss |

| Significant risks | Our audit approach |
| --- | --- |
| across the health economy.<br>The MTFS was left with a shortfall of £15million in 2016/17 as a result of additional funding planned for the Better Care Fund (BCF) no longer being available due to financial challenges within the NHS. The Council delayed signing of the 2016/17 BCF whilst this was under negotiation, subsequently signing in January 2017 without the receipt of the £15million.<br>Recently local partners have outlined a “Sustainability and Transformation Plan (STP)” on how they will work together to improve health and social care service and a deliver a financially resilient system for local people. The challenges set in the STP are significant and will require joint working and integrated solutions to deliver planned outcomes.<br>For the purposes of our 2016/17 audit, there is a significant risk to the VFM conclusion that the Council does not have effective arrangements in place to work effectively with the Staffordshire CCGs to deliver strategic priorities through the BCF. | whether arrangements and relationships over the Better Care Fund have improved, including how KPIs have been incorporated into decision making;<br>► use any work by internal audit to inform our risk assessment on the adequacy of the Council’s arrangements;<br>► understand the Council’s approach to bridge the £15m gap in the BCF; and<br>► understand the Council’s approach to incorporate learning and the development of a BCF for 2017/18;<br>► understand how the Council is working with local partners to develop the STP. |
| **Working with third parties effectively to deliver strategic priorities**<br>VFM Criteria: Commissioning services effectively to support the delivery of strategic priorities | |
| Adult social care is provided by Staffordshire & Stoke-on-Trent Partnership NHS Trust (SSOTP) who were inspected by the CQC during 2016/17, rating community adult services rated as 'inadequate'.<br>Combined with the financial pressures and risk share agreement noted above, there is a significant risk to the VFM conclusion that the Council does not have adequate arrangements in place to oversee performance and enact change in a timely manner. | We will review the Council's governance arrangements over the SSOPT contract.<br>We will discuss with management, and obtained supporting evidence, as to the actions taken by the Council as to how it has considered the Trust's performance and what action has been taken to enact change in a timely manner. |

## 3.2 Other matters

We will remain alert to the possibility of new or emerging significant risks as our audit progresses. In particular, we will keep under review:

- The work and reports of regulators, such as the Care Quality Commission and OFSTED.
- The outcome of other aspects of assurance work, such as the audited financial position and the Head of Internal Audit’s opinion.

Should our risk assessment change, we will notify the Director of Finance and Resources and Audit & Standards Committee.

# 4. Our audit process and strategy

## 4.1 Objective and scope of our audit

Under the National Audit Office's Code of Audit Practice (the 'Code') our principal objectives are to review and report on, the Council's:

- Financial statements
- Arrangements for securing economy, efficiency and effectiveness in its use of resources to the extent required by the relevant legislation and the requirements of the Code.

We issue a two-part audit report covering both of these objectives.

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

We will also review and report to the NAO on the Whole of Government Accounts return to the extent and in the form they require.

**ii Arrangements for securing economy, efficiency and effectiveness**
We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. We report by exception only.

## 4.2 Group audit

The Council has two principal entities that fall within the group structure:

- Entrust Support Services Ltd. The Council owns 49% of the ordinary shareholding of Entrust, and Capita plc holds the remaining 51% of the shares in the joint venture.
- Penda Limited, a joint venture company with Kier and the County Council.

On the basis of our initial risk assessment, neither entity is judged to be a significant component of the Group.

Further details are included at Appendix C.

## 4.3 Audit process overview

**Processes**
A key consideration in our audit planning process is the effectiveness of entity level controls; including the extent to which the Council assesses risk, implements controls in order to minimise risk and performs ongoing testing and monitoring of the effectiveness of the controls implemented.

**Analytics**
We will aim to use our computer-based data analytics tools to:

- Focus our testing on specific exceptions and anomalies such as duplicate payments, round sum amounts, items outside of our range of expectations, for example:
    - high volume of payments to individuals or suppliers; and
    - repeated items just below authorisation and approval levels.
- Perform data integrity checks; for example between static supplier master data and the transactional amounts.
- Give greater likelihood of identifying errors than random sampling techniques.

In using our data analytics tool we will be able to gain assurance over populations of transactions and assess if appropriate internal controls are in place to avoid fraud/ error.

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

**Internal audit**

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

**Use of experts**

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

| Area | Specialists |
|---|---|
| Pensions | EY Pensions team<br>Management specialist - Hymans Robertson LLP |
| Property, Plant and Equipment | EY Asset Valuation team<br>Management specialist – in-house valuation team |
| Waste PFI | EY FAAS / PFI 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 environment 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 expert to establish whether the source date is relevant and reliable;
- Assess the reasonableness of the assumptions and methods used;
- Consider the appropriateness of the timing of when the specialist carried out the work; and
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

**Mandatory procedures required by auditing standards**

As well as the financial statement risks outlined in section three, we must perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

***Procedures required by standards***

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

***Procedures required by the Code***

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

Reviewing and examining, where appropriate, evidence relevant to the Council's corporate performance management and financial management arrangements, and its reporting on these arrangements.

## 4.4 Materiality

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

Materiality determines:

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

At this early stage of our audit, we have determined that materiality for the 2016/17 financial statements is £13.25 million based on 1% of the Council's gross expenditure for 2015/16. We will communicate uncorrected misstatements greater than £0.66million to you.

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

## 4.5 Fees

The duty to prescribe scales of fees is a statutory function delegated to PSAA by the Secretary of State for Communities and Local Government. In law, audit fees are not a fee for audit services, but a charge to fund operating costs, out of which the costs of audits are met (http://www.psaa.co.uk/audit-and-certification-fees/201617-work-programme-and-scales-of-fees/).

PSAA has published a scale fee for all authorities. The indicative scale fee for the audit of Staffordshire County Council is **£109,755** and the assumptions underpinning the fee are set out in Appendix A. If any of the assumptions prove to be unfounded, we will seek a variation to the agreed fee and this will be discussed with the Council in advance.

## 4.6 Your audit team

The engagement team is led by Steve Clark, who has significant experience of local authority audits. Steve is supported by Mark Surridge, a Senior Manager who will be responsible for the day-to-day direction of our audit and the key point of contact for the Director of Finance & Resources.

Our audit team also includes a number of specialists to assist us with our procedures, including specialists in pensions, taxation and IT. Where appropriate we will also leverage wider expertise from within the firm. For example: we have a firm wide local authority audit network to share best practice, identify common issues and to develop a consistent audit approach.

## 4.7 Timetable of communication, deliverables and insights

We have set out below a timetable showing the key stages of the audit, including the VFM work and the Whole of Government Accounts. The timetable includes the deliverables we have agreed to provide to the Council through the Audit Committee's cycle in 2016/17.

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Committee Chair as appropriate.

Following the conclusion of our audit we will prepare an Annual Audit Letter to communicate the key issues arising from our work to the Council and external stakeholders, including members of the public

| Audit phase | Timetable | Audit committee timetable | Deliverables |
|---|---|---|---|
| High level planning | **January 2017** | February 2017 | |
| Risk assessment and interim testing of routine processes and controls | **February** | March 2017 | Audit Plan |
| Year-end audit | **July** | | |
| Completion of audit | **July** | September 2017 | Report to those charged with governance via the Audit Results Report<br>Audit report (including our opinion on the financial statements; our opinion on the regularity of your expenditure and income; and overall value for money conclusion).<br>Audit completion certificate<br>Reporting to the NAO on the Whole of Government Accounts return. |
| Conclusion of reporting | **October** | October 2017 | Annual Audit Letter |

In addition to the above formal reporting and deliverables we will seek to provide practical business insights and updates on regulatory matters.

# 5. Independence

## 5.1 Introduction

The APB Ethical Standards and ISA (UK and Ireland) 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 on our independence and objectivity. The Ethical Standards, as revised in December 2010, require that we do this formally both at the planning stage and at the conclusion of the audit, as well as during 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 |
|---|---|
| ► The principal threats, if any, to objectivity and independence identified by EY including consideration of all relationships between you, your affiliates and directors and us;<br>► The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality Review;<br>► The overall assessment of threats and safeguards;<br>► Information about the general policies and process within EY to maintain objectivity and independence. | ► A written disclosure of relationships (including the provision of non-audit services) that bear on our objectivity and independence, the threats to our independence that these create, 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;<br>► Details of non-audit services provided and the fees charged in relation thereto;<br>► Written confirmation that we are independent;<br>► Details of any inconsistencies between APB Ethical Standards, the PSAA Terms of Appointment and your policy for the supply of non-audit services by EY and any apparent breach of that policy; and<br>► An opportunity to discuss auditor independence issues. |

During the course of the audit we must also communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of our safeguards, for example when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future contracted services, and details of any written proposal to provide non-audit services;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period are disclosed, analysed in appropriate categories.

## 5.2 Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including any principal threats. However we have adopted the safeguards below to mitigate these threats along with the reasons why they are considered to be effective.

***Self-interest threats***

A self-interest threat arises when EY has financial or other interests in your entity. Examples include where we have an investment in your entity; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with the Council

At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services, and we will comply with the policies that the Council has approved and that are in compliance with PSAA Terms of Appointment.

At the time of writing, there are no non-audit fees to audit fees is approximately

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

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

***Self-review threats***

Self-review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

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

***Management threats***

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

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

***Other threats***

Other threats, such as advocacy, familiarity or intimidation, may arise.

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

***Overall Assessment***

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

## 5.3 Other required communications

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

Details of the key policies and processes within EY for maintaining objectivity and independence can be found in our annual Transparency Report, which the firm is required to publish by law. The most recent version of this report is for the year ended June 2016 and can be found here:

http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2016

# Appendix A Fees

The fee for 2016/17 is unchanged from the previous period:

| | 2015/16 fee | Planned Fee |
|---|---|---|
| Opinion Audit and VFM Conclusion | £109,755 | £109,755 |
| **Total Audit Fee – Code work** | **£109,755** | **£109,755** |
| Non-audit work | Nil | Nil |

*All fees exclude VAT.*

The agreed fee presented above is based on the following assumptions:

- All working papers are provided in accordance with an agreed timetable.
- Good quality early drafts of the Council's Annual Governance Statement and Financial Statements are available for us to review.
- Appropriate quality supporting documentation is provided by the Council.
- The Council has an effective control environment.
- Our accounts opinion and value for money conclusion being unqualified.

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

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

# Appendix B UK required communications with those charged with governance

There are certain communications that we must provide to the [Audit Committee]. These are detailed here:

| Required communication | Reference |
|---|---|
| **Planning and audit approach**<br>Communication of the planned scope and timing of the audit including any limitations. | ► Audit Plan |
| **Significant findings from the audit**<br>► Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures<br>► Significant difficulties, if any, encountered during the audit<br>► Significant matters, if any, arising from the audit that were discussed with management<br>► Written representations that we are seeking<br>► Expected modifications to the audit report<br>► Other matters if any, significant to the oversight of the financial reporting process<br>► Findings and issues regarding the opening balances on initial audits [delete if not an initial audit] | ► Audit Results Report |
| **Misstatements**<br>► Uncorrected misstatements and their effect on our audit opinion<br>► The effect of uncorrected misstatements related to prior periods<br>► A request that any uncorrected misstatement be corrected<br>► In writing, corrected misstatements that are significant | ► Audit Results Report |
| **Fraud**<br>► Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity<br>► Any fraud that we have identified or information we have obtained that indicates that a fraud may exist<br>► A discussion of any other matters related to fraud | ► Audit Results Report |
| **Related parties**<br>Significant matters arising during the audit in connection with the entity's related parties including, when applicable:<br>► Non-disclosure by management<br>► Inappropriate authorisation and approval of transactions<br>► Disagreement over disclosures<br>► Non-compliance with laws and regulations<br>► Difficulty in identifying the party that ultimately controls the entity | ► Audit Results Report |
| **External confirmations**<br>► Management's refusal for us to request confirmations<br>► Inability to obtain relevant and reliable audit evidence from other procedures | ► Audit Results Report |
| **Consideration of laws and regulations**<br>► 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<br>► 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 | ► Audit Results Report |

| Required communication | Reference |
| --- | --- |
| **Independence**<br>Communication of all significant facts and matters that bear on EY's objectivity and independence<br>Communication of key elements of the audit engagement director's consideration of independence and objectivity such as:<br>► The principal threats<br>► Safeguards adopted and their effectiveness<br>► An overall assessment of threats and safeguards<br>► Information about the general policies and process within the firm to maintain objectivity and independence | ► Audit Plan<br>► Audit Results Report |
| **Going concern**<br>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:<br>► Whether the events or conditions constitute a material uncertainty<br>► Whether the use of the going concern assertion is appropriate in the preparation and presentation of the financial statements<br>► The adequacy of related disclosures in the financial statements | ► Audit Results Report |
| **Significant deficiencies in internal controls identified during the audit** | ► Audit Results Report |
| **Fee Information**<br>► Breakdown of fee information at the agreement of the initial audit plan<br>► Breakdown of fee information at the completion of the audit | ► Audit Plan<br>► Audit Results Report<br>► Annual Audit Letter if considered necessary |

# Appendix C Detailed scopes

We set audit scopes for each reporting unit which together enable us to form an opinion on the group accounts. We take into account the size, risk profile, changes in the business environment and other factors when assessing the level of work to be performed at each reporting unit.

- Full scope: locations deemed significant based on size and those with significant risk factors are subject to a full scope audit, covering all significant accounts and processes using materiality levels assigned by the EY Birmingham audit team for the purposes of the consolidated audit. Procedures are full-scope in nature, but may not be sufficient to issue a stand-alone audit opinion on the local statutory financial statements (as materiality thresholds support to the consolidated audit).
- Specific scope: locations where only specific procedures are performed by the local audit team, based upon procedures, accounts or assertions identified by the EY Birmingham audit team.
- Limited Scope: limited scope procedures primarily consist of enquiries of management and analytical review. On-site or desk top reviews may be performed, according to our assessment of risk.

The Council has two principal entities that fall within the group structure:

- In April 2013 the Council entered into a partnership to form Entrust Support Services Ltd. The Council owns 49% of the ordinary shareholding of Entrust, and Capita plc holds the remaining 51% of the shares in the joint venture.
- The Council has created a Strategic Partnership, which involves the formation of a joint venture company, Penda, with Kier and the County Council. It began in April 2015 for an initial 10-year term, with a potential further five-year extension. As part of the partnership, the Council and PCC provide details of their property assets, local needs and access to other public sector organisations, which may have adjoining assets that can be pooled with the partnership's projects. Kier has appointed staff to the partnership, to provide expertise and advice on those assets, developing and managing the partners' property assets.

On the basis of our initial risk assessment, neither entity is judged to be a significant component of the Group and are outside the scope of our audit.

ISA 600 (UK and Ireland) requires that we provide you with an overview of the nature of our planned involvement in the work to be performed by the component auditors of significant locations/reporting units. Whilst neither entity is judged to be a significant component, our work can be summarised as follows:

- Obtaining the audited financial statements of each joint venture.
- Overall analytical procedures on the transactions recorded in the Council's financial statements.
- Reviewing related party disclosures.
- Reviewing all material adjustments between the Council's single entity accounts and the Group accounts.

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