Northumberland County Council

Audit planning report

Year ending 31 March 2018

January 2018

Building a better working world

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January 2018

Northumberland County Council Audit Committee
County Hall
Morpeth
NE61 2EF

Dear Audit Committee Members

Audit planning report

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the Audit Committee with a basis to review our proposed audit approach and scope for the 2017/18 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 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.

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 on 24 January 2018 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Stephen Reid

For and on behalf of Ernst & Young LLP

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Contents

In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued "Statement of responsibilities of auditors and audited bodies". It is available from the via the PSAA website (www.PSAA.co.uk).
The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.
The "Terms of Appointment (updated February 2017)" issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and 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 Northumberland County 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 Northumberland County 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 Northumberland County 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 2017/18 audit strategy

Overview of our 2017/18 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.

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Risk of fraud in revenue and expenditure recognition	Fraud risk/ Significant risk	No change in risk or focus	Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.
Risk of management override of control	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.
Valuation of land and buildings	Inherent risk	No change in risk or focus	Land and buildings is the most significant balance on the Council's balance sheet. The valuation of land and buildings is subject to a number of assumptions and judgements. A small movement in these assumptions can have a material impact on the financial statements.
Valuation of pension liability	Inherent risk	No change in risk or focus	The pension liability is the most significant liability on the Council's balance sheet and is calculated through use of a number of actuarial assumptions. A small movement in these assumptions can have a material impact on the balance sheet.
Changes in group structure	Inherent risk	New risk for this year	The Arch Group is a wholly owned subsidiary company of the Council. In November 2017, the Arch Board released a statement setting out their intentions to wind up the Company and transfer the assets of the Arch Group to a new company. This could have a material impact a number of areas of the Group financial statements, including asset valuations, intercompany loan balances and going concern disclosures.

Overview of our 2017/18 audit strategy

Materiality

Planning materiality **£18.1m**	Group materiality has been set at £18.1 million, which represents 2% of the prior years gross expenditure on provision of services.
Performance materiality **£13.5m**	Group performance materiality has been set at £13.5 million, which represents 75% of planning materiality.
Audit differences **£0.9m**	We will report all uncorrected misstatements relating to the primary and supplementary statements in the financial statements (comprehensive income and expenditure statement, balance sheet, movement in reserves statement, cash flow statement, housing revenue account , collection fund, and firefighters' pension fund financial statements) greater than £0.9 million. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

Overview of our 2017/18 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 the Council give a true and fair view of the financial position as at 31 March 2018 and of the income and expenditure for the year then ended; and
- Our conclusion on the Council's arrangements to secure economy, efficiency and effectiveness.

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.
- 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.

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.

Risk of fraud in revenue and expenditure recognition*

What is the risk?

Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

What will we do?

We will:

- Review and test revenue and expenditure recognition policies.
- Review and discuss with management any accounting estimates on revenue or expenditure recognition for evidence of bias.
- Develop a testing strategy to test material expenditure streams, including testing revenue and capital expenditure to ensure it has been correctly classified.
- Review and test revenue cut-off at 31 March 2018.
- Review and test the completeness of expenditure around 31 March 2018.

Financial statement impact

Misstatements that occur in relation to the risk of fraud in revenue and expenditure recognition could affect the income and expenditure accounts. These accounts had the following balances in the 2016/17 financial statements:

Income Account: £964.5 million

Expenditure Account: £903.6 million

Our response to significant risks (continued)

Risk of management override of control*	What is the risk?	What will we do?
	The financial statements as a whole are not free of material misstatements whether caused by fraud or error. As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.	▶ Identifying fraud risks during the planning stages. ▶ Inquiry of management about risks of fraud and the controls put in place to address those risks. ▶ Understanding the oversight given by those charged with governance of management's processes over fraud. ▶ Consideration of the effectiveness of management's controls designed to address the risk of fraud. ▶ Determining an appropriate strategy to address those identified risks of fraud. ▶ Performing mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments in the preparation of the 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?
Valuation of Land and Buildings The value of Land and buildings represents a significant balance in the Council's financial statements and is subject to valuation changes, impairment reviews and depreciation charges. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.	We will: ▸ Consider the work performed by the Council's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work. ▸ Sample test key asset information used by the valuer in performing their valuation (e.g. floor plans to support valuations based on price per square metre). ▸ Consider the annual cycle of valuations to ensure that assets have been valued as part of a five-year rolling programme as required by CIPFA. ▸ Review assets not subject to valuation in 2017/18 to satisfy ourselves that the remaining asset base is not materially misstated. ▸ Consider changes to useful economic lives as a result of the most recent valuation. ▸ Test that the accounting entries have been correctly processed in the financial statements.
Pension Liability Valuation The Council's local government pension scheme liability is a material estimate on the Council's balance sheet. At 31 March 2017 the total value of the liability was £678 million. Calculation of the liability involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. A small movement in the assumptions can have a material impact on the value of the liability and auditing standards require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	We will: ▸ Liaise with the audit team of the Northumberland Pension Fund, to obtain assurances over the information supplied to the actuary for calculating the Council's pension liability. ▸ Assess the work of the Pension Fund actuary (AON Hewitt), including the assumptions they have used by relying on the work of PWC, the consulting Actuaries commissioned by PSAA for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team. ▸ Review and test the accounting entries and disclosures made within the Council's financial statements in relation to the pensions disclosures.

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?
Changes to Group structure The Arch Group is a wholly owned subsidiary company of the Council. In November 2017, the Arch Board released a statement setting out their intentions to wind up the Company and transfer the assets of the Arch Group to a new company. This could have a material impact a number of areas of the Group financial statements, including asset valuations, intercompany loan balances and going concern disclosures.	We will: ▸ Discuss with management the progress being made in relation to winding up the Arch Group and review any Council and other legal papers to confirm the status of the Company at the year end. ▸ Consider whether the plans for winding up the Arch Group have any impact on the valuation of the assets and liabilities held in the Group balance sheet. ▸ Review Council and other documentation to support the set up of any new companies. ▸ Review the disclosures in the financial statements to ensure that they accurately reflect the latest position of progress being made on the new group structure

03 Value for Money Risks

Value for Money

Background

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. This is known as our value for money conclusion.

For 2017/18 this is based on the overall evaluation criterion:

"In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people"

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

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

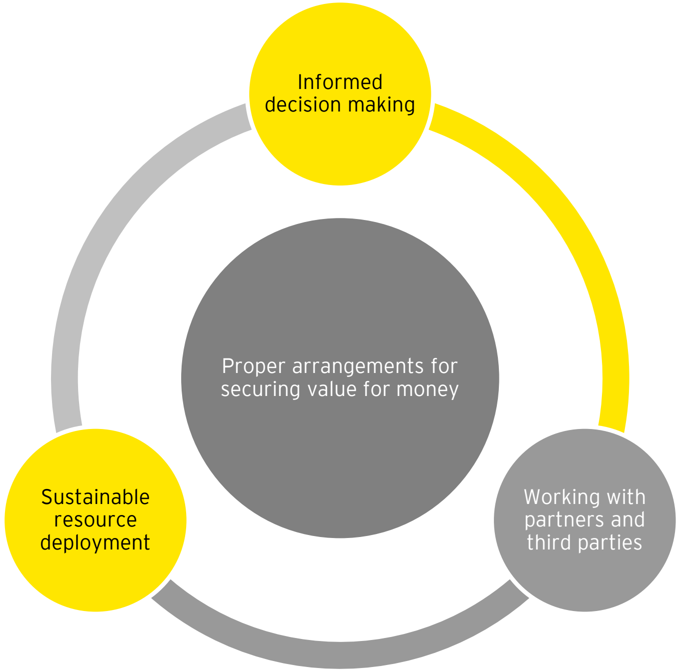
In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

We are only required to determine whether there are any risks that we consider significant, which the NAO's Code of Audit Practice defines as:

"A matter is significant if, in the auditor's professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public"

Our risk assessment supports the planning of sufficient work to enable us to deliver a safe conclusion on arrangements to secure value for money and enables us to determine the nature and extent of further work that may be required. If we do not identify any significant risks there is no requirement to carry out further work.

Our risk assessment has therefore considered both the potential financial impact of the issues we have identified, and also the likelihood that the issue will be of interest to local taxpayers, the Government and other stakeholders. This has resulted in the identification of the significant risks noted on the following page which we view as relevant to our value for money conclusion.



Value for money risks (continued)

Arrangements in place for making informed decisions

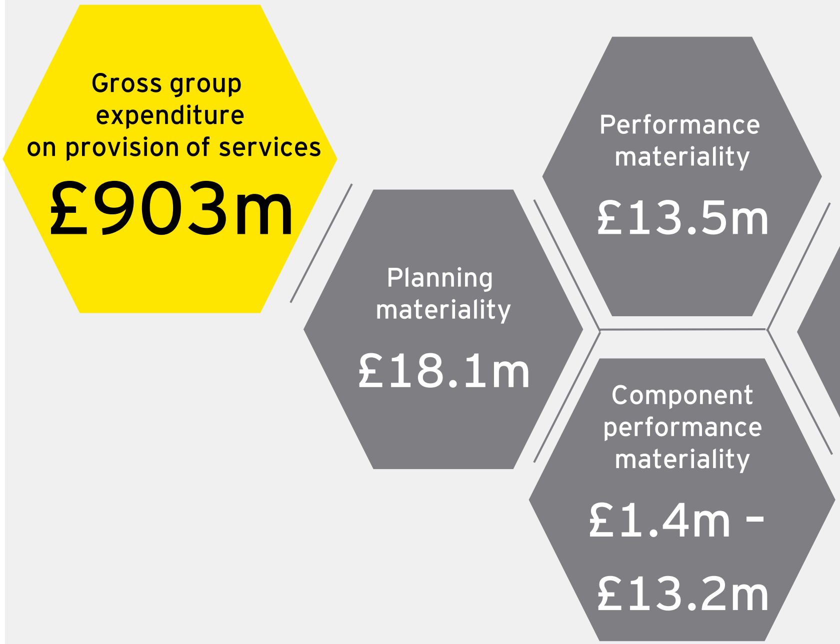
What is the risk?	What will we do?
In the period from 1 April 2017 to date the Council has made a number of high profile decisions, including: ▶ Agreeing a termination package for the former Chief Executive. ▶ Restructuring of the senior management team of the Council. ▶ Reversing the decision to move Council headquarters from the current site in Morpeth to Ashington. ▶ Withdrawal of the Local Plan. ▶ Announcing the intention to wind up the Arch Group, a group of wholly owned subsidiary companies, and transfer the assets to a new development company. The above decisions have a significant impact on the operations of the Council.	Our approach will focus on: ▶ Discussing with management the process undertaken for approval of high profile decisions. ▶ Reviewing relevant documentation from Council and Cabinet meetings alongside any external advice received in relation to each high profile decision. ▶ Considering whether the decision making process followed the policies and procedures established by the Council. ▶ Considering whether there was any other evidence that could have reasonably been expected to be made available to Members and officers to inform the decision making process.

04 Audit materiality

Materiality

Materiality

For planning purposes, group materiality for 2017/18 has been set at £18.1 million. This represents 2% of the Council's group prior year gross expenditure on provision of services. It will be reassessed throughout the audit process. We have provided supplemental information about audit materiality in Appendix D.



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 £13.5 million which represents 75% of planning materiality. We have used a threshold of 75% as we have identified limited audit adjustments in previous years.

Component performance materiality range – we determine component performance materiality as a percentage of Group performance materiality based on risk and relative size to the Group. Component materiality for the Council single entity financial statements is £13.2 million and for the Arch Group is £1.4 million.

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, housing revenue account, collection fund and firefighters' pension fund financial statements 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.

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 review and report on the Council's financial statements and 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 objective is to form an opinion on the financial statements under International Standards on Auditing (UK).

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Procedures required by standards

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

Procedures required by the Code

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

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

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.

Our Audit Process and Strategy (continued)

Audit Process Overview

Our audit involves:

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

For 2017/18 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.
- 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 meet with the Chief Internal Auditor, and 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 components 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.

For all other components we perform other procedures to confirm that there is no risk of material misstatement within those locations. These procedures are detailed below.

Scoping by Entity

Our preliminary audit scopes we have adopted are set out below. Note that these scopes are only for the purpose of the consolidated financial statements, separate statutory opinions will also be issued for all Group entities.

Council	Full scope audit
Arch	Specific scope audit

There have been no changes in scope to that designated in our 2016/17 audit.

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.

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. For the audit of the Arch Group, our initial planning procedures have identified the following accounts as material to the group financial statements:

- Gross income
- Gross expenditure
- Property Plant and Equipment
- Investment Property
- Borrowings

Group audit team involvement in component audits

Auditing standards require us to be involved in the work of our component teams. We will liaise closely with our colleagues auditing the Arch Group and review their working papers where required to support our work on the Group audit opinion.

06 Audit team

Audit team

The engagement team is led by Stephen Reid who will have responsibility for ensuring that our audit delivers high quality and value to the Council. He will supported by Caroline Mulley, the associate partner that leads the audit of the Arch Group for matters that impact the Group financial statements.

Claire Mellons will be the senior manager responsible for the day-to-day direction of audit work and is the key point of contact for the finance team.

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	Cushman & Wakefield (Management's valuation specialists) EY Valuations Team
Pensions disclosure	AON Hewitt (Management's actuarial specialists) EY Actuaries

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.
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

07 Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2017/18.

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.

Audit phase	Timetable	Audit committee timetable	Deliverables
Risk assessment and setting of scopes. Walkthrough of key systems and processes	December		
	January	Audit Committee	Audit Planning Report
Interim audit testing Value for Money work	February		
	March	Audit Committee	Interim audit update
Interim top up testing	April		
	May	Audit Committee	Interim audit update
Year end audit work	June		
Completion and reporting	July	Audit Committee	Audit Results Report Audit opinions and completion certificates

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 June 2016, 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 the 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. ▶ Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard	▶ 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 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; ▶ Written confirmation that all covered persons are independent; ▶ 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 any contingent fee arrangements for non-audit services provided by us or our network firms; 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 also provide information on any contingent fee arrangements , the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted;

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 Stephen Reid 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 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 we will comply with the policies that you have approved.

None of the services are prohibited under the FRC's ES or the National Audit Office's Auditor Guidance Note 01 and the services have been approved in accordance with your policy on pre-approval. The ratio of non audit fees to audits fees is not permitted to exceed 70%.

At the time of writing, the current ratio of non-audit fees to audit fees is approximately 6%. 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.

Relationships, services and related threats and safeguards

Other threats

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

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

EY Transparency Report 2017

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 ended 1 July 2017 and can be found here:

http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-20167

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 Communities and Local Government.

PSAA has published a scale fee for all relevant bodies. 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 NAO Code of Audit Practice.

	Planned fee 2017/18	Scale fee 2017/18	Final Fee 2016/17
	£	£	£
Total Fee – Code work	190,596	190,596	TBC
Total Fee – Housing Benefit certification work	9,341	9,341	9,900
Total Audit fee	**199,937**	**199,937**	**TBC**
Non-audit work – Other certification work	TBC	-	15,000**
Non-audit work – Tax advice	12,475	-	40,350
Total other non-audit services	**0**	**0**	**55,350**
Total fees	**212,412**	**199,937**	**TBC**

All fees exclude VAT

* We have requested a scale fee variation for the additional work undertaken in respect of the Value for Money risks in 2016/17 and we will update the Audit Committee with the final fee once this has been confirmed. Given the number of risks to the Value for Money opinion identified in 2017/18 we expect there will also be a scale fee variation for this work and we will quantify the value following our initial scoping of the work.

** We have completed our certification work on the Morpeth Bypass claim and the Teachers Pension Return. Our work on the pooling of housing capital receipts return is due to be completed by 31 January 2018; however we do not expect any issues to arise that will result in a variation to the agreed fee.

The agreed fee presented is based on the following assumptions:

- Officers meeting the agreed timetable of deliverables;
- Our financial statement opinion and value for money conclusion being unqualified;
- Appropriate quality of documentation is provided by the Council; and
- The Council has an effective control environment.

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

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

Appendix B

Regulatory update

In previous reports to the Audit Committee, we highlighted the issue of regulatory developments. The following table summarises progress on implementation:

Earlier deadline for production and audit of the financial statements from 2017/18	
Proposed effective date	Effective for annual periods beginning on or after 1 April 2017.
Details	The Accounts and Audit Regulations 2015 introduced a significant change in statutory deadlines from the 2017/18 financial year. From that year the timetable for the preparation and approval of accounts will be brought forward with draft accounts needing to be prepared by 31 May and the publication of the audited accounts by 31 July.
Impact on Northumberland County Council	These changes provide challenges for both the preparers and the auditors of the financial statements. We held a faster close workshop for clients in December 2017 to facilitate early discussion and sharing of ideas and good practice. We are now working with the Council on ideas coming from the workshop, for example: ▸ Streamlining the Statement of Accounts removing all non-material disclosure notes; ▸ Bringing forward the commissioning and production of key externally provided information such as IAS 19 pension information, asset valuations; and ▸ Re-ordering tasks from year-end to monthly/quarterly timing, reducing year-end pressure.

Appendix C

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
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

Appendix C

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
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 ▸ Corrected misstatements that are significant ▸ Material misstatements corrected by management	Audit results report
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 ▸ A discussion of any other matters related to fraud	Audit results report
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

Appendix C

Required communications with the Audit Committee (continued)

Required communications	What is reported?	Our Reporting to you When and where
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	Audit Planning Report and Audit Results Report
External confirmations	▸ Management's refusal for us to request confirmations ▸ Inability to obtain relevant and reliable audit evidence from other procedures	Audit results report
Consideration of laws and regulations	▸ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ▸ 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
Internal controls	▸ Significant deficiencies in internal controls identified during the audit	Management letter/Audit results report

Appendix C

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 Audit results report
Representations	Written representations we are requesting from management and/or those charged with governance	Audit results report
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report
Auditors report	▸ Key audit matters that we will include in our auditor's report ▸ Any circumstances identified that affect the form and content of our auditor's report	Audit results report
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 Audit results report
Certification work	Summary of certification work undertaken	Certification report

Appendix D

Additional audit information

Other required procedures during the course of the audit	
In addition to the key areas of audit focus outlined in section 2, 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 Group and 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 Group to express an opinion on the consolidated financial statements. Reading other information contained in the financial statements, including the board's statement that the annual report is fair, balanced and understandable, 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.

Appendix D

Additional audit information (continued)

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 locations at which we conduct audit procedures to support the opinion given on the Group financial statements; and
- 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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Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

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