Stevenage Borough Council
Audit Planning Report

Year ended 31 March 2021

February 2022

Building a better working world

Stevenage Borough Council
Daneshill House
Danestrete
Stevenage
SG1 1HN

26 January 2023

Dear Members of the Audit Committee,

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as your auditor. Its purpose is to provide the Audit Committee with a basis to review our proposed audit approach and scope for the 2020/21 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2020 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This Plan summarises our initial 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. Our planning procedures are still on-going and we will inform the Audit Committee and management if there are any significant changes or revisions once we have completed these procedures.

This report is intended solely for the information and use of the Audit 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 report with you at the 7 February 2023 Audit Committee meeting as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Debbie Hanson

For and on behalf of Ernst & Young LLP

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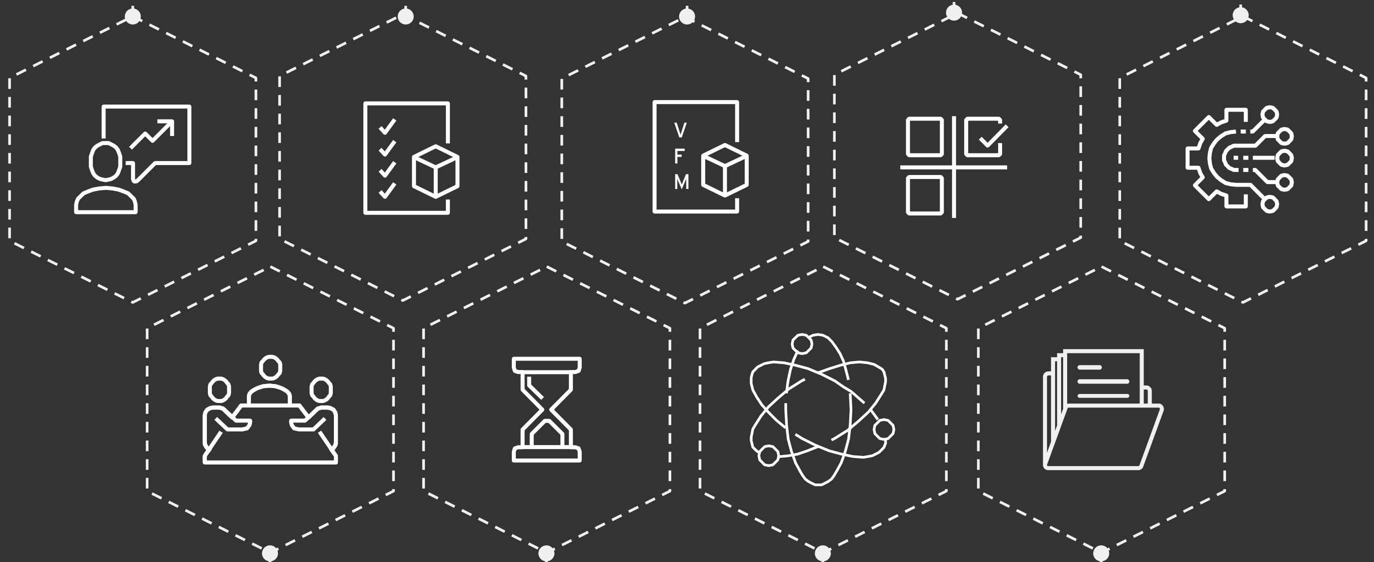


Public Sector Audit Appointments Ltd (PSAA) issued the "Statement of responsibilities of auditors and audited bodies". It is available from the PSAA website (https://www.psaa.co.uk/managing-audit-quality/statement-of-responsibilities-of-auditors-and-audited-bodies/).The Statement of responsibilities 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 and further guidance (updated July 2021)" issued by the PSAA (https://www.psaa.co.uk/managing-audit-quality/terms-of-appointment/terms-of-appointment-and-further-guidance-1-july-2021/) 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 in legislation, and covers matters of practice and procedure which are of a recurring nature.

This report is made solely to the Audit Committee and management of the Stevenage Borough Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee and management of Stevenage Borough Council those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit Committee and management of Stevenage Borough Council for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.

01 Overview of our 2020/21 audit strategy

Overview of our 2020/21 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Risk / area of focus	Risk identified	Change from PY	Details
Misstatements due to fraud or error (Risk of management override)	Fraud Risk	**No change** in risk or focus	As identified in ISA 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 would otherwise appear to be operating effectively. In addition to our overall response, we consider where these risks may manifest themselves and identify separate fraud risks as necessary below.
Inappropriate classification of revenue spend as capital	Fraud Risk	**No change** in risk or focus	As noted above, we have considered the main areas where management may have the incentive and opportunity to do override controls. We have identified the inappropriate capitalisation of revenue expenditure on property, plant and equipment as an area of risk, given the extent of the Council's capital programme and regeneration schemes.
Incorrect accounting for financing of capital regeneration schemes	Significant Risk	**New risk**	The Council has a number of highly material capital schemes aimed at the regeneration and revitalisation of Stevenage town centre. In particular for 2020/21 the Council received £9.6m of LEP funding in relation to the new bus interchange in Stevenage town centre. Given the material misstatement identified and subsequently corrected during the 2019/20 audit in relation to LEP financing of capital schemes, there is a risk that the accounting of the funding of the capital regeneration projects is incorrect within the 2020/21 financial statements.
Valuation of market based property assets (including property, plant and equipment, Council dwellings and investment properties)	Significant Risk	**No change** in risk or focus	The Council has highly material property assets that are valued on a market basis (including property, plant and equipment, Council dwellings and investment properties). The valuation of such assets is a significant accounting estimate that, in the context of an uncertain economic environment as a result of Covid, has a material impact on the financial statements. The Council engages property valuation specialists to determine asset valuations. Small changes in assumptions when valuing these assets can have a material impact on the financial statements. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of experts and assumptions underlying fair value estimates.

Overview of our 2020/21 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Risk / area of focus	Risk identified	Change from PY	Details
Valuation of property, plant and equipment assets under depreciated replacement cost (DRC) model	Inherent Risk	**No change** in risk or focus	Property, plant and equipment (PPE) represents a significant balance in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Material judgemental inputs and estimation techniques are required to calculate the year-end PPE balances held in the balance sheet. For assets valued using depreciated replacement cost (DRC) this risk is heightened due to the specialised nature of the assets and the risk of insufficient availability of market-based evidence to assist the valuation. As the Council's DRC asset base is significant, and the outputs from the valuer are subject to estimation, there is an inherent risk that PPE may be under/overstated.
Queensway lease accounting treatment	Inherent Risk	**No change** in risk or focus	In preparing Queensway LLP financial statements significant judgements are taken in relation to the lease accounting treatment. In our 2019/20 audit, a number of amendments were made to the group financial statements due to the incorrect split of lease repayment amounts between principal and interest in the model used.
Preparation of group accounts	No Risk	**Removal of the risk for 2020/21**	The financial statement of Queensway LLP have been consolidated since 2018/19. During our audit we have not noted significant issue arsing from the Council's group accounts consolidation procedures and process. Thus, we have removed the inherent risk attached in the preparation of group accounts.

Overview of our 2020/21 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Risk / area of focus	Risk identified	Change from PY	Details
Pension liability valuation	Inherent Risk	**No change** in risk or focus	The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding the Local Government Pension Scheme (LGPS) in which it is an admitted body. The Council's current pension fund deficit is a material and sensitive item and the Code requires that this liability be disclosed on the Council's balance sheet. The information disclosed is based on the IAS 19 report issued to the Council by the Actuary. Accounting for this scheme involves significant estimation and judgement and due to the nature, volume and size of the transactions, in the current uncertain economic environment, we consider this to be a higher inherent risk. In addition, every three years, a formal valuation of the whole fund in carried out in accordance with the LGPS Regulations 2013 to assess and examine the ongoing financial position of the fund.
Recognition of grant income associated with Covid-19	Inherent Risk	**No change** in risk or focus	The Council has received additional funding in the form of grants as a result of Covid-19 amounting to £22.4 million (of which (£17.5 million was paid to business and residents and £4.9 million was covid funding). Whilst there is no change in the CIPFA Code or accounting standard (IFRS 15) in respect of accounting for grant funding, the emergency nature of some of the grants received and in some cases the lack of clarity on any associated restrictions and conditions, means that the Council will need to apply a greater degree of assessment and judgement to determine the appropriate accounting treatment in the 2020/21 statements, and therefore a risk of error. We will consider the elements of grant income and their susceptibility to error as part of our audit and ensure the Council has correctly assessed whether it is acting as principal or agent and whether any conditions attached have also been appropriately considered.
Going concern disclosures	Inherent Risk	**No change** in risk or focus	This auditing standard has been revised in response to enforcement cases and well-publicised corporate failures where the auditor's report failed to highlight concerns about the prospects of entities which collapsed shortly after. The revised standard is effective for audits of financial statements for periods commencing on or after 15 December 2019, which for Stevenage Borough Council is the audit of the 2020/21 financial statements. The revised standard increases the work we are required to perform when assessing whether the Council is a going concern. It means UK auditors will follow significantly stronger requirements than those required by current international standards; and we have therefore judged it appropriate to bring this to the attention of the Audit Committee.

Overview of our 2020/21 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Risk / area of focus	Risk identified	Change from PY	Details
Infrastructure asset accounting	Inherent Risk	New risk	In March 2022, an issue was raised with the National Audit Office's Local Government technical network in relation to the accounting for infrastructure assets which are held at depreciated historic cost. Following more detailed consideration, it has been identified that although local authorities add expenditure incurred on replacing or enhancing such assets, most do not appear to be considering the Cipfa Code requirement to establish whether this spend is a replacement of an asset, or a recognised component, and therefore are not derecognising the old asset or component. As a consequence, the gross cost and gross accumulated depreciation are continually increasing and the notes to the financial statements may be misstated where the expenditure is a replacement for an asset/component that is not fully depreciated. Cipfa established a task and finish group to address this issue. The Department to Levelling Up, Housing and Communities (DLUHC) and Cipfa have worked on a sector wide approach to resolution of the reporting of infrastructure assets. Following consultations with FRAB, local councils, ICAEW and external audit firms, a resolution has been agreed which has two elements: 1) Cipfa have issued an adaptation to the Code of Practice on Local Authority Accounting. 2) DLUHC have issued a Statutory Instrument (The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2022). The Code allows for infrastructure assets to be reported in the notes to the accounts on a net basis. The SI allows for the infrastructure assets opening balance to be brought forward without amendment and determines the carrying amount to be derecognised in respect of replaced components to be nil. The Council plans to apply both the Code update and the SI to the 2020/21 financial statements. As at 31 March 2021, infrastructure assets were reported with a gross cost of £8.31 million and accumulated depreciation and impairment of £5.34 million.

Overview of our 2020/21 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Risk / area of focus	Risk identified	Change from PY	Details
Impact of non-compliance with the minimum decent home standards	Inherent Risk	New risk	In 2022, the Council was subject to a referral to the Housing Regulator in relation to non-compliance with the minimum decent home standards in a number of areas. The Council has been working with the regulator since the referral was made and has received a response to the action plan they have put in place to address the areas of non-compliance identified. Depending on the time at which the Council's housing stock fell below these minimum standards and the nature of the non-compliance, this may have an impact on valuation of the Council's dwellings. In addition, a consideration regarding whether a provision should be recorded in the accounts to reflect the works required to comply with the standard. Management will therefore need to undertake an assessment of compliance during 2020/21 (as well as 2019/20) to clearly establish the fact pattern and consider the potential impact on these two areas in the financial statements.

Overview of our 2020/21 audit strategy

Materiality

Planning materiality

£2.04m

Materiality for the Council's financial statements has been set at £2.04 million, which represents 2.0% of the 2020/21 gross expenditure of the Council. The use of 2% of gross expenditure has increased from the level we used in the prior year which was set at 1%. This reflects the reduction in our assessment of the risk profile of the Council and its business. Our assessment of risk was increased in the prior year, and materiality reduced accordingly, as a result of the financial pressures being faced by the Council at the time as a result of the impact of Covid on their income streams.

Performance materiality

£1.02m

Performance materiality has been set at £1.02 million (2019/20: £833,000), which represent 50% of materiality. This is a reduction from the prior year when we used 75% of materiality and reflects our assessment of an increased risk of errors in the 2020/21 financial statements.

Audit differences

£102k

We will report all uncorrected misstatements relating to the primary statements (comprehensive income and expenditure statement, balance sheet, movement in reserves statement, cash flow statement, and collection fund) greater than £102,000 (2019/20: £55,500). Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

Overview of our 2020/21 audit strategy

Audit scope

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

- Our audit opinion on whether the financial statements of Stevenage Borough Council give a true and fair view of the financial position as at 31 March 2021 and of the income and expenditure for the year then ended; and

- Our commentary on your arrangements to secure value for money in your use of resources for the relevant period. We include further details on VFM in Section 03.

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.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

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.

Taking the above into account, and as articulated in this audit plan, our professional responsibilities require us to independently assess the risks associated with providing an audit opinion and undertake appropriate procedures in response to that. Our Terms of Appointment with PSAA allow them to vary the fee dependent on "the auditors assessment of risk and the work needed to meet their professional responsibilities". PSAA are aware that the setting of scale fees has not kept pace with the changing requirements of external audit with increased focus on, for example, the valuations of land and buildings, the auditing of groups, the valuation of pension obligations, the introduction of new accounting standards such as IFRS 9 and 15 in recent years as well as the expansion of factors impacting the ISA 540 (revised) and the value for money conclusion. Therefore to the extent any of these or any other risks are relevant in the context of Stevenage Borough Council's audit, we will discuss these with management as to the impact on the scale fee.

Effects of climate-related matters on financial statements and Value for Money arrangements
Public interest in climate change is increasing. We are mindful that climate-related risks may have a long timeframe and therefore while risks exist, the impact on the current period financial statements may not be immediately material to an entity. It is nevertheless important to understand the relevant risks to make this evaluation. In addition, understanding climate-related risks may be relevant in the context of qualitative disclosures in the notes to the financial statements and value for money arrangements.

We make inquiries regarding climate-related risks on every audit as part of understanding the entity and its environment. As we re-evaluate our risk assessments throughout the audit, we continually consider the information that we have obtained to help us assess the level of inherent risk.

Overview of our 2020/21 audit strategy

Value for money

We include details in Section 03 but in summary:

- We are required to consider whether the Council has made 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources.
- Planning on value for money and the associated risk assessment is focused on gathering sufficient evidence to enable us to document our evaluation of the Council's arrangements, to enable us to draft a commentary under three reporting criteria (see below). This includes identifying and reporting on any significant weaknesses in those arrangements and making appropriate recommendations.
- We will provide a commentary on the Council's arrangements against three reporting criteria:
  - Financial sustainability - How the Council plans and manages its resources to ensure it can continue to deliver its services;
  - Governance - How the Council ensures that it makes informed decisions and properly manages its risks; and
  - Improving economy, efficiency and effectiveness - How the Council uses information about its costs and performance to improve the way it manages and delivers its services.
- The commentary on VFM arrangements will be included in the Auditor's Annual Report.
- Our VFM risk assessment in the prior year identified a risk of significant weakness in relation to the Council's secure economy, efficiency and effectiveness in your use of resources.

Timeline

We are currently working with the Council to agree appropriate timelines for the delivery of the 2020/21 audit which will be the most efficient and effective for both the finance team and EY, taking into account other deadlines and in particular the 2022/23 financial closedown processes.

Audit team changes

Debbie Hanson will be the Engagement Partner and Karen Cunanan will be the Senior Manager of the engagement for 2020/21

02 Audit risks

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

	What is the risk?	What will we do?

Misstatements due to fraud or error*
 	
 (Management override)
	The financial statements as a whole are not free of material misstatements whether caused by fraud or error.
	
	 As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.
		We will:
		▶ Identify fraud risks during the planning stages.
		▶ Inquire of management about risks of fraud and the controls put in place to address those risks
		▶ Understand the oversight given by those charged with governance of management's processes over fraud
		▶ Consider of the effectiveness of management's controls designed to address the risk of fraud
		▶ Determine an appropriate strategy to address those identified risks of fraud
		▶ Perform mandatory procedures regardless of specifically identified fraud risks, including:
		    ▶ Testing of journal entries and other adjustments in the preparation of the financial statements;
		    ▶ reviewing accounting estimates for evidence of management bias; and
		    ▶ evaluating the business rationale for significant unusual transactions;

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Inappropriate classification of revenue spend as capital*

What is the risk?

In considering how the risk of management override may present itself, we conclude that this is primarily through management taking action to override controls and manipulate in year financial transactions that impact the medium to longer term financial position. A key way of improving the revenue position is through the inappropriate capitalisation of revenue expenditure.

Stevenage Borough Council has a significant fixed asset base and as a result has a significant capital programme of £70.81 million for 2020/21. Therefore, we have concluded there is a potential risk that revenue expenditure could be incorrectly classified as capital. Refcus (revenue expenditure financed from capital under statute) is reported as 1.275 million in the draft accounts and therefore there is also a risk that this could be overstated.

What will we do?

We will:

- Obtain a general ledger (GL) breakdown of capital additions in the year, reconcile to the Fixed Assets Register (FAR), and review the GL descriptions to identify whether there are any potential transactional items that could be revenue in nature;
- Sample test additions to property, plant and equipment at a lower testing threshold to ensure they have been correctly classified as capital and included at the correct value in order to identify any revenue items that have been inappropriately capitalised;
- Sample test Refcus expenditure at a lower testing threshold to ensure items are meet the definition of Refcus and have not been inappropriately classified within the financial statements;
- We will extend our testing of items capitalised in the year by lowering our testing threshold. We will also review a random sample of capital additions below our testing threshold;
- As part of our journal testing strategy, we will review unusual journals related to capital expenditure posted around the year-end; for example where the debit is to capital expenditure and the credit to income and expenditure.

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

	What is the risk?	What will we do?
Incorrect accounting for financing of capital regeneration schemes	The Council has a number of highly material capital schemes aimed at the regeneration and revitalisation of Stevenage town centre. In particular for 2020/21 the Council received £9.6m of LEP funding in relation to the new bus interchange in Stevenage town centre. Given the material misstatement identified and subsequently corrected during the 2019/20 audit in relation to LEP financing of capital schemes, there is a risk that the accounting of the funding of the capital regeneration projects is incorrect within the 2020/21 financial statements.	We will: ▸ Review the financial statements for how the financing of capital regeneration schemes have been accounted for. ▸ Confirm that the accounting treatment adopted is supported by the nature of the underlying funding agreements, e.g. with the Hertfordshire LEP, including if there are any conditions or repayment terms included into the agreement. ▸ Test receipt of capital funding to supporting bank statement evidences to verify that the financing of capital schemes has been accounted for in the correct financial period and any balances at the end of the financial year are appropriately reflected on the balance sheet.

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Valuation of market based property assets (including property, plant and equipment, Council dwellings and investment properties)

What is the risk?

The Council has highly material property assets valued on a market basis (including property, plant and equipment, Council dwellings and investment properties). The valuation of such assets is a significant accounting estimate that, in the context of an uncertain economic environment as a result of Covid, has a material impact on the financial statements.

The Council engages property valuation specialists to determine asset valuations and small changes in assumptions when valuing these assets can have a material impact on the financial statements.

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

What will we do?

We will:

- Test that assets have been classified and valued on an appropriate basis.
- Consider the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work;
- Sample test and challenge the key asset information and assumptions used by the valuers in performing their valuation; for example floor plans, price per square metre, yields, etc.
- Consider the annual cycle of valuations to ensure that assets have been valued within an appropriate timescale.
- Consider any specific changes to assets that have occurred and that these have been communicated to the valuer;
- Review assets not subject to valuation in 2020/21 to confirm that the remaining asset base is not materially misstated;
- Consider changes to useful economic lives as a result of the most recent valuation; and
- Test accounting entries have been correctly processed in the financial statements.

We will also engage EY valuation specialists to assist the audit team on a sample of assets, based on our assessment of the asset valuations subject to a higher degree of risk for their valuations as at 31 March 2021.

We will also consider how the Council's valuer has addressed the impact of Covid-19 in the year-end valuation of assets and assessment of impairments.

Other areas of audit focus

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

What is the risk/area of focus?	What will we do?
<u>Valuation of property, plant and equipment assets under depreciated replacement cost (DRC) model</u> Property, plant and equipment (PPE) represents a significant balance in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Material judgemental inputs and estimation techniques are required to calculate the year-end PPE balances held in the balance sheet. For assets valued using depreciated replacement cost (DRC) this risk is heightened due to the specialised nature of the assets and insufficient availability of market-based evidence to assist the valuation. As the Council's DRC asset base is significant, and the outputs from the valuer are subject to estimation, there is a significant risk PPE may be under/overstated or the associated accounting entries incorrectly posted.	We will: ▸ Consider the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work; ▸ Sample testing key asset information and assumptions used by the valuers in performing their valuation (e.g. gross internal area, build cost, depreciation adjustments, external works, professional fees and land values); ▸ Consider the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code. ▸ Consider if there are any specific changes to assets that have occurred and that these have been communicated to the valuer; ▸ Review assets not subject to valuation in 2020/21 to confirm that the remaining asset base is not materially misstated; ▸ Consider changes to useful economic lives as a result of the most recent valuation; and ▸ Test accounting entries have been correctly processed in the financial statements. Involved EY Valuation specialists to review sample of DRC asset valuations.
<u>Queensway Lease Accounting Treatment</u> In preparing Queensway LLP financial statements significant judgements are taken in relation to the lease accounting treatment. In our 2019/20 audit, a number of amendments were made to the group financial statements due to the incorrect split of lease repayment amounts between principal and interest in the model used.	We will: ▸ Review the lease accounting treatment adopted including follow up on points identified during the 2019/20. In particular the interest rates applied to the leasing and borrowing elements of the lease agreement and the split of repayment of principal and interest. ▸ Consider whether the appropriate accounting journal entries are consistent with the prevailing accounting standard IAS 17 Leases. ▸ Review the relevant lease disclosures in the Council's financial statements.

Other areas of audit focus

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

What is the risk/area of focus?	What will we do?
<u>Pension liability valuation</u> The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme (LGPS) in which it is an admitted body. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2021, this totalled £61.58 million. The information disclosed is based on the IAS 19 report issued to the Council by the actuary to the administering body. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	We will: ▸ Liaise with the auditors of Hertfordshire Pension Fund, to obtain assurances over the information supplied to the actuary in relation to the Stevenage Borough Council; ▸ Assess the work of the Pension Fund actuary (Hymans Robertson LLP) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by the National Audit Office for all Local Government sector auditors, and considering reviews by the EY actuarial team; ▸ Review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS19; ▸ Consider the nature and value of level 3 investments held by Hertfordshire Pension Fund and the proportion of the overall Fund relating to Stevenage Borough Council in order to identify any additional procedures required to support the estimates of the valuation of these asset as at 31 March 2021; and ▸ In response to the revised requirements of ISA540, the auditing standard on accounting estimates, we will engage an EY Pensions specialist to review the Council's IAS19 reports and run a parallel actuarial model which we will compare to that produced by the Council's actuary.

Other areas of audit focus

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

What is the risk/area of focus?	What will we do?
<u>Recognition of Grant Income associated with Covid-19</u> The Council has received additional funding in the form of grants as a result of the Covid-19 amounting to £22.40 million (of which £17.5 million was paid to business and residents and £4.9 million was covid funding). Whilst there is no change in the CIPFA Code or accounting standard (IFRS 15) in respect of accounting for grant funding, the emergency nature of some of the grants received and in some cases the lack of clarity on any associated restrictions and conditions, means that the Council will need to apply a greater degree of assessment and judgement to determine the appropriate accounting treatment in the 2020/21 statements, and therefore a risk of error. We will consider the elements of grant income and their susceptibility to error as part of our audit and ensure the Council has correctly assessed whether it is acting as principal or agent and whether any conditions attached have also been appropriately considered.	We will: ▸ Consider the revenue and capital grants received by the Council; ▸ Review the Council's judgement on material grants received in relation to whether it is acting as principal or agent, and assess the appropriateness of this judgement; ▸ Undertake substantive procedures to ensure that grants have been claimed and recognised in accordance with scheme rules and conditions; and ▸ Responsive to the risk, carry out testing to ensure the accounting treatment and recognition applied to grant income is appropriate.
<u>Going concern disclosures</u> There is a presumption that the Council will continue as a going concern for the foreseeable future. However, the Council is required to carry our a going concern assessment that is proportionate to the risks it faces. In light of the continued impact of Covid-19 on the Council's day to day finances, its annual budget, its cashflow and its medium term financial strategy, there is a need for the Council to ensure it's going concern assessment is thorough and appropriately comprehensive. The Council is then required to ensure that its going concern disclosure within the statement of accounts adequately reflects its going concern assessment and in particular highlights any uncertainties it has identified.	We will meet the requirements of auditing standard on going concern (ISA 570) and consider the adequacy of the Council's going concern assessment and its disclosure in the accounts by: ▸ Challenging management's identification of events or conditions impacting going concern; ▸ Testing management's resulting assessment of going concern by evaluating supporting evidence (including consideration of the risk of management bias); ▸ Reviewing the Council's cashflow forecast covering at least 1 months from the expected date of our audit report, to ensure that it has sufficient liquidity to continue to operate as a going concern; ▸ Undertaking a 'stand back' review to consider all of the evidence obtained, whether corroborative or contradictory, when we draw our conclusions on going concern; ▸ Challenging the disclosure made in the accounts in respect of going concern and any material uncertainties.

Other areas of audit focus

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

What is the risk/area of focus?	What will we do?
<u>Infrastructure asset accounting</u> In March 2022, an issue was raised with the National Audit Office's Local Government technical network in relation to the accounting for infrastructure assets which are held at depreciated historic cost. Following more detailed consideration, it has been identified that although local authorities add expenditure incurred on replacing or enhancing such assets, most do not appear to be considering the Cipfa Code requirement to establish whether this spend is a replacement of an asset, or a recognised component, and therefore are not derecognising the old asset or component. As a consequence, the gross cost and gross accumulated depreciation are continually increasing and the notes to the financial statements may be misstated where the expenditure is a replacement for an asset/component that is not fully depreciated. Cipfa established a task and finish group to address this issue. The Department to Levelling Up, Housing and Communities (DLUHC) and Cipfa have worked on a sector wide approach to resolution of the reporting of infrastructure assets. Following consultations with FRAB, local councils, ICAEW and external audit firms, a resolution has been agreed which has two elements: 1) Cipfa have issued an adaptation to the Code of Practice on Local Authority Accounting. 2) DLUHC have issued a Statutory Instrument (The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2022). The Code allows for infrastructure assets to be reported in the notes to the accounts on a net basis. The SI allows for the infrastructure assets opening balance to be brought forward without amendment and determines the carrying amount to be derecognised in respect of replaced components to be nil. The Council plans to apply both the Code update and the SI to the 2020/21 financial statements. As at 31 March 2021, infrastructure assets were reported with a gross cost of £8.31 million and accumulated depreciation and impairment of £5.34 million.	Following the guidance from Cipfa we will: ‣ Confirm with the Council the first financial year they are applying the statutory instrument. This should be a financial year beginning on or before 1st April 2024; and in respect of which a certificate has not been entered under section 20(2)(a) of that Act; ‣ Check the disclosure of infrastructure assets is in accordance with the Cipfa Code adaptation; ‣ Agree the opening balance for infrastructure assets to the closing balance on the prior year audited financial statements; ‣ Ensure the financial statements include a disclosure note setting out the application of the Code adaptation and SI; ‣ Ensure the accounting policies disclosed are consistent with this determination. As part of this we will ensure that that Council's accounting policies clearly set out how the Council is accounting for infrastructure assets. Accounting policies should include commentary on statutory prescriptions (if applied) and depreciation. Annex A of the Cipfa Bulletin on Infrastructure Assets (Jan 2023) provides an example accounting policy; ‣ Document how the SI provides assurance over all assertions for the opening balance as the Council is not required to make any prior period adjustment to the balances in the statement of accounts in respect of infrastructure assets, when preparing a statement of accounts to which the regulation applies; ‣ Test in year movements (additions, derecognition and depreciation) of infrastructure assets; and ‣ Consider management's assessment of whether the depreciation policy applied to derive the net book values is supportable and correctly applied. A key element of this will be the determination and application of the useful economic life (UE). The Cipfa Bulletin on Infrastructure Assets (issued in January 2023) provides further guidance to local authorities, including expert views on UEL ranges for different asset groups and illustrative examples for estimating depreciation.

Other areas of audit focus

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

What is the risk/area of focus?	What will we do?
<u>Impact on non-compliance with the minimum decent home standards</u> In 2022, the Council was subject to a referral to the Housing Regulator in relation to non-compliance with the minimum decent home standards in a number of areas. The Council has been working with the regulator since the referral was made and has received a response to the action plan they have put in place to address the areas of non-compliance identified. Depending on the time at which the Council's housing stock fell below these minimum standards and the nature of the non-compliance, this may have an impact on valuation of the Council's dwellings. In addition, a consideration regarding whether a provision should be recorded in the accounts to reflect the works required to comply with the standard. Management will therefore need to undertake an assessment of compliance during 2020/21 (as well as 2019/20) to clearly establish the fact pattern and consider the potential impact on these two areas in the financial statements.	We will: ‣ Obtain monitoring reports from management regarding the number of housing dwellings that are not meeting the Home Standard as at 31 March 2021; ‣ Obtain from management details of expenditure required to bring the dwellings back to the required standards and review and assess the reasonableness of the break down between capital and revenue expenditure; ‣ Obtain and review the assessment from management as to whether provision for required revenue works should be recorded as at 31 March 2021; and ‣ Obtain and review the assessment from management and the Council's valuers regarding how the non-compliance has been considered in the valuation of the council dwellings.

03 Value for Money Risks

Value for Money

The Council's responsibilities for value for money

The Council is required to maintain an effective system of internal control that supports the achievement of its policies, aims and objectives while safeguarding and securing value for money from the public funds and other resources at its disposal.

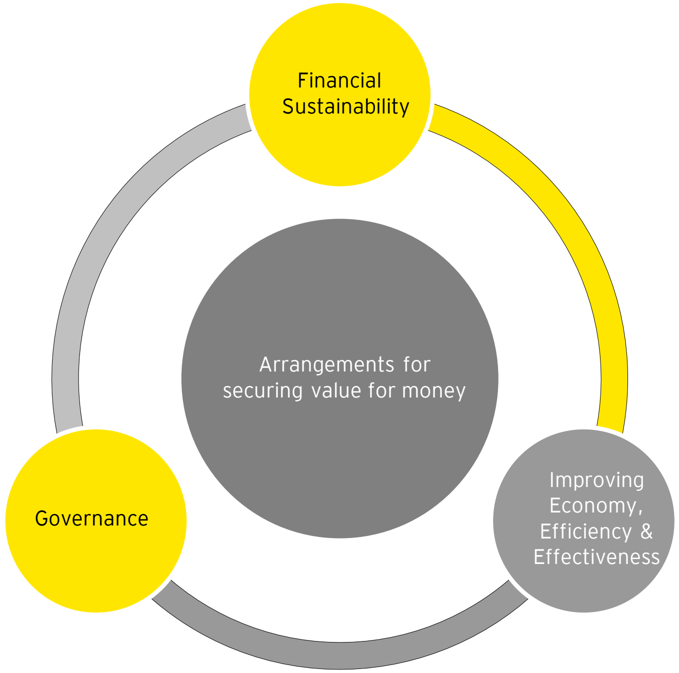
As part of the material published with the financial statements, the Council is required to bring together commentary on the governance framework and how this has operated during the period in a governance statement. In preparing the governance statement, the Council tailors the content to reflect its own individual circumstances, consistent with the requirements of the relevant accounting and reporting framework and having regard to any guidance issued in support of that framework. This includes a requirement to provide commentary on arrangements for securing value for money from the use of resources.

Auditor responsibilities

Under the NAO Code of Audit Practice 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. The Code requires the auditor to design their work to provide them with sufficient assurance to enable them to report to the Council a commentary against specified reporting criteria (see below) on the arrangements the Council has in place to secure value for money through economic, efficient and effective use of its resources for the relevant period.

The specified reporting criteria are:

- **Financial sustainability** - How the Council plans and manages its resources to ensure it can continue to deliver its services.
- **Governance** - How the Council ensures that it makes informed decisions and properly manages its risks.
- **Improving economy, efficiency and effectiveness** - How the Council uses information about its costs and performance to improve the way it manages and delivers its services.



Value for Money

Planning and identifying risks of significant weakness in VFM arrangements

The NAO's guidance notes requires us to carry out a risk assessment which gathers sufficient evidence to enable us to document our evaluation of the Council's arrangements, in order to enable us to draft a commentary under the three reporting criteria. This includes identifying and reporting on any significant weaknesses in those arrangements and making appropriate recommendations.

In considering the Council's arrangements, we are required to consider:

- The Council's governance statement;
- Evidence that the Council's arrangements were in place during the reporting period;
- Evidence obtained from our work on the accounts;
- The work of inspectorates and other bodies; and
- Any other evidence source that we regards as necessary to facilitate the performance of our statutory duties.

We then consider whether there is evidence to suggest that there are significant weaknesses in arrangements. The NAO's guidance is clear that the assessment of what constitutes a significant weakness and the amount of additional audit work required to adequately respond to the risk of a significant weakness in arrangements is a matter of professional judgement. However, the NAO states that a weakness may be said to be significant if it:

- Exposes – or could reasonably be expected to expose – the Council to significant financial loss or risk;
- Leads to – or could reasonably be expected to lead to – significant impact on the quality or effectiveness of service or on the Council's reputation;
- Leads to – or could reasonably be expected to lead to – unlawful actions; or
- Identifies a failure to take action to address a previously identified significant weakness, such as failure to implement or achieve planned progress on action/improvement plans.

We should also be informed by a consideration of:

- The magnitude of the issue in relation to the size of the Council;
- Financial consequences in comparison to, for example, levels of income or expenditure, levels of reserves (where applicable), or impact on budgets or cashflow forecasts;
- The impact of the weakness on the Council's reported performance;
- Whether the issue has been identified by the Council's own internal arrangements and what corrective action has been taken or planned;
- Whether any legal judgements have been made including judicial review;
- Whether there has been any intervention by a regulator or Secretary of State;
- Whether the weakness could be considered significant when assessed against the nature, visibility or sensitivity of the issue;
- The impact on delivery of services to local taxpayers; and
- The length of time the Council has had to respond to the issue.

Value for Money

Responding to identified risks of significant weakness

Where our planning work has identified a risk of significant weakness, the NAO's guidance requires us to consider what additional evidence is needed to determine whether there is a significant weakness in arrangements and undertake additional procedures as necessary, including where appropriate, challenge of management's assumptions. We are required to report our planned procedures to the Audit Committee.

Reporting on VFM

Where we are not satisfied that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources the Code requires that we should refer to this by exception in the audit report on the financial statements.

In addition, the Code requires us to include the commentary on arrangements in the Auditor's Annual Report. The Code states that the commentary should be clear, readily understandable and highlight any issues we wish to draw to the Council's attention or the wider public. This should include details of any recommendations arising from the audit and follow-up of recommendations issued previously, along with our view as to whether they have been implemented satisfactorily.

Status of our 2020/21 VFM planning

We have yet to complete our detailed VFM planning. However, based on the planning we have undertaken to date we expect that one area of focus will be on the arrangements that the Council has in place in relation to financial sustainability.

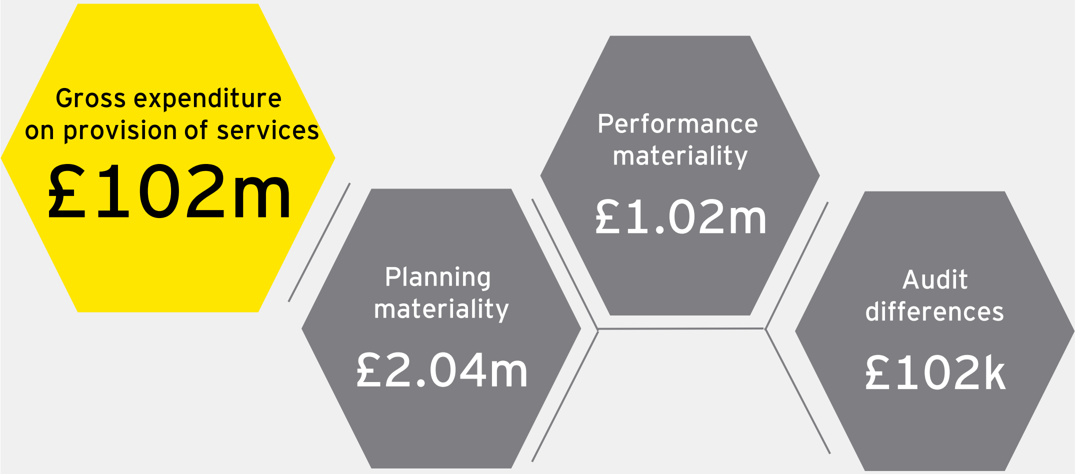
We will update the Audit Committee on the outcome of our VFM planning and our planned response to any identified risks of significant weaknesses in arrangements at a future meeting.

04 Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2020/21 has been set at £2.04 million (2019/20: £1.11 million). This represents 2.0% of the Council's 2020/21 gross expenditure on provision of services. It will be reassessed throughout the audit process. We consider that the focus from interested parties will be on how income is spent and therefore our judgement is that Gross Expenditure is considered to be the most appropriate measurement basis for materiality. We have provided supplemental information about audit materiality in Appendix C.



We request that the Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

Key definitions

Planning materiality – the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

Performance materiality – the amount we use to determine the extent of our audit procedures. We have set performance materiality at £1.02 million (2019/20: £833,000) which represents 50% of planning materiality due to the level of audit adjustments identified in the prior year, and our assessed risk of the likelihood of errors in the current year financial statements.

Audit difference threshold – we propose that misstatements identified below this threshold are deemed clearly trivial. The same threshold for misstatements is used for component reporting. We will report to you all uncorrected misstatements over this amount relating to the comprehensive income and expenditure statement, balance sheet and collection fund that have an effect on income or that relate to other comprehensive income.

Other uncorrected misstatements, such as reclassifications and misstatements in the cashflow statement and movement in reserves statement or disclosures, and corrected misstatements will be communicated to the extent that they merit the attention of the audit committee, or are important from a qualitative perspective.

Group materiality – This considers the balances of Queensway LLP. Group materiality follows:

Planning materiality - £2.10 million
Performance materiality – £1.05 million
Audit differences – £105k

Materiality

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 the circumstances that might ultimately influence our judgement. 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 financial statements, including the total effect of any audit misstatements, and our evaluation of materiality at that date.

Specific materiality

We also identify areas where misstatement at a lower level than our overall materiality level might influence the reader and develop an audit strategy specific to these areas, including:

- Remuneration disclosures including severance payments, exit packages and termination benefits: we will agree all disclosures back to source data, and councillor allowances to the agreed and approved amounts. We will treat any differences over £5k or which result in changes in bandings as material.
- Member allowances: we will agree all disclosures back to source data and agreed and approved amounts. We will treat any differences over £5k as material.
- Related party transactions we will test the completeness of related party disclosures and the accuracy of all disclosures by checking back to supporting evidence. We will treat any differences over £5k or which result in changes in bandings as material.
- Audit Fees: we will agree all disclosures back to source data and agreed amounts. We will treat any differences over £5k as material.

05 Scope of our audit

Our Audit Process and Strategy

Objective and Scope of our Audit scoping

Under the Code of Audit Practice, our principal objectives are to undertake work to support the provision of our audit report to the audited body and to satisfy ourselves that the audited body has made proper 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 an audit report that covers:

1. Financial statement audit

Our opinion on the financial statements:

- whether the financial statements give a true and fair view of the financial position of the audited body and its expenditure and income for the period in question; and
- whether the financial statements have been prepared properly in accordance with the relevant accounting and reporting framework as set out in legislation, applicable accounting standards or other direction.

Our opinion on other matters:

- whether other information published together with the audited financial statements is consistent with the financial statements; and
- where required, whether the part of the remuneration report to be audited has been properly prepared in accordance with the relevant accounting and reporting framework.

Other procedures required by the Code:

- Examine and report on the consistency of the Whole of Government Accounts schedules or returns with the body's audited financial statements for the relevant reporting period in line with the instructions issued by the NAO.

2. Arrangements for securing economy, efficiency and effectiveness (value for money)

As outlined in Section 03, 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 and report a commentary on those arrangements.

Our Audit Process and Strategy (continued)

Audit Process Overview

Our audit involves:

- Identifying and understanding the key processes and internal controls; and
- Substantive tests of detail of transactions and amounts.

For 2020/21, we plan to follow a substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

Analytics:

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular journal entries. These tools:

- Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- Give greater likelihood of identifying errors than random sampling techniques.

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

Internal audit:

We will review internal audit plans and the results of their 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 they raise issues that could have an impact on the financial statements.

Scoping the group audit

Group scoping

Our audit strategy for performing an audit of an entity with multiple locations is risk based. We identify components as:

1. **Significant components:** A component is significant when it is likely to include risks of material misstatement of the group financial statements, either because of its relative financial size to the group (quantitative criteria), or because of its specific nature or circumstances (qualitative criteria). We generally assign significant components a full or specific scope given their importance to the financial statements.
2. **Not significant components:** The number of additional components and extent of procedures performed depended primarily on: evidence from significant components, the effectiveness of group wide controls and the results of analytical procedures.

Stevenage Borough Council has control of Queensway LLP through a partnership with Marshgate Ltd (a subsidiary holding company that the Council owns). Marshgate Ltd is not consolidated into the Council's group financial statements on the grounds of materiality. Queensway LLP is consolidated into the Council's group financial statements. For the purpose of the group audit we have consider Queensway LLP to be a significant component and have designated it a 'specific' scope. This is approach is consistent with that adopted in the prior year.

Scope definitions

Full scope: locations where a full audit is performed to the materiality levels assigned by the Group audit team for purposes of the consolidated audit. Procedures performed at full scope locations support an interoffice conclusion on the reporting package. These may not be sufficient to issue a stand-alone audit opinion on the local statutory financial statements because of the materiality used and any additional procedures required to comply with local laws and regulations.

Specific scope: locations where the audit is limited to specific accounts or disclosures identified by the Group audit team based on the size and/or risk profile of those accounts.

Review scope: locations where procedures primarily consist of analytical procedures and inquiries of management. On-site or desk top reviews may be performed, according to our assessment of risk and the availability of information centrally.

Specified Procedures: locations where the component team performs procedures specified by the Group audit team in order to respond to a risk identified.

Other procedures: For those locations that we do not consider material to the Group financial statements in terms of size relative to the Group and risk, we perform other procedures to confirm that there is no risk of material misstatement within those locations. Individually, these components do not exceed more than 1% of the Group's profit before tax.

Scope definitions

Based on a review of Queensway LLP's financial data at the planning stage of the audit, we consider the following areas to for this component to be included within the specific scope of the group audit:

- Property – Land & buildings
- Cash and cash equivalents
- Finance lease liability
- Long term borrowing
- Financing costs
- Turnover

The scope of the Queensway LLP component may change based on the result of our audit procedures. If we identify any changes in scope of the group audit we will communicate these at the next Audit Committee.

Scoping the group audit

Group audit team involvement in component audits

Queensway LLP does not have external auditor since it qualifies for an audit exemption. Planned group audit procedures to be performed by the audit team (EY) include:

- Performing substantive procedures for the specific accounts identified to be in scope.
- Analytical review of actual performance compared to budget, the prior year and KPIs.
- Review of group wide entity level controls over the component, including the level of CEO, CFO and other group management oversight.
- Testing of consolidation journals, intercompany eliminations and foreign currency translation recalculations.
- Enquiry of management about unusual transactions in the component.

06 Audit team

Audit team

Audit team structure:

Debbie Hanson
Lead Audit Partner

Karen Joan Cunanan
Senior Manager

Nicholas Hoar
Senior

EY Pensions

Pensions Specialist

EY Real Estate

Valuations Specialist

Use of specialists

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
Valuation of Land and Buildings	EY Real Estate Management Specialist – Savills PLC
Pensions disclosure	EY Pensions Specialist PWC as consulting actuary engaged by the NAO Management Specialist – Hymans Robertson LLP - LGPS

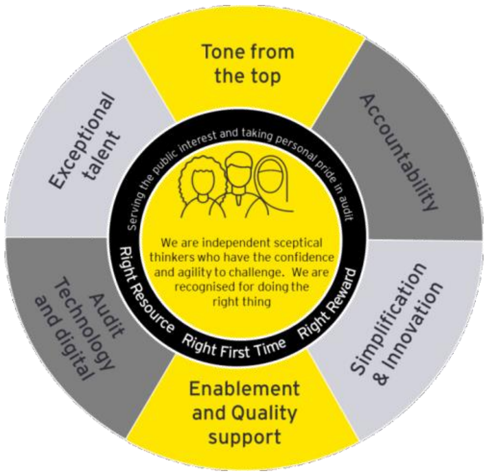
In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

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

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

Developing the right Audit Culture

In July 2021, EY established a UK Audit Board (UKAB) with a majority of independent Audit Non-Executives (ANEs). The UKAB will support our focus on delivering high-quality audits by strengthening governance and oversight over the culture of the audit business. This focus is critical given that audit quality starts with having the right culture embedded in the business.



Our audit culture is the cement that binds together the building blocks and foundation of our audit strategy. We have been thoughtful in articulating a culture that is right for us: one that recognises we are part of a wider, global firm and is clear about whose interests our audits serve.

There are three elements underpinning our culture:

1. Our people are focused on a **common purpose**. It is vital we foster and nurture the values, attitudes and behaviours that lead our people to do the right thing.
2. The essential attributes of our audit business are:
   - **Right resources** – We team with competent people, investing in audit technology, methodology and support
   - **Right first time** – Our teams execute and review their work, consulting where required to meet the required standard
   - **Right reward** – We align our reward and recognition to reinforce the right behaviours
3. The six pillars of **Sustainable Audit Quality** are implemented.

01

Tone at the top

The internal and external messages sent by EY leadership, including audit partners, set a clear tone at the top - they establish and encourage a commitment to audit quality

02

Exceptional talent

Specific initiatives support EY auditors in devoting time to perform quality work, including recruitment, retention, development and workload management

03

Accountability

The systems and processes in place help EY people take responsibility for carrying out high-quality work at all times, including their reward and recognition

04

Audit technology and digital

The EY Digital Audit is evolving to set the standard for the digital-first way of approaching audit, combining leading-edge digital tools, stakeholder focus and a commitment to quality

05

Simplification and innovation

We are simplifying and standardising the approach used by EY auditors and embracing emerging technologies to improve the quality, consistency and efficiency of the audit

06

Enablement and quality support

How EY teams are internally supported to manage their responsibility to provide high audit quality

A critical part of this culture is that our people are **encouraged and empowered to challenge and exercise professional scepticism** across all our audits. However, we recognise that creating a culture requires more than just words from leaders. It has to be reflected in the lived experience of all our people each and every day enabling them to challenge themselves and the companies we audit.

Each year we complete an audit quality culture assessment to obtain feedback from our people on the values and behaviours they experience, and those they consider to be fundamental to our audit quality culture of the future. We action points that arise to ensure our culture continues to evolve appropriately.

<u>2021 Audit Culture Survey result</u>
A cultural health score of 78% (73%) was achieved for our UK Audit Business

We bring our culture alive by investing in three priority workstreams:

- Audit Culture with a focus on professional scepticism
- Adopting the digital audit
- Standardisation

This investment has led to a number of successful outputs covering training, tools, techniques and additional sources. Specific highlights include:

- Audit Purpose Barometer
- Active Scepticism Framework
- Increased access to external sector forecasts
- Forensic risk assessment pilots
- Refreshed PLOT training and support materials, including embedding in new hire and trainee courses
- Digital audit training for all ranks
- Increased hot file reviews and improved escalation processes
- New work programmes issued on auditing going concern, climate, impairment, expected credit losses, cashflow statements and conducting effective group oversight
- Development of bite size, available on demand, task specific tutorial videos

"A series of company collapses linked to unhealthy cultures.....have demonstrated why cultivating a healthy culture, underpinned by the right tone from the top, is fundamental to business success."

Sir John Thompson
Chief Executive of the FRC

07 Audit timeline

Audit timeline

Timetable of communication and deliverables

Timeline

We are currently working with the Council to agree appropriate timelines for the delivery of the 2020/21 audit which will be the most efficient and effective for both the finance team and EY, taking into account other deadlines and in particular the 2022/23 financial closedown processes.

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.

08 Independence

Introduction

The FRC Ethical Standard and ISA (UK) 260 "Communication of audit matters with those charged with governance", requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in December 2019, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	**Final stage**
▸ The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between you, your affiliates and directors and us; ▸ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review; ▸ The overall assessment of threats and safeguards; ▸ Information about the general policies and process within EY to maintain objectivity and independence.	▸ In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed; ▸ Details of non-audit/additional services provided and the fees charged in relation thereto; ▸ Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us; ▸ Details of any non-audit/additional services to a UK PIE audit client where there are differences of professional opinion concerning the engagement between the Ethics Partner and Engagement Partner and where the final conclusion differs from the professional opinion of the Ethics Partner ▸ Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy; ▸ Details of all breaches of the IESBA Code of Ethics, the FRC Ethical Standard and professional standards, and of any safeguards applied and actions taken by EY to address any threats to independence; and ▸ An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement 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, analysed in appropriate categories, are disclosed.

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 the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non –audit services if the service has been pre-approved in accordance with your policy.

Overall Assessment

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

Self interest threats

A self interest threat arises when EY has financial or other interests in the Council. Examples include where we have an investment in the Council; 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 you. 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 where we do so, we will comply with the policies that you have approved, and the Financial Reporting Council's Ethical Standards, and the National Audit Office's Auditor Guidance Note 01. The ratio of non audit fees to audits fees is not permitted to exceed 70%.

At the time of writing, our non-audit work on behalf of the Council is within this ratio. No additional safeguards are required.

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 you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 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 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 the Council. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision 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.

Other communications

EY Transparency Report 2021

Ernst & Young (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 in place 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 end 30 June 2022: EY UK 2022 Transparency Report | EY UK

09 Appendices

Appendix A

Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Housing, Communities and Local Government.

This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the requirements of the Code of Audit Practice and supporting guidance published by the National Audit Office, the financial reporting requirements set out in the Code of Practice on Local Authority Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.

	Planned fee 2020/21	Scale Fee 2019/20
	£	£
Total Scale Fee – Code work	49,283	49,283
Changes in work required to address professional and regulatory requirements and scope associated with risk (**Note 1**)	TBC	TBC
Other Fee variations:		
Additional work required related to revised ISA 540, pension and PPE valuation, lease agreements, group audit work, increase in FRC challenge, VFM commentary quality and preparation issues and procedures related to going concern **(Note 2)**	TBC	TBC
VFM additional risk **(Note 3)**	TBC	TBC
Total audit fee	**£**	**£**
Non-audit fees – certification work (Housing Benefits)	TBC	TBC
Total fees	**£**	**£**

Note 1:

The scale fee for both 2019/20 and 2020/21 has been re-assessed to take into account a number of risk factors which includes procedures performed to address the risk profile of Stevenage Borough Council and additional work to address increase in Regulatory standards. The additional fee is still in discussion with management and will be subject for approval of PSAA.

Note 2:

The additional fee to address specific risks will be calculated and then determined by PSAA Ltd once the 2019/20 and 202/21 audits are complete.

Note 3:

This relates to work performed to address the additional vfm risk. The amount will be submitted with PSAA Ltd once the audit is complete for final determination.

All fees exclude VAT

Appendix B

Required communications with the Audit Committee

We have detailed the communications that we must provide to the Audit Committee**.**

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Terms of engagement	Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified. When communicating key audit matters this includes the most significant risks of material misstatement (whether or not due to fraud) including those that have the greatest effect on the overall audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team	Audit Planning Report - February 2023
Significant findings from the audit	▸ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▸ Significant difficulties, if any, encountered during the audit ▸ Significant matters, if any, arising from the audit that were discussed with management ▸ Written representations that we are seeking ▸ Expected modifications to the audit report ▸ Other matters if any, significant to the oversight of the financial reporting process	Audit results report - *Upon completion of the audit* Auditor's Annual Report - *Upon completion of the audit*

Appendix B

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Public Interest Entities	For the audits of financial statements of public interest entities our written communications to the Audit Committee include: ▸ A declaration of independence ▸ The identity of each key audit partner ▸ The use of non-member firms or external specialists and confirmation of their independence ▸ The nature and frequency of communications ▸ A description of the scope and timing of the audit ▸ Which categories of the balance sheet have been tested substantively or controls based and explanations for significant changes to the prior year, including first year audits ▸ Materiality ▸ Any going concern issues identified ▸ Any significant deficiencies in internal control identified and whether they have been resolved by management ▸ Actual or suspected non-compliance with laws and regulations identified relevant to the Audit Committee ▸ The valuation methods used and any changes to these including first year audits ▸ The scope of consolidation and exclusion criteria if any and whether in accordance with the reporting framework ▸ The identification of any non-EY component teams used in the group audit ▸ The completeness of documentation and explanations received ▸ Any significant difficulties encountered in the course of the audit ▸ Any significant matters discussed with management ▸ Any other matters considered significant	Audit results report – *Upon completion of the audit* Auditor's Annual Report – *Upon completion of the audit*

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: ▸ Whether the events or conditions constitute a material uncertainty ▸ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▸ The adequacy of related disclosures in the financial statements	Audit results report – *Upon completion of the audit*
Misstatements	▸ Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation ▸ The effect of uncorrected misstatements related to prior periods ▸ A request that any uncorrected misstatement be corrected ▸ Material misstatements corrected by management	Audit results report – *Upon completion of the audit*
Subsequent events	▸ Enquiries of the audit committee where appropriate regarding whether any subsequent events have occurred that might affect the financial statements	Audit results report – *Upon completion of the audit*
Fraud	▸ Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity ▸ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist ▸ Unless all of those charged with governance are involved in managing the entity, any identified or suspected fraud involving: a. Management; b. Employees who have significant roles in internal control; or c. Others where the fraud results in a material misstatement in the financial statements ▸ The nature, timing and extent of audit procedures necessary to complete the audit when fraud involving management is suspected ▸ Any other matters related to fraud, relevant to Audit Committee responsibility	Audit results report – *Upon completion of the audit*

Appendix B

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Related parties	▸ Significant matters arising during the audit in connection with the entity's related parties including, when applicable: ▸ Non-disclosure by management ▸ Inappropriate authorisation and approval of transactions ▸ Disagreement over disclosures ▸ Non-compliance with laws and regulations ▸ Difficulty in identifying the party that ultimately controls the entity	Audit results report – *Upon completion of the audit*
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: ▸ The principal threats ▸ Safeguards adopted and their effectiveness ▸ An overall assessment of threats and safeguards ▸ Information about the general policies and process within the firm to maintain objectivity and independence Communication whenever significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place. For public interest entities and listed companies, communication of minimum requirements as detailed in the FRC Revised Ethical Standard 2019: ▸ Relationships between EY, the Council and senior management, its affiliates and its connected parties ▸ Services provided by EY that may reasonably bear on the auditors' objectivity and independence ▸ Related safeguards ▸ Fees charged by EY analysed into appropriate categories such as statutory audit fees, tax advisory fees, other non-audit service fees	Audit Planning Report – February 2023 Audit results report – *Upon completion of the audit*

Appendix B

Required communications with the Audit Committee (continued)

Required communications	What is reported?	Our Reporting to you When and where
	► A statement of compliance with the Ethical Standard, including any non-EY firms or external experts used in the audit ► Details of any inconsistencies between the Ethical Standard and Group's policy for the provision of non-audit services, and any apparent breach of that policy ► Details of any contingent fee arrangements for non-audit services ► Where EY has determined it is appropriate to apply more restrictive rules than permitted under the Ethical Standard ► The Audit Committee should also be provided an opportunity to discuss matters affecting auditor independence	
External confirmations	► Management's refusal for us to request confirmations ► Inability to obtain relevant and reliable audit evidence from other procedures	Audit results report – *Upon completion of the audit*
Consideration of laws and regulations	► Subject to compliance with applicable regulations, matters involving identified or suspected non-compliance with laws and regulations, other than those which are clearly inconsequential and the implications thereof. Instances of suspected non-compliance may also include those that are brought to our attention that are expected to occur imminently or for which there is reason to believe that they may occur ► 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 – *Upon completion of the audit*
Internal controls	► Significant deficiencies in internal controls identified during the audit	Audit results report – *Upon completion of the audit*

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Group audits	▸ An overview of the type of work to be performed on the financial information of the components ▸ An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components ▸ Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work ▸ Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted ▸ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements	Audit planning report - February 2023 Audit results report - *Upon completion of the audit*
Representations	Written representations we are requesting from management and/or those charged with governance	Audit results report - *Upon completion of the audit*
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report - *Upon completion of the audit*
Auditors report	▸ Any circumstances identified that affect the form and content of our auditor's report	Audit results report - *Upon completion of the audit* Auditor's Annual Report - *Upon completion of the audit*
Fee Reporting	▸ Breakdown of fee information when the audit plan is agreed ▸ Breakdown of fee information at the completion of the audit ▸ Any non-audit work	Audit planning report - February 2023 Audit results report - *Upon completion of the audit*
Value for Money	▸ Risks of significant weakness identified in planning work ▸ Commentary against specified reporting criteria on the VFM arrangements, including any exception report on significant weaknesses.	Audit planning report - February 2023 Audit results report - *Upon completion of the audit* Auditor's Annual Report - *Upon completion of the audit*

Appendix C

Additional audit information

Objective of our audit
Our objective is to form an opinion on the Council's and Group's consolidated financial statements under International Standards on Auditing (UK) as prepared by you in accordance with with International Financial Reporting Standards as adopted by the EU, and as interpreted and adapted by the Code of Practice on Local Authority Accounting. Our responsibilities in relation to the financial statement audit are set out in the formal terms of engagement between the PSAA's appointed auditors and audited bodies. We are responsible for forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of the Audit Committee. The audit does not relieve management or the Audit Committee of their responsibilities.

Other required procedures during the course of the audit	
In addition to the key areas of audit focus outlined in section 02, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.	
Our responsibilities required by auditing standards	▸ Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. ▸ Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Council's internal control. ▸ Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management. ▸ Concluding on the appropriateness of management's use of the going concern basis of accounting. ▸ Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation. ▸ Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Council to express an opinion on the consolidated financial statements. Reading other information contained in the financial statements, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and ▸ Maintaining auditor independence.

Additional audit information (continued)

Other required procedures during the course of the audit (continued)	
Procedures required by the Audit Code	▸ Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance Statement. ▸ Examining and reporting on the consistency of consolidation schedules or returns with the Council's audited financial statements for the relevant reporting period
Other procedures	▸ We are required to discharge our statutory duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice
We have included in Appendix B a list of matters that we are required to communicate to you under professional standards.	

Purpose and evaluation of materiality

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

Materiality determines the level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, 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.

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