



Epping Forest District Council

Audit planning report to the Audit and Governance Committee for
the year ending 31 March 2019

Issued 13 March 2019 for the meeting on 25 March 2019

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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 statement of accounts.
- 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 planning report to the Audit and Governance Committee for the 2019 audit. I would like to draw your attention to the key messages of this paper:

Scope of our work

Our audit work will be carried out in accordance with the requirements of the Code of Audit Practice ('the Code') and supporting guidance published by the National Audit Office (NAO) on behalf of the Comptroller and Auditor General.

The Code sets the overall scope of the audit which includes an audit of the accounts of the Council and work to satisfy ourselves that the Council has made proper arrangements to secure value for money (VFM) in its use of resources. There have not been any changes to the Code, itself, and therefore the scope of our work is broadly similar to the scope of work set for your auditor in the prior year.

Our responsibilities as auditor, and the responsibilities of the Council, are set out in "*PSAA Statement of responsibilities of auditors and audited bodies: Principal Local Authorities and Police Bodies*", published by Public Sector Audit Appointments Limited.

Areas of focus in our work on the accounts

We summarise below the areas of significant audit risk we have so far identified:

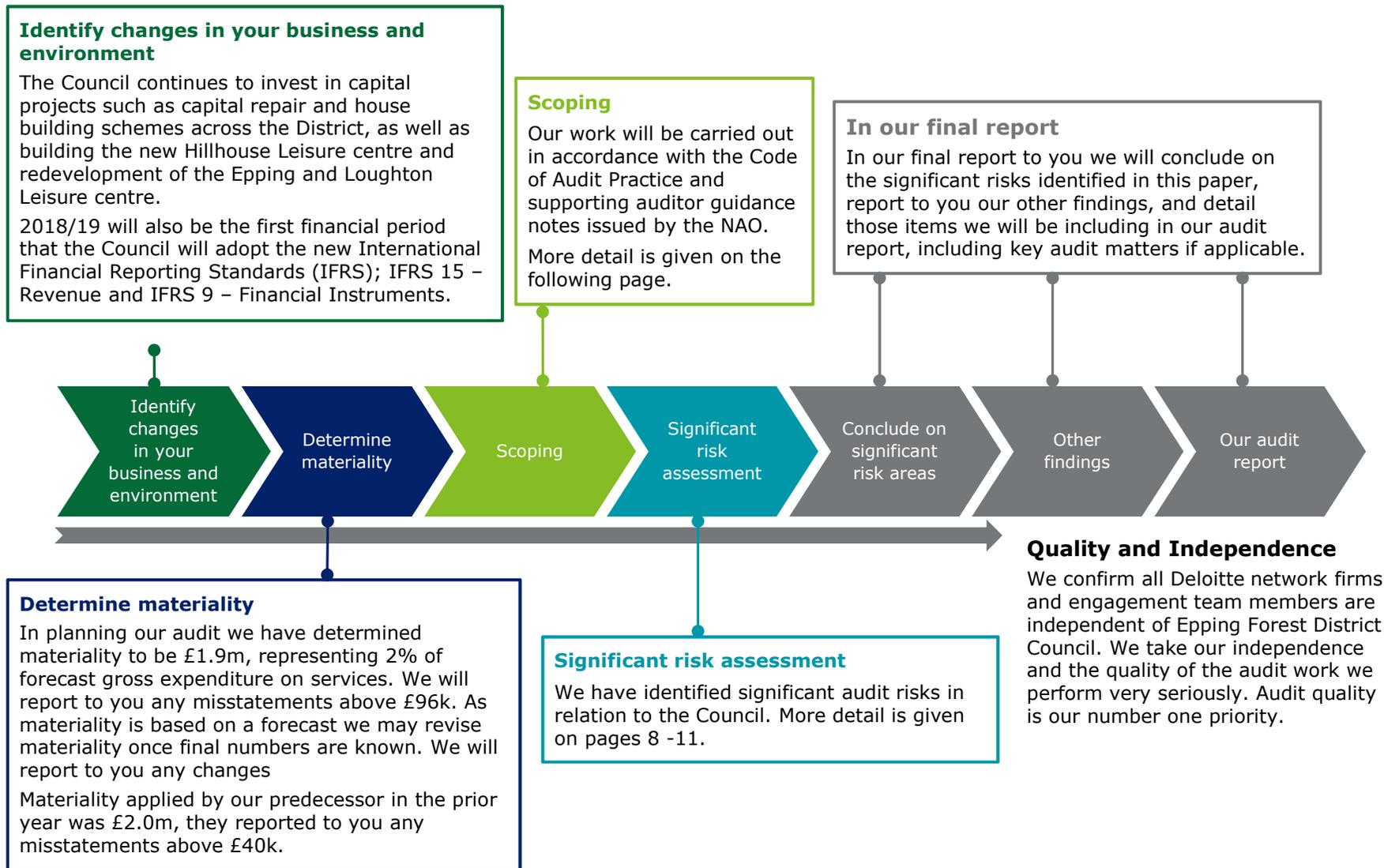
- Valuation of properties – Fixed assets and investment properties – there is significant judgement over the subjective inputs to the valuation.
- Capitalisation of expenditure – there is judgement over the appropriate classification of spend between capital and revenue. The Council has greater flexibility over the use of its revenue compared to its capital resources. This provides an incentive to inappropriately classify spend as capital which does not meet the accounting criteria for classification as such.
- Management override of controls – auditing standards presume there is a risk that the accounts may be fraudulently misstated by management overriding controls. Key areas of focus are: bias in the preparation of accounting estimates; inappropriate journal entries and transactions which have no economic substance.

Brexit

The arrangements following the UK's exit from the EU are not yet clear. Our audit plan does not include any risks or procedures in respect of the impact upon the Council, whether on Value-for-Money (VfM) arrangements, or more widely. We will update the Audit and Governance Committee if any risks are identified as the eventual circumstances of the UK's exit become clear.

Our audit of the statement of accounts explained

We tailor our audit to your Council



Scope of work and approach

We have the following areas of responsibility under the Code of Audit Practice

Opinion on the Council's financial statements

We will conduct our audit in accordance with the Code of Audit Practice and supporting guidance issued by the National Audit Office ("NAO") and International Standards on Auditing (UK) ("ISA (UK)") as adopted by the UK Auditing Practices Board ("APB").

We report on whether the financial statements:

- Give a true and fair view of the financial position and income and expenditure
- Are prepared properly in accordance with the Code of Practice on Local Authority Accounting ("the Code").

Opinion on other matters

We are required to report on whether other information published with the audited financial statements is consistent with the financial statements.

Other information includes information included in the statement of accounts, in particular the Narrative Report. It also includes the Annual Governance Statement which the Council is required to publish alongside the Statement of Accounts.

In reading the information given with the financial statements, we take into account our knowledge of the Council, including that gained through work in relation to the body's arrangements for securing value for money through economy, efficiency and effectiveness in the use of its resources.

Whole Government Accounts

We are required to issue a separate assurance report on the Council's separate return required to facilitate the preparation of the Whole of Government Accounts.

Our work on the return is carried out in accordance with instructions issued by the NAO and typically focuses on testing the consistency of the return with the Council's financial statements, together with the validity, accuracy and completeness of additional information about the Council's transaction and balances with other bodies consolidated within the Whole of Government Accounts. We are also typically asked to report to the NAO on key findings from our audit of the accounts.

Value for Money conclusion

We are required to provide a conclusion on whether the Council has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

We carry out a risk assessment to identify any risks that, in our judgement, have the potential to cause us to reach an inappropriate conclusion on the audited body's arrangements. The risk assessment enables us to determine the nature and extent of further work that may be required. This means that if we do not identify any significant risks, there is no requirement to carry out further work.

We also consider the impact of findings of other inspectorates, review agencies and other relevant bodies on their risk assessment, where they are relevant and available.

Our responsibilities as auditor, and the responsibilities of the Council, are set out in "PSAA Statement of responsibilities of auditors and audited bodies: Principal Local Authorities and Police Bodies", published by PSAA

Scope of work and approach

Our approach

Liaison with internal audit

The Auditing Standards Board's version of ISA (UK) 610 "Using the work of internal auditors" prohibits use of internal audit to provide "direct assistance" to the audit. Our approach to the use of the work of Internal Audit has been designed to be compatible with these requirements.

We plan to meet with Internal Audit to discuss their work. We have reviewed reports issued in the period to 31 January 2019 and will update this for further reports issued as part of the 2018/19 internal audit programme. We consider the findings from their work and where significant control weaknesses are identified, we consider the impact on the scope of our own work.

Approach to controls testing

For controls considered to be 'relevant to the audit', our work involves evaluating the design of these controls and determining whether they have been implemented ("D & I").

We do not expect to place reliance on the operating effectiveness of controls in the current year.

Promoting high quality reporting to stakeholders

We view the audit role as going beyond reactively checking compliance with requirements: we seek to provide advice on evolving good practice to promote high quality reporting.

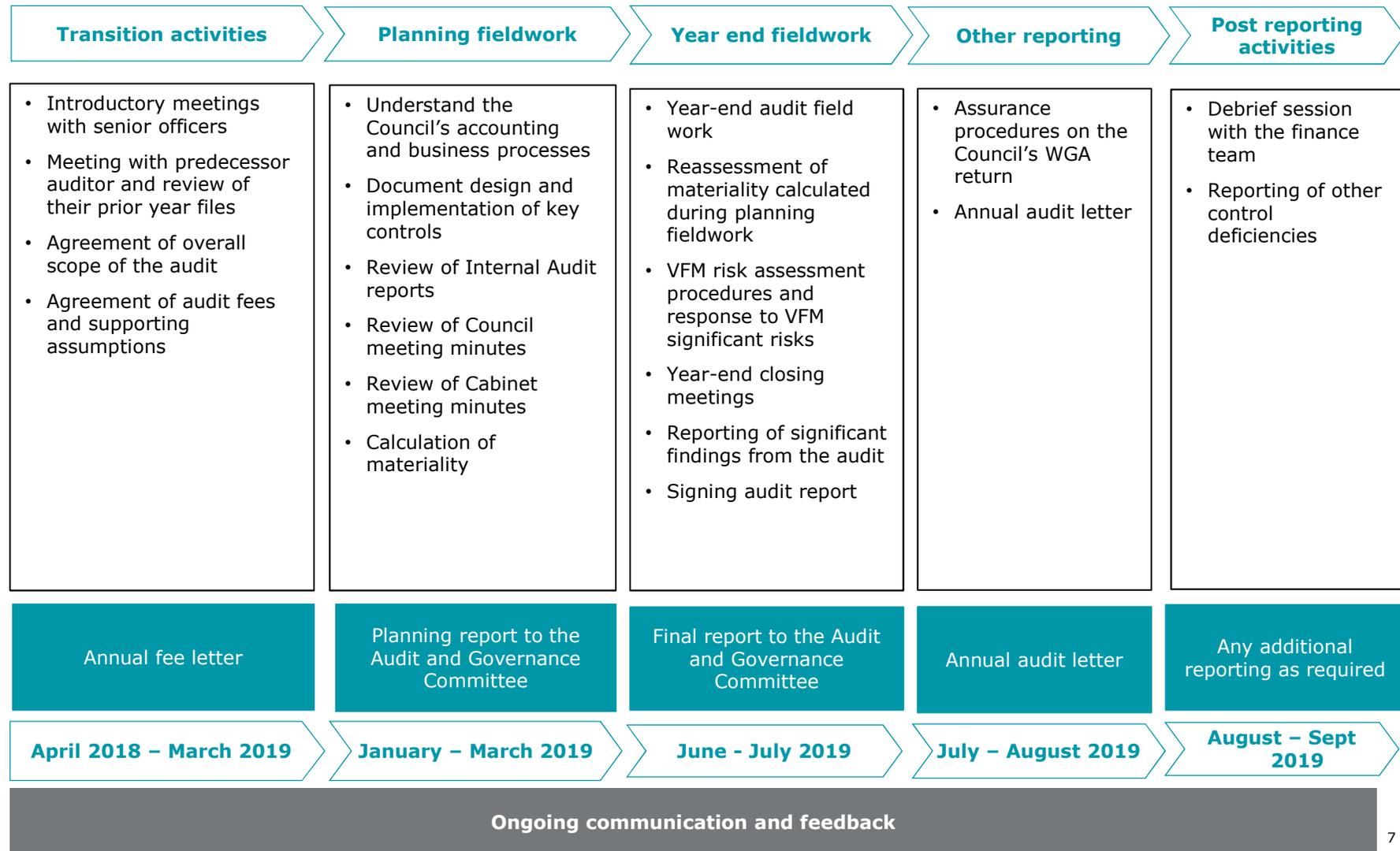
We recommend the Council complete the Code checklist during drafting of their statement of accounts.

We would welcome early discussion on the planned format of the statement of accounts, and whether there is scope for simplifying or streamline disclosures, as well as the opportunity to review a skeleton set of statement of accounts and early drafts of the narrative report and annual governance statement ahead of the typical reporting timetable to feedback any comments to officers.

Continuous communication and reporting

Planned timing of the audit

As the audit plan is executed throughout the year, the results will be analysed continuously and conclusions (preliminary and otherwise) will be drawn. The following sets out the expected timing of our reporting to and communication with you.



Significant risks – statement of accounts

Our risk assessment process

We consider a number of factors when deciding on the significant audit risks. These factors include:

- the significant risks and uncertainties previously reported in the narrative report and financial statements;
- the IAS 1 critical accounting estimates previously reported in the annual report and financial statements;
- review of board papers and management accounts;
- Discussion with management and other key stakeholders;
- our assessment of materiality; and
- the changes that have occurred in the business and the environment it operates in since the last annual report and financial statements.

Our audit planning process includes an on-going assessment of internal and external factors affecting the Council, in accordance with the requirements of International Standards on Auditing (UK and Ireland).

Presumed risk of fraud in revenue recognition

Auditing standards presume there is a risk of fraud in revenue recognition. Following an analysis of the Council's income streams, we have rebutted this presumption. The key factors considered include: the amount of annual income from each source; the transaction size; the extent of any estimates; and the complexity of the recognition principles.

Significant risks identified by the predecessor auditor

The risks we have identified as significant are summarised on the following pages. They reflect the following changes to the equivalent summary of risks identified by our predecessor for their audit of the 2017/18 accounts:

- Our predecessor identified a significant risk in relation to the valuation of the pension liability. The process of estimating the quantum of the pension liabilities is usually complex and small changes in assumptions can have a significant impact on the estimated liability. However, the Council has engaged a reputable actuary and we understand that there are no significant changes in the membership of the scheme or significant transactions in the pension scheme which impact on the valuation. For these reasons our preliminary assessment is that the risk of material misstatement is towards the higher end of the range, but is not a significant audit risk. We will update our assessment when we have received and evaluated further information on the actuary's approach and assumptions.
- Our predecessor also identified the presumed significant risk of fraud in revenue recognition, as noted above, we have rebutted this presumption.
- We have identified an additional risk in relation to the appropriate capitalisation of expenditure as the capital plan in the current year is substantial.

Significant risks

Risk 1 – Property Valuation – Fixed assets and investment properties

Risk identified The Council held Council Dwellings & Garages of £676m, other land & buildings of £41m and investment properties of £114m at 31 March 2018 which are required to be recorded at current or fair value at the balance sheet date, the significant risk identified therefore applies to these classes of assets.

Key judgements include:

- Whether there has been a material change since the date of the last valuation.
 - In the valuation of dwellings, defining appropriate beacon groups, such that the level of homogeneity of properties within each group is appropriate, and selecting appropriate comparators and, where relevant, making appropriate adjustments.
 - Whether investment properties have been valued by reference to their highest and best use.
-

Our response

- We will test the design and implementation of key controls in place around the property valuation.
- We will use our valuation specialists, Deloitte Real Estate, to review the methodology and approach and to challenge the appropriateness of the year-end valuation, focusing on the key subjective inputs.

Significant risks

Risk 2 – Capital Expenditure

Risk identified	<p>The Council has a substantial capital programme, and has budgeted £29m for capital works during 2018/19 (2017/18: £33m). Key projects include capital repair and house building schemes, as well as the new Hillhouse Leisure centre and redevelopment of the existing Epping and Loughton Leisure centres.</p> <p>Determining whether or not expenditure should be capitalised can involve judgement as to whether costs should be capitalised under International Financial Reporting Standards.</p> <p>The Council has greater flexibility of the use of revenue resource compared to capital resource. There is also, therefore an incentive for officers to misclassify revenue expenditure as capital as will impact the surplus/deficit recorded by the Council at year end.</p>
Our response	<ul style="list-style-type: none">• We will test the design and implementation of controls around the capitalisation of costs.• We will select a sample of additions in the year to test whether they have been appropriately capitalised in accordance with the accounting requirements.

Significant risks

Risk 3 – Management override of controls

Risk identified In accordance with ISA 240 (UK and Ireland) management override of controls is a presumed 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.

The key judgments in the financial statements are those which we have selected to be the significant audit risks; capitalisation of expenditure and valuation of the Council’s estate. These are inherently the areas in which management has the potential to use their judgment to influence the financial statements.

Our response In considering the risk of management override, we plan to perform the following audit procedures that directly address this risk:

- We will risk assess journals and select items for detailed follow up testing. We do this by using computer-assisted profiling to identify journals which have characteristics of increased interest. We will then test the appropriateness of journal entries selected through this profiling activity, and other adjustments made in the preparation of financial reporting.
 - We will review accounting estimates for evidence of bias that could, in aggregate, result in material misstatements due to fraud. Other areas of estimation in addition to the above include pension liability assumptions, provisions, bad debt provisions and estimation of depreciation based on a selection of useful economic lives.
 - We will obtain an understanding of the business rationale of significant transactions that we become aware of that are outside of the normal course of business for the entity, or that otherwise appear to be unusual, given our understanding of the entity and its environment.
-

Value for money conclusion

Our risk assessment process and significant risks

We are required to provide a conclusion on whether the Council has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

The Code and supporting auditor guidance note require us to perform a risk assessment to identify any risks that have the potential to cause us to reach an inappropriate conclusion on the audited body's arrangements. We are required to carry out further where we identify a significant risk - if we do not identify any significant risks, there is no requirement to carry out further work.

Our risk assessment procedures include:

- Reading the annual governance statement
- Considering local and sector developments and how they impact on the Council
- Reviewing the audit report issued by our predecessor in respect of 2017/18
- Meeting with senior officers
- Reviewing reports issued by internal audit
- Reviewing other documentation of the Council including budget setting reports, financial and operational performance monitoring reports
- Reviewing reports issued by regulators

Our risk assessment to determine whether there are any further significant risks is ongoing, in particular to update for the findings of internal audit work completed in the latter part of the year, outturn performance against financial and operational metrics and the outcome of any findings from the work of regulators.

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our respective responsibilities are set out in "PSAA Statement of responsibilities of auditors and audited bodies: Principal Local Authorities and Police Bodies." The responsibilities of auditors are derived from statute, principally the Local Audit and Accountability Act 2014 and from the NAO Code of Audit Practice. The responsibilities of audited bodies are derived principally the Local Audit and Accountability Act 2014 and from the Accounts and Audit Regulations 2015.

Our report is designed to establish our respective responsibilities in relation to the audit, to agree our audit plan and to take the opportunity to ask you questions at the planning stage of our audit. Our report includes our audit plan, including key audit judgements and the planned scope.

Use of this report

This report has been prepared for the Audit and Governance Committee, 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. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

What we don't report

As you will be aware, our audit is 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 officers or by other specialist advisers.

Finally, the views on internal controls and business risk assessment in our final report should not be taken as comprehensive or as an opinion on effectiveness since they will be based solely on the audit procedures performed in the audit of the statement of accounts and the other procedures performed in fulfilling our audit plan.

Other relevant communications

We will update you if there are any significant changes to the audit plan.



Deloitte LLP
St Albans | **13 March 2019**

Appendix 1 - Fraud responsibilities and representations

Responsibilities explained



Your Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with officers 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.



Our responsibilities:

- We are required to obtain representations from your officers regarding internal controls, assessment of risk and any known or suspected fraud or misstatement.
- As auditors, we obtain reasonable, but not absolute, assurance that the statement of accounts as a whole are free from material misstatement, whether caused by fraud or error.
- As set out in the significant risks section of this document, we have identified the risk of valuation of land and buildings, capital expenditure and management override of controls as key audit risks for your organisation.

Fraud Characteristics:



- Misstatements in the statement of accounts can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the statement of accounts is intentional or unintentional.
- Two types of intentional misstatements are relevant to us as auditors – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.

We will request the following to be stated in the representation letter:

- We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.
- We have disclosed to you the results of our assessment of the risk that the statement of accounts may be materially misstated as a result of fraud.
- We are not aware of any fraud or suspected fraud / We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity or group and involves:
 - (i) officers;
 - (ii) officers who have significant roles in internal control; or
 - (iii) others where the fraud could have a material effect on the statement of accounts.
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's statement of accounts communicated by officers, former officers, analysts, regulators or others.

Appendix 1 - Fraud responsibilities and representations

Inquiries

We will make the following inquiries regarding fraud:

Officers:



- Officers assessment of the risk that the statement of accounts may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Officers process for identifying and responding to the risks of fraud in the entity.
- Officers communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity.
- Officers communication, if any, to employees regarding its views on business practices and ethical behaviour.
- Whether officers have knowledge of any actual, suspected or alleged fraud affecting the entity.
- We plan to involve officers from outside the finance function in our inquiries.



Internal audit

- Whether internal audit has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain its views about the risks of fraud.

Those charged with governance



- How those charged with governance exercise oversight of officers processes for identifying and responding to the risks of fraud in the entity and the internal control that officers have established to mitigate these risks.
- Whether those charged with governance have knowledge of any actual, suspected or alleged fraud affecting the entity.
- The views of those charged with governance on the most significant fraud risk factors affecting the entity.

Appendix 2 - Independence and fees

Independence

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

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 Audit and Governance Committee for the year ending 31 March 2019 in our final report to the Audit and Governance Committee.
Non-audit fees	There are no non-audit fees.
Independence monitoring	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.
Relationships	We have no other relationships with the Council, its members, officers and affiliates, and have not supplied any services to other known connected parties.

Appendix 2 - Fees

The professional fees expected to be charged by Deloitte in the period from 1 April 2018 to 31 March 2019 are as follows:

	Current year £
Audit under the NAO's Code of Audit Practice: Council	49,797
Total audit fees	49,797



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