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This version of the report is a draft. Its contents and subject matter remain under review and its contents may change and be expanded as part of the finalisation of the report.
This draft has been created from the template dated DD MMM YYYY

External Audit Plan

Year ending 31 March 2020

London Borough of Hammersmith and Fulham and Hammersmith and Fulham Pension Fund

March 2020

Contents

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The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit planning process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect the Authority or all weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

1. Introduction & headlines

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Purpose

This document provides an overview of the planned scope and timing of the statutory audits of the London Borough of Hammersmith and Fulham ('the Council') and Hammersmith and Fulham Pension Fund ('the Pension Fund') for those charged with governance.

Respective responsibilities

The National Audit Office ('the NAO') has issued a document entitled Code of Audit Practice ('the Code'). This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. Our respective responsibilities are also set out in the Terms of Appointment and Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA), the body responsible for appointing us as auditor of London Borough of Hammersmith and Fulham and Hammersmith and Fulham Pension Fund. We draw your attention to both of these documents on the PSAA website. We draw your attention to both of these documents.

Scope of our audit

The scope of our audit is set in accordance with the Code and International Standards on Auditing (ISAs) (UK). We are responsible for forming and expressing an opinion on the :

- Council and Pension Fund's financial statements that have been prepared by management with the oversight of those charged with governance (the Audit and Pensions Committee); and
- Value for Money arrangements in place at the Council for securing economy, efficiency and effectiveness in your use of resources.

The audits of the financial statements for the Council and Fund do not relieve management or the Audit and Pensions Committee of their responsibilities. It is the responsibility of the Council and Pension Fund to ensure that proper arrangements are in place for the conduct of their business, and that public money is safeguarded and properly accounted for. We have considered how the Council and Pension Fund are fulfilling these responsibilities.

Our audit approach is based on a thorough understanding of the Council and Pension Fund's business and is risk based.

Significant risks	Those risks requiring special audit consideration and procedures to address the likelihood of a material financial statement error have been identified as: • Valuation of land and buildings (Council only) • Valuation of net pension liability (Council only) • Management override of control (Council and Pension Fund) • Valuation of level 3 investments (Pension Fund only) We will communicate significant findings on these areas as well as any other significant matters arising from the audits to you in our Audit Findings (ISA 260) Report.
Materiality	We have determined planning materiality to be £10m (PY £13m) for the Council, which equates to 1.42% of your prior year gross expenditure for the year. We design our procedures to detect errors in specific accounts at a lower level of precision which we have determined to be £0.1m for disclosures around Officers' Remuneration. We have determined planning materiality for the Pension Fund to be £10m (PY £18m), which equates to 0.95% of your prior year net assets as at 31 March 2019. We are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. Clearly trivial has been set at £0.5m (PY £0.65m) for both the Council and the Pension Fund.
Value for Money arrangements	Our risk assessment regarding the Council's arrangements to secure value for money have identified the following VFM significant risk: • Medium Term Financial Planning
Audit logistics	Our interim visits will take place in February and March and our final visits will take place in June and July. Our key deliverables are this Audit Plan and our Audit Findings Report. Our audit approach is detailed in Appendix A. Our fee for the audit will be £152,242 (PY: £140,242) for the Council, and £25,000 for the Pension Fund (PY: £16,170), subject to the Council and Pension Fund meeting our requirements set out on page 14.
Independence	We have complied with the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express objective opinions on the financial statements of both the Council and Pension Fund.

2. Key matters impacting our audit – Council

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Factors

The wider economy and political uncertainty

Local Government funding continues to be stretched with increasing cost pressures and demand from residents. For the London Borough of Hammersmith and Fulham, there is uncertainty over the future funding that will be made available by a new government, in particular as a result of the Fair Funding review. This will be important in determining the Council's capacity to respond to future demand pressures, in particular relating to social care, children's services and housing.

At a national level, the government continues its negotiation with the EU over Brexit, and future arrangements remain clouded in uncertainty. The Council will need to ensure that it is prepared for all outcomes, including in terms of any impact on contracts, on service delivery and on its support for local people and businesses.

As of month 9, the Council is forecasting an overspend to budget of £7.7m for 2019/20, with the majority of this being attributable to demand pressures on Children's Services. A balanced budget has been set for 2020/21, which includes around £5m anticipated growth relating to this area.

However the medium-term forecast to 2023/24 shows increasing budget gaps year-on-year, approaching £60m.

Financial reporting and audit – raising the bar

The Financial Reporting Council (FRC) has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge, and to undertake more robust testing as detailed in Appendix 1.

Our work in 2018/19 has highlighted areas where local government financial reporting needs to be improved and increased audit procedures are required. Particular areas of additional audit focus are property, plant and equipment, and pensions. We have also identified an increase in the complexity of local government financial transactions which require greater audit scrutiny.

Accounting developments

International Financial Reporting Standard (IFRS) 16 will be introduced across the public sector from 1 April 2020 and will have a significant impact on the way in which the Council accounts for leases, or other contracts which contain a lease. The standard will require management to assess the present value of the liability associated with any arrangement containing a lease and bring this on to the Balance Sheet, along with the value of the associated right of use asset. The Council will be required to disclose in its 2019/20 financial statements the expected initial impact of the implementation of IFRS 16 on its net asset position and reserves as at 1 April 2020.

Our response

- We will consider your arrangements for managing and reporting your financial resources as part of our work in reaching our Value for Money conclusion.
- We will consider whether your financial position leads to material uncertainty about the going concern of the Council and will review related disclosures in the financial statements.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and local government financial reporting. Our proposed work and fee, as set further in our Audit Plan, has been discussed with the Strategic Director, Finance and Governance and is subject to PSAA agreement.

Members of the finance team attended our financial reporting workshops which took place during February 2020, where further guidance and support on IFRS 16 implementation will be provided.

We will review management's assessment of the impact of IFRS 16 on the net assets and reserves of the Council as at 1 April 2020, and review disclosures made in the 2019/20 financial statements, to gain assurance that the standard has been appropriately applied.

2. Key matters impacting our audit – Pension Fund

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Factors

The wider picture and political uncertainty

- Local Government funding continues to be stretched with increasing cost pressures.
- The market value of LGPS funds at end of March 2019 was £287.2 billion (an increase of £16.3 billion or 6.0%) but for the first time, the LGPS in England & Wales is now cashflow negative, with benefit payments rising to £10.4bn while contributions fell to £9.3bn. There are now over 18,000 employers. Local authorities represent around 18.3% of these but have 74% of the members.
- The UK exited the EU on 31 January 2020. The economic impact of this remains uncertain as is the wider global economic picture. The Pension Fund will need to ensure that it's investment strategy has considered potential outcomes.

Governance

- The Scheme Advisory Board (SAB) has published the *Good Governance – Phase II Report*. Proposals include having a single named officer responsible for the delivery of LGPS related activity for a fund, an enhanced annual governance compliance statement and establishing a set of key performance indicators.
- SAB is also consulting on Responsible Investment guidance to assist and help investment decision makers.
- tPR continues to apply pressure on pension schemes to improve the quality of scheme member data. The 2019 valuation process will likely have thrown up some data issues (large or small) that need addressing.

Financial reporting and audit – raising the bar

The Financial Reporting Council (FRC) has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge, and to undertake more robust testing as detailed in Appendix 1.

Our work in 2018/19 has highlighted areas where financial reporting, in particular Level 3 and Financial Instrument investment valuations and disclosures, needs to be improved, with a corresponding increase in audit procedures.

In addition, disclosures around significant judgements and estimation uncertainty are likely to be an area of focus

Triennial LGPS valuation

The local government pension scheme underwent a full triennial valuation as at 31 March 2019 The impact the balance sheet will be reported for the first time in the 2019/20 financial statements for the Council, having also been updated for the 31 March 2020 valuation. Forward contributions required being determined from 2020/21 onwards, after which the funding note in the Pension Fund accounts will also be updated

Our response

- We will consider whether your financial position leads to material uncertainty about the going concern of the Pension Fund and will review related disclosures in the financial statements.

- We will consider the Pension Fund's responses to the SAB initiatives and whether they impact upon our risk assessment.
- We will consider the impact of any data issues raised as part of the 2019 on the risks identified as part of our 2019/20 audit.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and financial reporting. Our proposed work and fee, as set further in our Audit Plan, has been discussed with the Strategic Director, Finance and Governance and is subject to PSAA agreement

We will perform additional procedures to gain assurance over the completeness and accuracy of financial and non-financial data provided to the Pension Fund actuary in respect of the triennial valuation, and consider the impact of the updated funding ratio on the Fund's going concern position.

3. Significant risks identified

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Significant risks are defined by ISAs (UK) as risks that, in the judgement of the auditor, require special audit consideration. In identifying risks, audit teams consider the nature of the risk, the potential magnitude of misstatement, and its likelihood. Significant risks are those risks that have a higher risk of material misstatement.

Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
Fraud in revenue and expenditure recognition	**Council and Pension Fund**	Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Council and Pension Fund, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because: • there is little incentive to manipulate revenue recognition • opportunities to manipulate revenue recognition are very limited • the culture and ethical frameworks of local authorities, including the London Borough of Hammersmith and Fulham, mean that all forms of fraud are seen as unacceptable Practice Note 10: Audit of Financial Statements of Public Sector Bodies in the United Kingdom (PN10) further states: "As most public bodies are net spending bodies, then the risk of material misstatement due to fraud related to expenditure may be greater than the risk of material misstatements due to fraud related to revenue recognition". Public sector auditors therefore need to consider whether they have any significant concerns about fraudulent financial reporting of expenditure which would need to be treated as a significant risk for the audit. We have assessed the significant expenditure streams of the Council and the risk of material misstatement arising from inappropriate expenditure recognition has a low likelihood of occurrence and is unlikely to be of a size which would be material to the users of the financial statements. Therefore we do not consider this to be a significant risk for the Council or the Pension Fund.	
Management over-ride of controls	**Council and Pension Fund**	Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities. In particular journals, management estimates and transactions outside the course of business are areas susceptible to management override.	We will: • evaluate the design effectiveness of management controls over journals • analyse the journals listing and determine the criteria for selecting high risk unusual journals • test unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration • gain an understanding of the accounting estimates and critical judgements applied made by management and consider their reasonableness with regard to corroborative evidence • evaluate the rationale for any changes in accounting policies, estimates or significant unusual transactions.

3. Significant risks identified – continued

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Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
Valuation of land and buildings	**Council only**	The Council revalues its land and buildings on a rolling four-yearly basis. Council dwellings are revalued annually. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved (£1.6 billion) and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the Council's financial statements is not materially different from the current value or the fair value (for surplus assets) at the financial statements date, where a rolling programme is used. Management have engaged the services of a valuer, Wilks Head and Eve, to estimate the current value as at 31 March 2020. We therefore identified valuation of land and buildings, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement.	We will: • Evaluate management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work; • evaluate the competence, capabilities and objectivity of the valuation expert; • write to the valuer to confirm the basis on which the valuation was carried out to ensure that the requirements of the Code are met; • engage our own valuer, Gerald Eve, to assess the instructions to the Council's valuer, the Council's valuer's report and the assumptions that underpin the valuation; • test revaluations made during the year to determine whether they had been input correctly into the Council's asset register; • assess the value of a sample of assets in relation to market rates for comparable properties; • evaluate the assumptions made by management for any assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value; and • test a sample of beacon properties in respect of council dwellings to consider whether their valuation assumptions are appropriate and whether they are truly representative of the other properties within that beacon group.

3. Significant risks identified – continued

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Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
Valuation of the net pension liability	**Council only**	The Council's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements. The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£624 million in the Council's balance sheet) and the sensitivity of the estimate to changes in key assumptions.	We will: • update our understanding of the processes and controls put in place by management to ensure that the Council's pension fund net liability is not materially misstated and evaluate the design of the associated controls; • evaluate the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work; • assess the competence, capabilities and objectivity of the actuary who carried out the Council's pension fund valuation; • assess the reasonableness of the actuary's assumptions and calculations in-line with the relevant standards, including their consideration of the ongoing impact of the McCloud and Guaranteed Minimum Pension cases; • assess the accuracy and completeness of the information provided by the Council to the actuary to estimate the liability; • test the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary; and • undertake procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report.

3. Significant risks identified – continued

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Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
Valuation of level 3 investments	**Pension Fund only**	The Pension Fund values its investments on an annual basis to ensure that the carrying value is not materially different from the fair value at the financial statements date. By their nature Level 3 investment valuations lack observable inputs. These valuations therefore represent a significant estimate by management in the financial statements due to the size of the numbers involved (£77 million) and the sensitivity of this estimate to changes in key assumptions Under ISA 315 significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end. Management utilise the services of investment managers and/or custodians as valuation experts to estimate the fair value as at 31 March 2020.	We will: • Evaluate management's processes for valuing Level 3 investments • Review the nature and basis of estimated values and consider what assurance management has over the year end valuations provided for these types of investments; to ensure that the requirements of the Code are met • Independently request year-end confirmations from investment managers and/or custodian(s) • For a sample of investments, test the valuation by obtaining and reviewing the audited accounts, (where available) at the latest date for individual investments and agreeing these to the fund manager reports at that date. Reconcile those values to the values at 31 March 2020 with reference to known movements in the intervening period and • In the absence of available audited accounts, we will evaluate the competence, capabilities and objectivity of the valuation expert • Test revaluations made during the year to see if they had been input correctly into the Pension Fund's asset register • Where available review investment manager service auditor report on design effectiveness of internal controls.

We will communicate significant findings on these areas as well as any other significant matters arising from the audit to you in our Audit Findings Report in July 2020.

4. Other risks identified

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Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
International Financial Reporting Standard (IFRS) 16 Leases – (issued but not adopted)	**Council**	The public sector will implement this standard from 1 April 2020. It will replace IAS 17 Leases, and the three interpretations that supported its application (IFRIC 4, Determining whether an Arrangement contains a Lease, SIC-15, Operating Leases – Incentives, and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease). Under the new standard the current distinction between operating and finance leases is removed for lessees and, subject to certain exceptions, lessees will recognise all leases on their balance sheet as a right of use asset and a liability to make the lease payments. In accordance with IAS 8 and paragraph 3.3.4.3 of the Code disclosures of the expected impact of IFRS 16 should be included in the Authority's 2019/20 financial statements. The Code adapts IFRS 16 and requires that the subsequent measurement of the right of use asset where the underlying asset is an item of property, plant and equipment is measured in accordance with section 4.1 of the Code.	We will: • Evaluate the processes the Authority has adopted to assess the impact of IFRS16 on its 2020/21 financial statements and whether the estimated impact on assets, liabilities and reserves has been disclosed in the 2019/20 financial statements. • Assess the completeness of the disclosures made by the Authority in its 2019/20 financial statements with reference to The Code and CIPFA/LASAAC Local Authority Leasing Briefings.

We will communicate significant findings on these areas as well as any other significant matters arising from the audit to you in our Audit Findings Report in July 2020.

5. Other matters

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Other work – Council

In addition to our responsibilities under the Code of Practice, we have a number of other audit responsibilities, as follows:

- We read the Council's Narrative Report and Annual Governance Statement and any other information published alongside the financial statements, to check that they are consistent with the financial statements on which we give an opinion and consistent with our knowledge of the Council
- We carry out work to satisfy ourselves that disclosures made in the Annual Governance Statement are in line with the guidance issued by CIPFA
- We carry out work on the Council's consolidation schedules for the Whole of Government Accounts process in accordance with NAO group audit instructions
- We consider our other duties under the Local Audit and Accountability Act 2014 (the Act) and the Code, as and when required, including:
    - Giving electors the opportunity to raise questions about your 2019/20 financial statements, consider and decide upon any objections received in relation to the 2019/20 financial statements
    - Issue of a report in the public interest or written recommendations to the Authority under section 24 of the Act, copied to the Secretary of State
    - Application to the court for a declaration that an item of account is contrary to law under Section 28 or for a judicial review under Section 31 of the Act or
    - Issuing an advisory notice under Section 29 of the Act.
- We certify completion of our audit.

Other work – Pension Fund

The Pension Fund is administered by the London Borough of Hammersmith and Fulham (the 'Council'), and the Pension Fund's accounts form part of the Council's financial statements.

Therefore, as well as our general responsibilities under the Code of Practice a number of other audit responsibilities also follow in respect of the Pension Fund, such as:

- We read any other information published alongside the Council's financial statements to check that it is consistent with the Pension Fund's financial statements on which we give an opinion and is consistent with our knowledge of the Authority.
- We consider our other duties under legislation and the Code, as and when required, including:
    - Giving electors the opportunity to raise questions about your 2018/19 financial statements, consider and decide upon any objections received in relation to the 2018/19 financial statements;
    - Issue of a report in the public interest or written recommendations to the Fund under section 24 of the Act, copied to the Secretary of State.
    - Application to the court for a declaration that an item of account is contrary to law under Section 28 or for a judicial review under Section 31 of the Act; or
    - Issuing an advisory notice under Section 29 of the Act.
- We carry out work to satisfy ourselves on the consistency of the pension fund financial statements included in the pension fund annual report with the audited Pension Fund accounts.

Other material balances and transactions

Under International Standards on Auditing, "irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance and disclosure". All other material balances and transaction streams will therefore be audited. However, the procedures will not be as extensive as the procedures adopted for the risks identified in this report.

Going concern

As auditors, we are required to "obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the Council and Pension Fund's ability to continue as going concerns" (ISA (UK) 570). We will review management's assessment of the going concern assumption and material uncertainties in respect of both the Council and the Pension Fund,, and evaluate the disclosures in the financial statements.

6. Materiality

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The concept of materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law. Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Materiality for planning purposes

For the Council, we have determined financial statement materiality based on a proportion of the gross expenditure for the financial year. In the prior year we used the same benchmark. Materiality at the planning stage of our audit is £10m (PY £13m) for the Council, which equates to 1.42% of your prior year gross expenditure for the year. We design our procedures to detect errors in specific accounts at a lower level of precision which we have determined to be £0.1m for disclosures around Officers' Remuneration.

For the Pension Fund, we have determined financial statement materiality based on a proportion of the net assets for the financial year. In the prior year we used the same benchmark. Materiality at the planning stage of our audit is £10m (PY £18m) for the Pension Fund, which equates to 0.95% of your prior year net assets as at 31 March 2019. We design our procedures to detect errors in specific accounts at a lower level of precision which we have determined to be £0.1m for disclosures around the remuneration of Key Management Personnel.

The reduction in materiality compared to the previous year, in respect of both the Council and the Pension Fund, reflects the higher profile of local audit following external reviews such as those led by Sir John Kingman and Sir Tony Redman.

We reconsider planning materiality if, during the course of our audit engagement, we become aware of facts and circumstances that would have caused us to make a different determination of planning materiality.

Matters we will report to the Audit and Pensions Committee

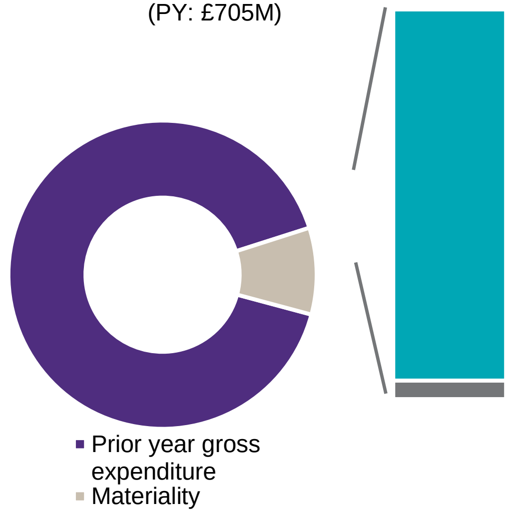
Whilst our audit procedures are designed to identify misstatements which are material to our opinions on the financial statements as a whole, we nevertheless report to the Audit and Pensions Committee any unadjusted misstatements of lesser amounts to the extent that these are identified by our audit work. Under ISA 260 (UK) 'Communication with those charged with governance', we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 (UK) defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. In the context of the Council, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.5m (PY £0.65m). In the context of the Pension Fund, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.5m (PY £0.9m).

If management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit and Pensions Committee to assist it in fulfilling its governance responsibilities.

Prior year gross expenditure

£702m Council

(PY: £705M)



Materiality

£10m

Authority financial statements materiality

(PY: £13m)

£0.5m

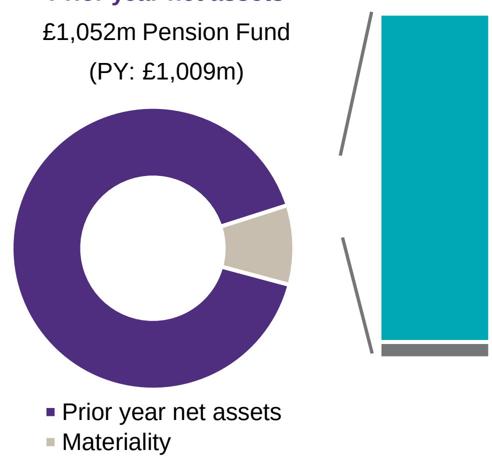
Misstatements reported to the Audit and Pensions Committee

(PY: £0.65m)

Prior year net assets

£1,052m Pension Fund

(PY: £1,009m)



Materiality

£10m

Pension Fund financial statements materiality

(PY: £18m)

£0.5m

Misstatements reported to the Audit and Pensions Committee

(PY: £0.9m)

7. Value for Money arrangements

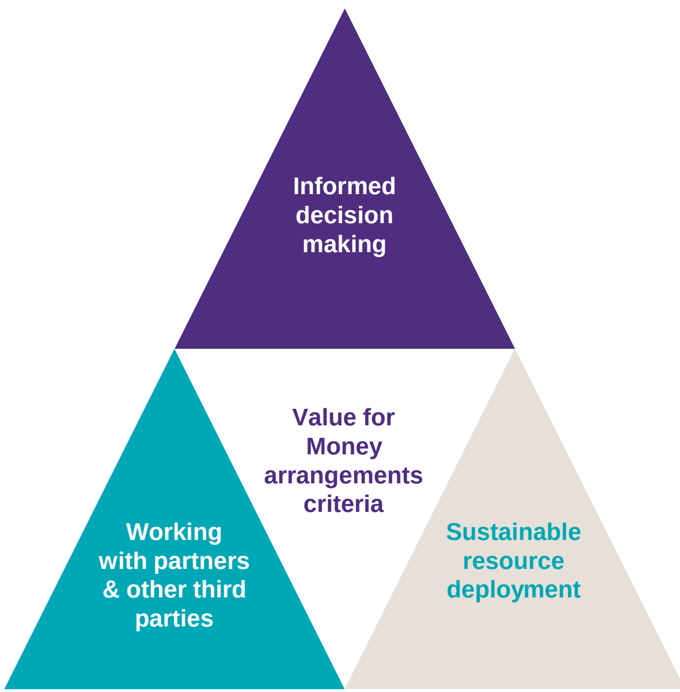
Background to our VFM approach

The NAO issued its guidance for auditors on Value for Money work in November 2017. The guidance states that for Local Government bodies, auditors are required to give a conclusion on whether the Authority has proper arrangements in place to secure value for money.

The guidance identifies one single criterion for auditors to evaluate:

"In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people."

This is supported by three sub-criteria, as set out below:



Significant VFM risks

Those risks requiring audit consideration and procedures to address the likelihood that proper arrangements are not in place at the Authority to deliver value for money.

Medium Term Financial Planning

You face a number of financial challenges over the both the short and medium term, including managing the impact of reductions in government funding, increasing demand for services, the impact of changes to business rates retention and the outcome of the Government's fairer funding review. You are currently forecasting a budget shortfall of £7.7 million for the year and although you are developing mitigating actions any shortfall will need to be met from reserves.

Part of your response to these challenges relates to increasing capital development and regeneration in the Borough, as well as internally considering issues such as work space for your employees and refining recruitment practices to enable you to better manage staffing costs.

Overspends predicted in the high needs school and early years block of the Dedicated Schools Grant, which remains the key area of pressure, will also be funded through reserves. You are beginning to make use of business information and data to aim to better understand the drivers of increasing costs.

A balanced budget has been set for 2020/21 although the four-year medium term financial forecast shows increasing budget gaps in future years, with a range of growth and savings proposals being proposed.

In response to this risk, we will:

- review the arrangements in place to monitor and report performance against budget and savings plans
- consider your arrangements for setting the Medium Term Financial Forecast and examine underlying assumptions and dependencies for robustness.
- examine the savings plans aimed at reducing future funding gaps, as well as likely outcomes from existing schemes in place.

We will continue our review of your arrangements, including reviewing the Council's Annual Governance Statement, before we issue our auditor's report.

8. Audit logistics & team

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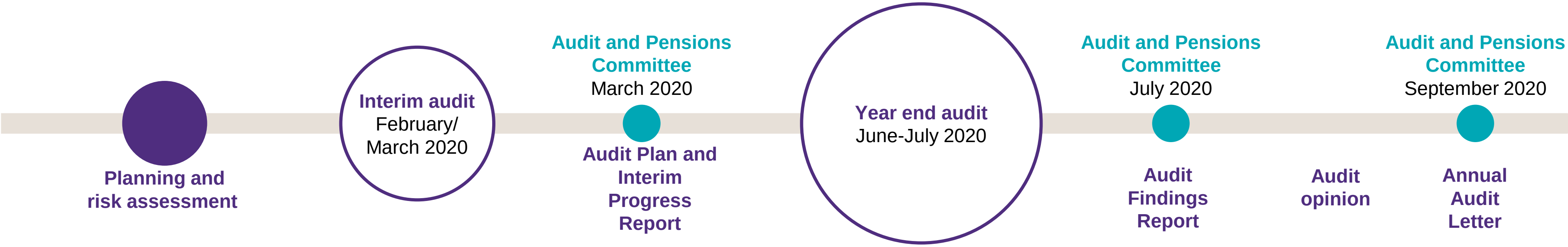

Paul Dossett, Key Audit Partner

Paul is the main point of contact for the Chief Executive, Director of Finance and Committee members. He will share his wealth of knowledge and experience across the sector providing challenge and sharing good practice. Paul will ensure our audit is tailored specifically to you, and he is responsible for the overall quality of our audit work. Paul will sign your audit opinion.

Ellen Millington, Manager

Ellen works with the senior members of the finance team ensuring early delivery of testing and agreement of accounting issues on a timely basis. Ellen will attend Audit and Pensions Committees, undertake reviews of the team's work and draft reports, ensuring they remain clear, concise and understandable. Ellen will be responsible for the delivery of our work on your arrangements in place to secure value for money.

Tanyaradzwa Chikari, Assistant Manager

Tanyaradzwa will lead the onsite team and will be the day to day contact for the audit. She will monitor the deliverables, manage the query log with your finance team and highlight any significant issues and adjustments to senior management. Tanyaradzwa will undertake the more technical aspects of the audit, coach the junior members of the team and review the team's work.

Client responsibilities

Where clients do not deliver to the timetable agreed, we need to ensure that this does not impact on audit quality or absorb a disproportionate amount of time, thereby disadvantaging other clients. Where the elapsed time to complete an audit exceeds that agreed due to a client not meeting its obligations we will not be able to maintain a team on site. Similarly, where additional resources are needed to complete the audit due to a client not meeting their obligations we are not able to guarantee the delivery of the audit to the agreed timescales. In addition, delayed audits will incur additional audit fees.

Our requirements

To minimise the risk of a delayed audit, you need to ensure that you:

- produce draft financial statements of good quality by the deadline you have agreed with us, including all notes, the narrative report and the Annual Governance Statement
- ensure that good quality working papers are available at the start of the audit, in accordance with the working paper requirements schedule that we have shared with you
- ensure that the agreed data reports are available to us at the start of the audit and are reconciled to the values in the accounts, in order to facilitate our selection of samples
- ensure that all appropriate staff are available on site throughout (or as otherwise agreed) the planned period of the audit
- respond promptly and adequately to audit queries.

9. Audit fees

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Planned audit fees 2019/20

- Across all sectors and firms, the FRC has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge and to undertake additional and more robust testing. Within the public sector, where the FRC has recently assumed responsibility for the inspection of local government audit, the regulator requires that all audits achieve a 2A (few improvements needed) rating.

Our work across the sector in 2018/19 has highlighted areas where local government financial reporting, in particular, property, plant and equipment and pensions, needs to be improved. We have also identified an increase in the complexity of local government financial transactions. Combined with the FRC requirement that 100% of audits achieve a 2A rating this means that additional audit work is required. We have set out below the expected impact on our audit fee. The table overleaf provides more details about the areas where we will be undertaking further testing.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and local government financial reporting. Our proposed work and fee for 2019/20 at the planning stage, as set out below and with further analysis overleaf, has been discussed with the Strategic Director, Finance and Governance and is subject to PSAA agreement.

	Actual Fee 2017/18	Actual Fee 2018/19	Proposed fee 2019/20
Council Audit	£163,950	£140,242	£152,242
Pension Fund Audit	£21,000	£16,170	£25,000
Audit of Wormwood Scrubs Charitable Trust	£9,900	£15,015	£TBC
Total audit fees (excluding VAT)	**£175,950**	**£171,427**	**£TBC**

Assumptions:

In setting the above fees, we have assumed that the Authority will:

- prepare a good quality set of accounts, supported by comprehensive and well presented working papers which are ready at the start of the audit
- provide appropriate analysis, support and evidence to support all critical judgements and significant judgements made during the course of preparing the financial statements
- provide early notice of proposed complex or unusual transactions which could have a material impact on the financial statements.

Relevant professional standards:

In preparing our fee estimate, we have had regard to all relevant professional standards, including paragraphs 4.1 and 4.2 of the FRC's Ethical Standard which stipulate that the Engagement Lead (Key Audit Partner) must set a fee sufficient to enable the resourcing of the audit with staff of appropriate skills, time and abilities to deliver an audit to the required professional standard.

Audit fee variations – Further analysis – Council

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Planned audit fees

The table below shows the planned variations to the original scale fee for 2019/20 based on our best estimate at the audit planning stage. Further issues identified during the course of the audit may incur additional fees. In agreement with PSAA (where applicable) we will be seeking approval to secure these additional fees for the remainder of the contract via a formal rebasing of your scale fee to reflect the increased level of audit work required to enable us to discharge our responsibilities. Should any further issues arise during the course of the audit that necessitate further audit work additional fees will be incurred, subject to PSAA approval.

Audit area	£	Rationale for fee variation
Scale fee	126,242	
Raising the bar	6,500	The Financial Reporting Council (FRC) has highlighted that the quality of work by all audit firms needs to improve across local audit. This will require additional supervision and leadership, as well as additional challenge and scepticism in areas such as journals, estimates, financial resilience and information provided by the entity. As outlined earlier in the Plan, we have also reduced the materiality level, reflecting the higher profile of local audit. This will entail an increase in scoped items and sample sizes selected for testing.
Pensions – valuation of net pension liabilities under International Auditing Standard (IAS) 19	4,000	We have increased the granularity, depth and scope of coverage, with increased levels of sampling, additional levels of challenge and explanation sought, and heightened levels of documentation and reporting.
PPE Valuation – work of experts	9,500	We have therefore engaged our own auditor's expert – Gerald Eve and increased the volume and scope of our audit work to ensure an adequate level of audit scrutiny and challenge over the assumptions that underpin PPE valuations]. The increase includes an estimate for the fee payable to the auditor's expert. We estimate that the cost of the auditors expert will be in the region of £5,000.
Changes in accounting standards including IFRS 16	3,000	IFRS 16 – Leases – will be implemented across the public sector with effect from 1 April 2020. This will require the recognition of an additional lease liability along with a corresponding right of use asset on the Authority's balance sheet. In 2019/20, the financial statements will need to contain the anticipated impact on transition, which from an audit perspective will include assessment of the Authority's processes and controls in place for ensuring completeness of recorded leases falling within the scope of the standard, including those held at a peppercorn rent, as well as lease terms where this is not clear from the contract; assessment of the recognition of the lease liability, including the Authority's determination of its incremental borrowing rate for each asset in order to discount the future cash flows appropriately.
Revised scale fee (to be approved by PSAA)	**152,242**	

Audit fee variations – Further analysis – Pension Fund

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Audit area	£	Rationale for fee variation
Scale fee	16,170	
Raising the bar	5,000	The Financial Reporting Council (FRC) has highlighted that the quality of work by all audit firms needs to improve across local audit. This will require additional supervision and leadership, as well as additional challenge and scepticism in areas such as journals, estimates, financial resilience and information provided by the entity.
Valuation of level 3 investments	3,830	The Financial Reporting Council (FRC) has highlighted that the quality of work by all audit firms in respect of valuations of hard to value investments needs to improve across the sector. Accordingly, we plan to enhance the scope and coverage of our work to ensure an adequate level of audit scrutiny and challenge over the assumptions and evidence that underpin the valuations of level 3 investments this year to reflect the expectations of the FRC and ensure we issue a safe audit opinion.
Revised scale fee (to be approved by PSAA)	**25,000**	

10. Independence & non-audit services

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Auditor independence

Ethical Standards and ISA (UK) 260 require us to give you timely disclosure of all significant facts and matters that may bear upon the integrity, objectivity and independence of the firm or covered persons relating to our independence. We encourage you to contact us to discuss these or any other independence issues with us. We will also discuss with you if we make additional significant judgements surrounding independence matters.

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements.

We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements. Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in December 2017 and PSAA's Terms of Appointment which set out supplementary guidance on ethical requirements for auditors of local public bodies.

Other services provided by Grant Thornton

For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The following other services were identified:

Service	£	Threats	Safeguards
Audit related:			
Certification of Housing Benefits subsidy claim	TBC	Self-Interest (because this is a recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is low in comparison to the total fee for the audit of the Council in 2018/19 of £140,242 and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level.
Agreed upon procedures engagement relating to the Teachers' Pensions End of Year Certificate	4,000	As above	As above
Agreed upon procedures engagement relating to Pooling of Housing Capital Receipts	4,000	As above	As above
Non-audit related:			
CFO Insights subscription	12,500	As above	As above

10. Independence & non-audit services – continued

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No non-audit services were identified in respect of the Pension Fund.

The amounts detailed are fees agreed to-date for audit related and non-audit services to be undertaken by Grant Thornton UK LLP in the current financial year. These services are consistent with the Council's policy on the allotment of non-audit work to your auditors. All services have been approved by the Audit and Pensions Committee. Any changes and full details of all fees charged for audit related and non-audit related services by Grant Thornton UK LLP and by Grant Thornton International Limited network member Firms will be included in our Audit Findings report at the conclusion of the audit. None of the services provided are subject to contingent fees. The firm is committed to improving our audit quality – please see our transparency report - https://www.grantthornton.co.uk/globalassets/1.-member-firms/united-kingdom/pdf/annual-reports/interim-transparency-report-2019.pdf

Appendices

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A. Audit Quality – national context

Appendix A: Audit Quality – national context

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What has the FRC said about Audit Quality?

The Financial Reporting Council (FRC) publishes an annual Quality Inspection of our firm, alongside our competitors. The Annual Quality Review (AQR) monitors the quality of UK Public Interest Entity audits to promote continuous improvement in audit quality.

All of the major audit firms are subject to an annual review process in which the FRC inspects a small sample of audits performed from each of the firms to see if they fully conform to required standards.

The most recent report, published in July 2019, shows that the results of commercial audits taken across all the firms have worsened this year. The FRC has identified the need for auditors to:

- improve the extent and rigour of challenge of management in areas of judgement
- improve the consistency of audit teams' application of professional scepticism
- strengthen the effectiveness of the audit of revenue
- improve the audit of going concern
- improve the audit of the completeness and evaluation of prior year adjustments.

The FRC has also set all firms the target of achieving a grading of '2a' (limited improvements required) or better on all FTSE 350 audits. We have set ourselves the same target for public sector audits from 2019/20.

Other sector wide reviews

Alongside the FRC, other key stakeholders including the Department for Business, energy and Industrial Strategy (BEIS) have expressed concern about the quality of audit work and the need for improvement. A number of key reviews into the profession have been undertaken or are in progress. These include the review by Sir John Kingman of the Financial Reporting Council (Dec 2018), the review by the Competition and Markets authority of competition within the audit market, the ongoing review by Sir Donald Brydon of external audit, and specifically for public services, the Review by Sir Tony Redmond of local authority financial reporting and external audit. As a firm, we are contributing to all these reviews and keen to be at the forefront of developments and improvements in public audit.

What are we doing to address FRC findings?

In response to the FRC's findings, the firm is responding vigorously and with purpose. As part of our Audit Investment Programme (AIP), we are establishing a new Quality Board, commissioning an independent review of our audit function, and strengthening our senior leadership at the highest levels of the firm, for example through the appointment of Fiona Baldwin as Head of Audit. We are confident these investments will make a real difference.

We have also undertaken a root cause analysis and put in place processes to address the issues raised by the FRC. We have already implemented new training material that will reinforce the need for our engagement teams to challenge management and demonstrate how they have applied professional scepticism as part of the audit. Further guidance on auditing areas such as revenue has also been disseminated to all audit teams and we will continue to evolve our training and review processes on an ongoing basis.

What will be different in this audit?

We will continue working collaboratively with you to deliver the audit to the agreed timetable whilst improving our audit quality. In achieving this you may see, for example, an increased expectation for management to develop properly articulated papers for any new accounting standard, or unusual or complex transactions. In addition, you should expect engagement teams to exercise even greater challenge management in areas that are complex, significant or highly judgmental which may be the case for accounting estimates, going concern, related parties and similar areas. As a result you may find the audit process even more challenging than previous audits. These changes will give the audit committee – which has overall responsibility for governance - and senior management greater confidence that we have delivered a high quality audit and that the financial statements are not materially misstated. Even greater challenge of management will also enable us to provide greater insights into the quality of your finance function and internal control environment and provide those charged with governance confidence that a material misstatement due to fraud will have been detected.

We will still plan for a smooth audit and ensure this is completed to the timetable agreed. However, there may be instances where we may require additional time for both the audit work to be completed to the standard required and to ensure management have appropriate time to consider any matters raised. This may require us to agree with you a delay in signing the announcement and financial statements. To minimise this risk, we will keep you informed of progress and risks to the timetable as the audit progresses.

We are absolutely committed to delivering audit of the highest quality and we should be happy to provide further detail about our improvement plans should you require it.

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