



## **East Ayrshire Council**

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

Issued on 17 September for the meeting on 24 September 2020

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# Introduction

## The key messages in this report

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

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

I have pleasure in presenting our final report to the Governance and Scrutiny Committee (“the Committee”) of East Ayrshire Council (“the Council”) for the 2019/20 audit. The scope of our audit was set out within our planning report presented to the Committee in February 2020.

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

This report summarises our findings and conclusions in relation to:

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



# Introduction (continued)

## The key messages in this report (continued)

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

### **Conclusions from our testing**

We have issued an unmodified audit opinion.

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

Following amendments made as a result of our audit, we are satisfied that the management commentary and annual governance statement comply with the statutory guidance and proper practice and are consistent with the financial statements and our knowledge of the Council.

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

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

Audit adjustments in excess of our reporting threshold (see page 9) have been identified in relation to valuations (page 15) and the pension liability (page 16). Both of these have been corrected by management. It should be noted that adjustments relating to the pension liability are as a result of a post balance sheet event rather than an error by management. One disclosure adjustment in relation to grants credited to services has been identified (page 11), which has been corrected by management.

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

There are no matters outstanding.

### **Conclusions on audit dimensions**

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

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

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

**Financial Management** - The Council has strong financial management arrangements. The General Fund and HRA ended the year with an in-year surplus and savings targets were substantially achieved. The financial position and variances were transparently reported to the Governance and Scrutiny Committee throughout the year.

# Introduction (continued)

## The key messages in this report (continued)

### Conclusions on audit dimensions (continued)

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

The Council has demonstrated good progress in reducing the budget gap each year through the achievement of in year savings. The publication of the Long-Term Financial Outlook is also a positive step to enable the Council to manage the financial challenges that it faces and to make well-informed decisions which are aligned to Council priorities. The impact of COVID-19 is expected to have a significant impact over the medium to longer term, and therefore the estimated financial impact of these challenges is likely to change.

The Council has made good progress during 2019/20 in relation to Transformational Workstreams and is undertaking a review of the performance management framework to monitor progress and benefits arising from the transformation work.

In recognition of the significant impact of COVID-19 on Council services, it is positive to note that a comprehensive report has been considered by the Council in June 2020 setting out the Renewal and Recovery Planning and how this closely aligns with the transformation work. We will continue to monitor this as part of our 2020/21 audit.

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

The Council continues to have strong leadership in place. This has been particularly evident in the response to COVID-19, the streamlined decision making arrangements and the arrangements for developing the Renewal and Recovery Plan.

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

The IJB has made some good progress during the year, continuing to achieve financial balance, driving forward transformation and reporting improvements in performance in some areas. The risks of COVID-19 on both the financial position and performance of the IJB will remain ongoing, however, we are satisfied that there are plans in place to carry out a comprehensive review of the MTFP and Strategic Plan during 2020/21.

**Value for money** - The Council continues to have a clear and robust performance management framework in place through the Local Outcome Improvement Plan (LOIP) and in line with best practice, clearly links its performance measures to the National Performance Framework. It also has robust and long-standing arrangements in place to comply with the new SPI Direction including its public performance reporting requirements.

The performance of the Council is showing evidence of improvements in a number of areas, although there has been a reduction in the number in the top and second quartile between 2017/18 and 2018/19. We recognise that the COVID-19 pandemic has had a significant impact on a number of services. It is important that the Council take any lessons learned as it moves into the recovery phase to consider alternative approaches to service delivery. It is positive to note that a comprehensive report has already been submitted to the Council to set out the plans for Renewal and Recovery Planning.

# Introduction (continued)

## The key messages in this report (continued)

### **Conclusions on audit dimensions (continued)**

#### **Best Value**

The Council has robust arrangements in place to secure best value and has a clear understanding of areas which require further development. Good progress has been made in implementing the agreed actions arising from the 2018 BVAR Report.

Our conclusions and detailed findings are included in our separate report submitted along with this report. Management have agreed to all the recommendations and are in the process of implementing them.

#### **Next steps**

An agreed Action Plan is included as an Appendix on page 26 of this report. A separate Action Plan on the findings of the audit dimensions work is included in our separate report. We will consider progress with the agreed actions as part of our 2020/21 audit.

### **Added value**

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

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

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

# Financial statements audit



# Quality indicators

## Impact on the execution of our audit

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

Area	Grading	Reason
Timing of key accounting judgements	●	Key accounting judgements, such as equal pay provisions, property valuations and net defined benefit pension asset support were provided on time and were of good quality.
Adherence to deliverables timetable	●	Key deliverables were provided on time ahead of our final fieldwork on 6 July.
Access to finance team and other key personnel	●	Deloitte and the Council have worked together to facilitate remote communication during the audit. This has included effective use of such technologies as Skype, Microsoft Teams and Dropbox.
Quality and accuracy of management accounting papers	●	Documentation provided has been a high standard, with working papers easily reconcilable to the annual accounts, clearly laid out and well documented.
Quality of draft annual accounts	●	A full draft of the annual accounts was received for audit on 29 June 2020. The draft was of a high standard and includes numerous areas of good practice, with significant improvements noted in the year. Changes were requested to more consistently disclose comparative information, setting out areas of challenge for the Council and plans to address these, explaining the Council's key risks and uncertainties and providing narrative on the group accounts and common good fund.
Response to control deficiencies identified	●	We have not noted any control deficiencies as a result of our work.
Volume and magnitude of identified errors	●	We have identified two financial adjustments above our reporting threshold, one of which relates to a post balance sheet event. We have identified one disclosure adjustment.



Lagging



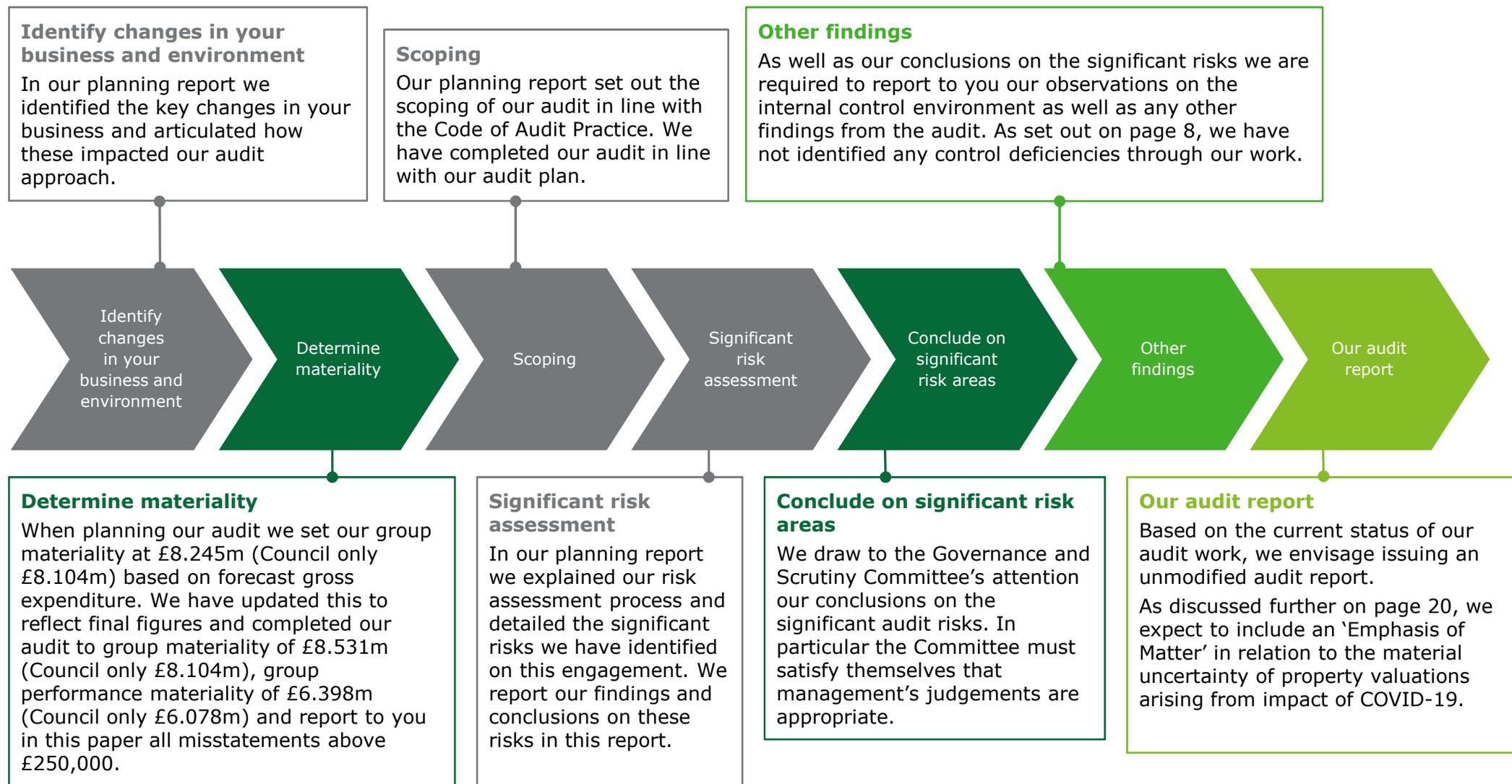
Developing



Mature

# Our audit explained

We tailor our audit to your business and your strategy



# Significant risks Dashboard

Risk	Material	Fraud risk	Planned approach to controls testing	Consistency of judgements with Deloitte's expectations	Comments	Slide no.
Recognition of grant income			D+I		Satisfactory	11
Management override of controls			D+I		Satisfactory	12
Valuation of property assets			D+I		Satisfactory	14

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

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

# Significant risks (continued)

## Risk 1 - Recognition of grant income

### Risk identified

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

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

The significant risk is pinpointed to the recognition of grant income, comprising other capital grants and grants credited to services.

### Key judgements and our challenge of them



Grant income is a significant risk due to:

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

### Deloitte response



We have performed the following:

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

Type of income	2019/20 (£m)	Significant risk
<b><u>Taxation and Non-Specific Grant Income</u></b>		
Income from council tax	50.321	
Revenue support grant	202.352	
Non domestic rates	27.360	
General capital grant	9.074	✓
Council House Building Programme	4.262	✓
<i>Other capital grants</i>	<i>10.351</i>	✓
<b><u>Service Income</u></b>		
<i>Grants credited to services</i>	<i>32.394</i>	✓
DWP Housing Benefit	29.914	
Housing Revenue Account	45.150	
IJB commission income (book entry)	110.626	
Other Service Income	28,621	
<b>Total Service Income</b>	<b>246.705</b>	

### Deloitte view

We have concluded that grant income has been correctly recognised in accordance with the requirements of the Code of Practice on Local Authority Accounting. We have not identified any issues with the recognition of grant income in the year. We identified a disclosure adjustment of £3.133m in relation to the disclosure of grants credited to services, which has been corrected by management.

# Significant risks (continued)

## Risk 2 - Management override of controls

### Risk identified

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



### Deloitte response

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

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

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

### Significant and unusual transactions

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

### Journals

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

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

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

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

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

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

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

### Deloitte view

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

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

# Significant risks (continued)

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

**Key judgements** The key judgement in the financial statements are those which we have selected to be the significant audit risks around the recognition of grant income (page 11) and the valuation methodology for property valuations (page 14). While not considered to be significant audit risks, we have considered the assumptions used to calculate the pension liability (page 16), and the recognition of expenditure (page 17). In the table below, we set out our challenge of the assumptions used in the determination of provisions.

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Provisions	The total provisions held within the Council's balance sheet is immaterial. This comprises provisions in respect of teachers holiday accrued while on maternity leave, a potential PAYE tax liability, equal pay claims and the Council's share of the former Strathclyde Regional Council's insurance claims. As the Council has utilised the exemption permitted under accounting standards whereby disclosure of the total amount of the provision would be seriously prejudicial to the Council's interests, we have not disclosed the total provision within our report, instead noting that it is immaterial.	<p>We examined the rationale for each provision, including a retrospective review of amounts provided in 2018/19. We have consulted with the Council's legal experts to confirm completeness of the provisions.</p> <p>In relation to the provision for equal pay, we have assessed the completeness of the provisions made through discussion with the Council's legal and HR advisers and benchmarked with our industry knowledge. We have also considered external developments and progress in dealing with the equal pay claims in determining whether the amount provided is reasonable.</p> <p>We have concluded that the provisions made were reasonable.</p>

# Significant risks (continued)

## Valuation of property assets

### Risk identified

The Council held £776.772m of property assets at 31 March 2020. This year represents year two of a five year rolling programme in which 20% of the land and buildings portfolio was revalued. The Council is required to hold property assets within Property, Plant and Equipment at a modern equivalent use valuation. The valuations are by nature significant estimates which are based on specialist and management assumptions and which can be subject to material changes in value. As reported in our 2018/19 annual audit report, we identified a number of material errors in relation to the revaluation movements recognised in the 2018/19 financial statement which were corrected by management. These errors arose as a result of deficiencies in the valuation process. As identified in our audit plan, there was a significant risk of material misstatement in 2019/20.



### Key judgements

The Council appointed an external valuer to carry out its revaluation work during 2019/20. The revaluation has resulted in a net downward revaluation to property values of £88.975m due to prevailing market conditions at the year-end date. Whilst we have identified an adjustment in relation to valuations (page 15), we are satisfied that the movement in the year and does not indicate issues in the prior year financial statements. The downward movement in 2019/20 is largely as a result of the net impairment of £66.4m posted against Other Land and Buildings. This specifically relates to the revaluation of assets valued in excess of £500,000. The downward movement is as a result of changes to the valuation methodology applied following the last revaluation of these assets five years ago. Our internal experts confirmed that they are satisfied that the overarching methodology applied for 2019/20 is appropriate (aside from issues detailed on page 15).

The valuer identified a material uncertainty due to the impact of COVID-19 on individual markets, in line with RICS guidance published on 18 March 2020, as follows:

*"The outbreak of the Novel Coronavirus (COVID-19), declared by the World Health Organisation as a "Global Pandemic" on 11 March 2020, has impacted global financial markets. There is a large degree of uncertainty as to how this outbreak will affect the wider global economy and its sub-markets.*

*Market activity is being impacted in many sectors. The situation involving the COVID-19 pandemic and its impact upon the commercial marketplace is currently ongoing.*

*Whilst there is no empirical evidence to suggest any impact on pricing, marketing periods will likely become protracted as a result until such time as the pandemic subsides and the basic functions of the economy can be restarted.*

*The date of this asset valuation is 31 March 2020 and therefore we must address the issue of valuation certainty in relation to the subjects under valuation. The majority of assets under valuation are operational and are held for their service potential and have been classified as 'specialised'; the approximate split being 80% (operational/specialised) 20% (non-operational/non-specialised). These specialist assets have been valued using the Depreciated Replacement Cost (DRC) method with reference to build rates (as at 31 March 2020) and is not based on the evidence of sales of similar assets in the market. It is too early to note the impact COVID-19 has had on the commercial marketplace; however we are of the opinion that the impact on build rates will be less severe. Whilst we consider that we can attach less weight to previous market evidence for comparison purposes of the non-specialised assets under valuation, to inform opinions of value, overall we believe the portfolio will be less subject to variances in value as a result of COVID-19 than one which is fully made up non-operation / non-specialised assets and as such we have a large degree of confidence in the valuations for 2019/20.*

*In line with the RICS Valuation Practice Alert dated 18 March 2020 and subsequently updated on 15 April 2020, our valuations are reported on the basis of 'material valuation uncertainty' as per VPS 3 and VPGA 10 of the RICS Red Book Global. Given the unknown future impact that COVID-19 might have on the real estate market, we recommend that you keep the valuations under frequent review."*

# Significant risks (continued)

## Valuation of property assets (continued)



### Deloitte response

- We have tested the design and implementation of key controls around the property valuation;
- We have followed up on the recommendations made in the previous years' audit to assess whether management's actions to address deficiencies in valuation process has been implemented;
- We engaged early with the Council, using valuation specialists to challenge the assumptions applied by management in the valuations. We also engaged our specialists in relation to the impact of COVID-19;
- We used our valuation specialists, Deloitte Real Estate, to review and challenge the appropriateness of the assumptions used in the year-end valuation of the Council's Land and Buildings, including considering movements compared to those of other Council's performing valuations for 2019/20;
- We assessed management's review of assets not subject to revaluation during the year for potential material changes;
- We consider the impact of uncertainties relating to the UK's exit from the EU and COVID-19 upon property valuations in evaluating the property valuations and related disclosures; and
- We have reviewed the valuer's report and assessed managements disclosure of the key source of estimation uncertainty.

### Deloitte view

We noted significant improvements in the valuation process in 2019/20 compared to 2018/19. We identified an audit adjustment of £3.665m due to an incorrect valuation methodology being used impacting the school portfolio, with this being a recurring issue from the prior year. Management have adjusted for this in the annual accounts.

We have made a further recommendation for improvement in the valuations process, as set out on page 26.

We expect to include an 'Emphasis of Matter' in our audit report (page 20) due to the material uncertainty identified by the valuers concerning valuations at 31 March 2020 due to the impact of COVID-19 on the property market. This has been appropriately disclosed in the notes to the financial statements.

# Other areas of audit focus (continued)

## Defined benefits pension scheme

### Background

The Council participates in two defined benefits schemes:

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

The net pension liability has decreased from £204.262m in 2018/19 to £129.177m in 2019/20. The decrease is combination of a reduction of £35m in the fair value of the assets and a reduction of £110m in the liabilities as a result of demographic changes and financial assumptions. This total includes the impact of the McCloud adjustments.

The Council's pension liability continues to be affected by the McCloud legal case in respect of potential discrimination in the implementation of transitional protections following changes in public sector pension schemes in 2015. Following recent consultation published by the SPPA subsequent to the year end, the actuary has amended its estimate of the impact of McCloud to only include members that were in service before 1 April 2012. This has resulted in a reduction of £6.203m to the liability disclosed in the draft accounts which has been updated in the final accounts. The actuary has made this adjustment to past service costs, but had not made any allowance within the current service costs for the impact of McCloud, resulting in a further required revision to the IAS 19 report. The Council's actuary has estimated that the potential impact of this is a £0.693m understatement of the liability, which has been amended by management. This is an estimate and the actual cost could be different.

In the current year there was an additional legal case - the Goodwin judgement - that has an impact on the scheme. The judgement, subsequent to the year-end, is in respect of a Teacher's Pension case where there was deemed to be discrimination in spousal transfer on death of the member (where a male widower was deemed to be discriminated against through receiving a different level of benefits than a female widow). The actuary has amended its estimates to take into account this case, which has resulted in an increase in liability of £1.203m to the liability disclosed in the draft accounts which have been updated in the final accounts.



### Deloitte response

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

	Council	Comments
Discount rate (% p.a.)	2.3	Prudent and reasonable
Consumer Price Index (CPI) Inflation rate (% p.a.)	2.9	Prudent end of reasonable range
Salary increase (% p.a.)	3	Real salary increases 1.1% above CPI inflation
Pension increase in payment (% p.a.)	1.9	Reasonable
Pension increase in deferment (% p.a.)	1.9	Reasonable
Mortality - Life expectancy of a male pensioner from age 65 (currently aged 65)	20.7	Prudent
Mortality - Life expectancy of a male pensioner from age 65 (currently aged 45)	22.2	Prudent

### Deloitte view

Adjustments were required to reflect the changes to the liability for both McCloud and Goodwin arising from events after the balance sheet date (net impact was a reduction in liability of £4.307m), which have been actioned by management.

# Other areas of audit focus (continued)

## Expenditure recognition

### Risk identified

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

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



### Deloitte response

We performed the following procedures using data analytics to address the above risk:

- A review of the number and median value of invoices processed in the year. As illustrated in table opposite, based on the median amount, the Council would need to omit over 47,000 invoices at year-end to result in a material error. We noted that in the month following the year-end, a total of 7,841 invoices were processed. We therefore concluded that a risk of material misstatement was remote.
- An analytical review to test the completeness and accuracy of year-end creditor balances. We identified no issues through our work.

	Invoice Analysis
Median invoice amount	£169
Average number of invoices processed per month	11,482
Number of invoices that would need to be unrecorded to cause a material misstatement	47,953
Total invoices processed in April 2020 (one month after year-end)	7,841 (total value £40.768m)

### Deloitte view

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

# Other areas of audit focus (continued)

## Charitable trusts

### Risk identified

From 2013/14, all Scottish Councils who act as sole trustees for any registered charities have to fully comply with the Charities Accounts Regulations. This requires Charities SORP compliant accounts to be prepared for each charity, and a separate audit of each. East Ayrshire Council administers three such registered charities – East Ayrshire Council Charitable Trust, Archibald Taylor Fund and Miss Annie Smith Mair Newmilns Trust Fund.

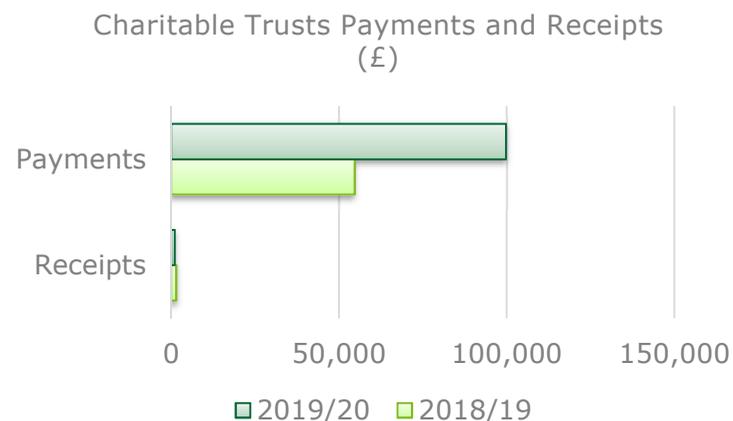
As the gross income of each of the Trusts is less than £100,000, the Council has opted to prepare the charitable trust accounts on a receipts and payments basis in accordance with The Charities Accounts (Scotland) Regulation 2006. Fully compliant Charities SORP accounts are therefore not required and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



### Deloitte response

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

A summary of the key movements is provided in the table adjacent. We note that there has been limited activity in the Trusts over the last 12 months.



### Deloitte view

We have not identified any issues through our audit work.

# Other significant findings (continued)

## Financial reporting findings

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

### **Qualitative aspects of your accounting practices:**

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

### **Other matters relevant to financial reporting:**

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

### **Significant matters discussed with management:**

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

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

# Our audit report

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

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



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

Our opinion on the financial statements is unmodified.



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

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

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



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

As discussed on page 15, we have included an 'Emphasis of Matter' paragraph within our audit report in relation to the material uncertainty associated with the property valuations arising from guidance issued by RICS.

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



### **Other reporting responsibilities**

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

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

# Coronavirus (COVID-19) outbreak

## Impact on the annual accounts and audit

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

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

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### Impact on the Council's annual accounts

The Council need to consider the impact of the outbreak on the annual report and financial statements including:

- Principal risk disclosures;
- Change in the funding regime for 20/21;
- Property valuation material uncertainty;
- Impairment of non-current assets;
- Allowance for expected credit losses;
- Fair value measurements based on unobservable inputs;
- Onerous contracts and any potential provisions;
- Going concern; and
- Events after the end of the reporting period.

### Impact on our audit

COVID-19 has fundamentally changed the way we have conducted our audit this year including:

- Teams are primarily working remotely;
  - The teams have had regular status updates to discuss progress and facilitate the flow of information;
  - Consideration of impacts on the areas of the financial statements and annual report listed has been included as part of our audit work in the current year and comments have been included where appropriate within this report; and
  - In conjunction with the Council staff, we will continue to consider any developments for potential impact up to the finalisation of our work in September 2020.
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# Your annual report

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

	Requirement	Deloitte response
Management Commentary	The management commentary comments on financial performance, strategy and performance review and targets. The commentary included both financial and non financial KPIs and made good use of graphs and diagrams. The Council also focusses on the strategic planning context.	<p>We have assessed whether the management commentary has been prepared in accordance with the statutory guidance.</p> <p>We have also read the management commentary and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading.</p> <p>Following amendments made during the course of the audits, we are satisfied that the management commentary has been prepared in accordance with guidance, is consistent with our knowledge and is not otherwise misleading.</p> <p>We welcome significant improvements in the presentation and content of the annual accounts in 2019/20. The Council has made commendable use of pictures, infographics and charts throughout the annual accounts to improve understanding. There is also a high level of signposting to where the reader can find additional information.</p>
Remuneration Report	The remuneration report has been prepared in accordance with the 2014 Regulations, disclosing the remuneration and pension benefits of Senior Councillors and Senior Employees of the Council.	<p>We have audited the disclosures of remuneration and pension benefits, pay bands, and exit packages.</p> <p>We can confirm that auditable parts of remuneration report have been properly prepared in accordance with the regulations.</p>
Annual Governance Statement	The Annual Governance Statement reports that the Council governance arrangements provide assurance, are adequate and are operating effectively.	We have assessed whether the information given in the Annual Governance Statement is consistent with the financial statements and has been prepared in accordance with the accounts regulations. We have not identified any issues through our review.

# Appendices



# Purpose of our report and responsibility statement

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

### What we report

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

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

### The scope of our work

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

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

### Use of this report

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

### What we don't report

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

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

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

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



**Pat Kenny, CPFA**

**For and on behalf of Deloitte LLP**

Glasgow | 17 September 2020

# Audit adjustments

## Summary of uncorrected misstatements and disclosure deficiencies

### **Uncorrected misstatements**

No uncorrected misstatements have been identified from our audit work performed to date.

### **Disclosure misstatements**

Auditing standards require us to highlight significant uncorrected disclosure misstatements to enable the Governance and Scrutiny Committee to evaluate the impact of those matters on the financial statements. We have noted no material disclosure deficiencies in the course of our audit work to date.

# Action plan

## Recommendations for improvement

No.	Area	Recommendation	Management Response	Responsible person	Target Date	Priority
1	<i>Property valuations</i>	While we have noted significant improvements in the property valuation process in 2019/20, Management have accepted this further improvements should be made with regards to setting out the Modern Equivalent Asset in 2020/21. valuation approach in greater detail in the valuation report.	recommendation and confirmed that it will be built into the valuation process	Chief Governance Officer	March 2021	Medium

We have followed up the recommendations made in our 2018/19 annual report in relation to the financial statements and are pleased to note both recommendations – in relation to property valuations and IFRS 16 – have been fully implemented. The recommendation above in relation to property valuations is distinct from the recommendations made in the prior year.

# Our other responsibilities explained

## Fraud responsibilities and representations



### Responsibilities:

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



### Required representations:

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

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



### Audit work performed:

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

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

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

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

### Concerns:

No concerns have been identified regarding fraud.



# Independence and fees



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

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**Independence confirmation** We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Council and will reconfirm our independence and objectivity to the Governance and Scrutiny Committee for the year ending 31 March 2020 in our final report to the Governance and Scrutiny Committee.

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**Fees** The audit fee for 2019/20, in line with the fee range provided by Audit Scotland, is £284,720 as analysed below:

	£
Auditor remuneration	174,810
Audit Scotland fixed charges:	
Pooled costs	17,100
Performance Audit and Best Value	82,240
Audit support costs	10,570
<b>Total proposed fee</b>	<b>284,720</b>

In addition, the audit fee for the charitable trusts audit is £1,200.

There are no non-audit services fees proposed for the period.

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**Non-audit services** In our opinion there are no inconsistencies between the FRC's Ethical Standard and the Council's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.

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**Relationships** We are required to provide written details of all relationships (including the provision of non-audit services) between us and the organisation, its board and senior management and its affiliates, including all services provided by us and the DTTL network to the audited entity, its board and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence.

We are not aware of any relationships which are required to be disclosed.

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# Quality of public audit in Scotland

## Annual report 2018/19

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

### Public audit in Scotland

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

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

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

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

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

### Key messages

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

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

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

Other performance measures showing good performance include:

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

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

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



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