Appendix 2

Grant Thornton

The Audit Findings (ISA260) report for Medway Council

Year ended 31 March 2020

July 2021

ISA260 Update

Contents

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Headlines

This table summarises the key findings and other matters arising from the statutory audits of the Medway Council ('the Council') for the year ended 31 March 2020 for those charged with governance. Much of the content of this report was presented to members in November 2020. **Commentary updating the reported November position is underlined** to assist and focus members' attention on the areas of change.

Covid - 19	The outbreak of the Covid-19 coronavirus pandemic has had a significant impact on the normal operations of the Council. The Council has faced extensive front-line challenges as a result of the pandemic such as administration of grants to businesses, closure of schools and car parks with additional complexities of reopening services under new government guidelines. Authorities are still required to prepare financial statements in accordance with the relevant accounting standards and the Code of Audit Practice, albeit to an extended deadline for the preparation of the financial statements up to 31 August 2020 and the date for audited financial statements to 30 November 2020.	We updated our audit risk assessment to consider the impact of the pandemic on our audit and issued an Audit Plan addendum to management in April 2020. This was shared with officers for discussion with Audit Committee members in the absence of a formal meeting due to the pandemic. In that addendum we reported an additional financial statement risk in respect of Covid -19 and highlighted the impact on our VfM approach. Further detail is set out on page 7. Restrictions for non-essential travel have meant that Council and audit staff have undertaken the accounts closedown and audit process remotely making use of remote access to financial systems and video conferencing, including screen sharing to verify information provided by the entity. Remote working requires our audit team to carry out additional tests to corroborate the completeness and accuracy of information produced by the Council which we would otherwise have performed in person on site (for example viewing a report being run from Council systems by the officer). Challenges were also faced in obtaining third party information remotely from the Council's investment and borrowing parties with the result that, at the time of writing, our audit work in respect of long and short term investments and borrowing remains in its early stages. There have been challenges for both the audit team and the Council's team to conduct the audit virtually during the pandemic. Council staff's capacity has been affected as they focus on supporting the operational response to the pandemic. In light of the above, the audit is proving more time consuming than carrying out an audit under normal circumstances. The financial statements were published and provided to the audit team on 05 August 2020.
Financial Statements	Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the Council's financial statements: • give a true and fair view of the financial position of the Council income and expenditure for the year; and • have been properly prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014. We are also required to report whether other information published together with the audited financial statements (including the Annual Governance Statement (AGS) and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.	Our audit work started in August and has been undertaken remotely. Our findings to date are summarised on pages 7 to 25. Our audit work is largely complete. The areas outstanding are shown in summary on page 5. This report sets out the current position on the audit which is now near completion subject to the resolution of a small number of items. We have identified a number of adjustments to the financial statements. Those that have been amended for in the revised statements are shown on page 45 in Appendix C. Agreed errors that have not been corrected are shown from page 46. We also identified a number of disclosure amendments agreed with management (page 48) . We have raised sixteen recommendations for management as a result of our audit work in Appendix A. Our follow up of recommendations from the prior year's audit are detailed in Appendix B. In Appendix C we note a total of 44 adjustments from our audit work, we also identified a number of more minor disclosure and formatting issues that have not been reported on.

Headlines - continued

Financial Statements - continued		Subject to the completion of the items listed on page 5, we anticipate issuing an unqualified audit opinion (Appendix E). Our anticipated audit opinion will include an Emphasis of Matter paragraph, highlighting material uncertainties around the valuation of land and buildings including investment properties, assets held for sale and council dwellings and your share of Kent pension fund assets attributable to the Council as at 31 March 2020 due to the Covid-19 pandemic. We have concluded that the other information to be published with the financial statements is consistent with our knowledge of your organisation. The number of audit adjustments and issues identified has contributed to additional audit time in undertaking the audit. This will result in a fee variance which will be discussed with the Chief Finance Officer on completion of the audit.
Value for Money arrangements	Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report if, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('the value for money (VFM) conclusion').	We have completed our risk based review of the Council's value for money arrangements. We have concluded that Medway Council does have proper arrangements to secure economy, efficiency and effectiveness in its use of resources, except for its arrangements to help and protect children in Medway. Ofsted's inspection report on the Council's children's social care services, issued on 27 August 2019, judged services to be 'inadequate'. We have updated our VfM risk assessment to document our understanding of your arrangements to ensure critical business continuity in the current environment. We have not identified any new VfM risks in relation to Covid-19. We therefore anticipate issuing a qualified 'except for' value for money conclusion, as detailed in Appendix E. Our findings are summarised on pages 26 to 33. We raised eight recommendations for management as a result of our VFM work in Appendix A.
Statutory duties	The Local Audit and Accountability Act 2014 ('the Act') also requires us to: • report to you if we have applied any of the additional powers and duties ascribed to us under the Act; and • To certify the closure of the audit.	We have not exercised any of our additional statutory powers or duties. Our work under the Code is in progress and we are on course to issue our opinion in December but are unable to issue our completion certificate until: • the required procedures in respect of the WGA have been performed.

Audit approach

Overview of the scope of our audit

This Audit Findings Report presents the observations arising from the audit that are significant to the responsibility of those charged with governance to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Its contents have been discussed with management.

As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK) and the Code, which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

Audit approach

Our audit approach was based on a thorough understanding of the Council business and is risk based, and in particular included:

- An evaluation of the Council's internal control environments, including their IT systems and controls; and
- Substantive testing on significant transactions and material account balances, including the procedures outlined in this report in relation to the key audit risks.

We have had to alter our Audit Plan, as communicated to the Audit Committee in March 2020, to reflect our response to the Covid-19 pandemic and its impact on the Council's financial statements and the Council's value for money arrangements.

Conclusion

- Our audit of the Council's financial statements is nearing completion. As at the date of writing (14 July) the outstanding items include:
- Auditor processing of information received to support actuary assumptions in relation to Pension durations.
- receipt and review of agreed audit amendments and disclosures
- receipt and review of evidence to support the treatment of two bank accounts held by the council on other parties behalf
- completion of quality review and resolution of any arising queries;
- updating our review of events after the reporting date;
- receipt of management representation letter; and
- receipt and review Whole of Government Accounts (WGA).

Summary

Our approach to materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

We have revised materiality levels from that reported in our Audit Plan due to an increase in net expenditure in 2019/20 compared to 2018/19 net expenditure.

	Council Amount (£)	Qualitative factors considered
Materiality for the financial statements	9,000,000	• We have determined materiality to be £9 million equates to 1.5% of your draft accounts net expenditure for the year.
Performance materiality	6,750,000	• We have determined performance materiality to be £6.75m, which equates to 75% of your materiality for the financial statements
Trivial matters	450,000	• We have determined triviality to be £450k which is the reporting level to those charged with governance
Specific materiality for Cash	500,000	
Specific materiality for Senior officer remuneration	100,000	

Significant audit risks

Risks identified in our Audit Plan	Auditor commentary
Covid – 19 The global outbreak of the Covid -19 virus pandemic has led to unprecedented uncertainty for all organisations, requiring urgent business continuity arrangements to be implemented. We expect current circumstances will have an impact on the production and audit of the financial statements for the year ended 31 March 2020, including and not limited to; • Remote working arrangements and redeployment of staff to critical front line duties may impact on the quality and timing of the production of the financial statements, and the evidence we can obtain through physical observation • Volatility of financial and property markets will increase the uncertainty of assumptions applied by management to asset valuation and receivable recovery estimates, and the reliability of evidence we can obtain to corroborate management estimates • Financial uncertainty will require management to reconsider financial forecasts supporting their going concern assessment and whether material uncertainties for a period of at least 12 months from the anticipated date of approval of the audited financial statements have arisen; and • Disclosures within the financial statements will require significant revision to reflect the unprecedented situation and its impact on the preparation of the financial statements as at 31 March 2020 in accordance with IAS1, particularly in relation to material uncertainties. We therefore identified the global outbreak of the Covid-19 virus as a significant risk, which was one of the most significant assessed risks of material misstatement.	Audit procedures undertaken in response to the identified risk included: • working with management to understand the implications the response to the Covid -19 pandemic had on the organisation's ability to prepare the financial statements and update financial forecasts and assessed the implications for our materiality calculations. No changes were made to materiality levels previously reported as a result of Covid-19 specifically. The draft financial statements were provided on 03 July 2020; • liaison with other audit suppliers, regulators and government departments to co-ordinate practical cross-sector responses to issues as and when they arose. Examples include the material uncertainty disclosed by the Council's property valuation expert; • evaluating the adequacy of the disclosures in the financial statements that arose in light of the Covid -19 pandemic; • evaluating whether sufficient audit evidence could be obtained through remote technology; • evaluating whether sufficient audit evidence could be obtained to corroborate significant management estimates such as assets and the pension fund liability valuations; • evaluating management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment; • discussion with management the implications for our audit report where we have been unable to obtain sufficient audit evidence. The Council's property valuation specialists reported that valuations of land and buildings, including investment properties, assets held for sale and council dwellings were subject to 'material valuation uncertainty' as at 31 March 2020 as a result of the impact of the Covid -19 pandemic on market activity, meaning that less certainty, and a higher degree of caution, should be placed on the recorded valuation of these assets than would otherwise be the case. We recommended management appropriately include an uncertainty disclosure in Note 4 to the Council's financial statements, and have updated the disclosure to include a sensitivity analysis as a result of audit challenge. Kent Pension Fund has disclosed a 'material valuation uncertainty' in relation to the directly held property and pooled property funds within the assets of the pension fund. Your share of these assets are material. We recommended you also include within Note 4 the material valuation uncertainty disclosure in respect of the Fund assets. These disclosures will be referred to in our auditor's reports for the Council in an emphasis of matter paragraph. This does not constitute a qualification of the audit opinion. <u>Our review is complete and no further issues have been identified which are required to be reported to those charged with governance.</u>

Significant audit risks

Risks identified in our Audit Plan	Auditor commentary
The revenue cycle includes fraudulent transactions (rebutted)	Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. In our Audit Plan we reported that having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Council, we had determined that the risk of fraud arising from revenue recognition could be rebutted, because: • there is little incentive to manipulate revenue recognition; • opportunities to manipulate revenue recognition are very limited; • the culture and ethical frameworks of local authorities, including the Medway Council, mean that all forms of fraud are seen as unacceptable. Therefore we did not consider this to be a significant risk for Medway Council. Our assessment remains consistent with that reported in our Audit Plan.
Management override of controls Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities. In particular journals, management estimates and transactions outside the course of business are areas susceptible to management override.	Audit procedures undertaken in response to the identified risk included: • evaluation of the design effectiveness of management controls over journals; • analysis of the journals listing and determining criteria for selecting high risk unusual journals; • testing unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration; • gaining an understanding of the accounting estimates and critical judgements made by management and considered their reasonableness with regard to corroborative evidence; • evaluating the rationale for any changes in accounting policies, estimates or significant unusual transactions. Our journal testing identified two journal errors which resulted in balance sheet classification errors. (refer to page 39) Last year we reported that no audit evidence could be provided to demonstrate that a key management control was operating as designed. On receipt of journals from directorates into the 'receipt inbox', members of the Finance team carry out a review of the journals for appropriateness, separation of duties and authorisation within directorates, prior to approving the journals within the 'ready for processing' inbox for other members of the team to post the journal into the ledger. We understand this remained unchanged during the audit year. Our review is complete and no further issues have been identified which are required to be reported to those charged with governance.

Significant audit risks

Risks identified in our Audit Plan	Auditor commentary
Valuation of land and buildings including council dwellings You revalue your assets as follows: • operational land and buildings on a rolling five-yearly basis • council dwellings based on a rolling five-year approach using underlying valuations of beacon properties; and • Investment Properties on a yearly basis. The Council revalues its 'other land and buildings' and Council Dwellings on a rolling five-yearly basis. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved (£539 million as at 31 March 2019) and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the financial statements is not materially different from the current value or fair value at the 31 March for those assets not revalued in the year. The Council also revalues its Investment Properties on an Annual basis (£17 million as at 31 March 2019, on a fair value basis. Like the other valuations obtained this represents a key estimate that is sensitive to changes in key assumptions. We therefore identified valuation of land and buildings, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement, and a key audit matter.	Audit procedures undertaken in response to the identified risk included: • evaluating management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work; • evaluating the competence, capabilities and objectivity of the valuation expert; • writing to the valuer to confirm the basis on which the valuation was carried out to ensure that the requirements of the Code are met; • engaging our own valuer to assess the instructions to the Council's valuer, the Council's valuer's report and the assumptions that underpin the valuation; • testing revaluations made during the year to see if they had been input correctly into the Council's asset register; • assessing the value of a sample of assets in relation to market rates for comparable properties; • testing a sample of beacon properties in respect of council dwellings to consider whether their valuation assumptions are appropriate and whether they are truly representative of the other properties within that beacon group. See our comments on page 7 on Covid material valuation uncertainty. Additionally, we note surplus assets of £40.7m includes 'Other Land and Building' Pentagon site which in our view has been incorrectly disclosed as a surplus asset. These should be disclosed as Other land and building. We also identified non material assets not revalued in line with your accounting policy (refer to page 34). Our review is substantially complete. We report at page 19 one key matter in respect of additions in the year that impacted on the carrying value of assets on the balance sheet. This issue also had a prior period impact on the General Fund.

Significant audit risks

Risks identified in our Audit Plan	Auditor commentary
Valuation of pension fund net liability The Council's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements. The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£261 million in the Council's balance sheet as at 31 March 2019) and the sensitivity of the estimate to changes in key assumptions. We therefore identified valuation of the Council's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement, and a key audit matter.	Audit procedures undertaken in response to the identified risk included: • updating our understanding of the processes and controls put in place by management to ensure the Council's pension fund net liability is not materially misstated and evaluated the design of the associated controls; • evaluating the instructions issued by management to their expert (actuary) for this estimate and the scope of the actuary's work; • assessing the competence, capabilities and objectivity of the actuary who carried out the pension fund valuation; • assessing of the reasonableness of the actuary's assumptions and calculations in-line with the relevant standards, including their consideration of the ongoing impact of the McCloud and Guaranteed Minimum Pension cases; • assessing the accuracy and completeness of the information provided by the Council to the actuary to estimate the liability; • testing the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary; • undertaking procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report; and • obtaining assurances from the auditor of Kent County Pension Fund as to the controls surrounding the validity and accuracy of membership data, contributions data and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements (assurance received 11 November 2020). We are aware that the Kent Pension Fund disclosed a 'material valuation uncertainty' in relation to the directly held property and pooled property funds within the assets of the pension fund. Your share of these assets are material. We recommended you include within Note 4, the pension material valuation uncertainty disclosure in line with the requirement of the Code {paragraphs 3.4.2.90 – 91}. Our work is complete and no material issues have been identified which are required to be reported to those charged with governance.

Significant audit risks

Risks identified in our Audit Plan	Auditor commentary
Minimum Revenue Provision (MRP) Management reported in January 2020 to the Audit Committee, that a review by its treasury advisors had revealed an "over provision" of MRP over a number of years. Management proposes to offset the "over provision" against future years MRP contributions starting in 2019/20 onwards. The net value of "over provision" to be offset against future years is £15.7 million. Our interpretation of the Regulations is that an authority must determine an amount of MRP which it considers to be prudent as outlined in The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 – Regulation 28. As MRP is a statutory charge, once an authority determines its charge for the year, that is accounted for in the financial statements". Any errors subsequently found in the calculation in our view should be corrected by adjusting debits or credits in the year that the discovery was made. Where these errors relate to the capital financing requirement (CFR), then it would be the CFR position that is corrected and we would expect MRP to be derived from that updated CFR position going forward. In our view, the only allowance for correction of an error in the statutory guidance is in relation to the calculation of adjustment A, however any correction would not be retrospective. The interpretation of the regulations and statutory guidance is a legal issue rather than an accounting issue and we have recommended the Council seek its own legal advice as soon as possible.	Audit procedures undertaken in response to the identified risk included: • evaluating the Council's MRP accounting treatment for appropriateness and compliance with the CIPFA accounting standards and the Local Authorities Regulations 2003; • considering your legal advice regarding the treatment of previous MRP provisions. The statutory requirement for the General Fund is simply to make a prudent provision to clear any CFR, and local variations outside of the examples in the statutory guidance are permitted, providing they lead to a prudent provision being made. The updated statutory guidance (paragraph 25) comments on the Adjustment A provisions and acknowledges that if errors had been made in the calculation of MRP under the statutory methods then adjustments can be made to reduce MRP to its 'proper level'. The impact of this change for 2019/20 is that under a 'corrected' calculation of your capital financing requirement (includes Adjustment A that had been excluded from 2015/16 and the removal of double counting of SCA approvals) the MRP on an annuity basis would be £3.371m. The actual MRP charge in 2019/20 is £1. The Council intend to charge to the accounts £1 for the following 5 years. The 'calculated' MRP charge based on its adopted methodology for the period 2019/20 to 2025/26 is £19.96m. In arriving at your decision, the Council has had regard to the statutory guidance in arriving at its determination of MRP, following one of the recommended basis for calculating its MRP. You also considered the advice of informed experts, sought the view of the Monitoring Officer and kept us as your external auditors of your plans. In line with your procedural process, the decision was approved by Full Council in February 2020 as part of your 2020/21 Treasury Management Strategy. In our view, the decision on what is a prudent MRP charge is for the Council and interpretation of the regulations and statutory guidance is a legal issue rather than an accounting issue. As set out above, the Council Officers satisfied themselves that changes to MRP met statutory requirements and this was supported by a legal view from your Monitoring Officer. Our view remains unchanged that in our opinion, the statutory guidance does not allow a retrospective correction and therefore potentially, the Council's approach is not following the statutory guidance. However, we are not minded to challenge the Council's decision. In reaching our conclusion, we took into account the following: • in prior years the Council has provided more MRP than it was required to from following one of the prescribed methods in the statutory guidance, due to a technical error; • your planned response merely reflects this past over provision and the profile of MRP going forward over the next 50 years demonstrates that your debt liabilities are being covered; • the difference between the 'corrected' calculated MRP and the MRP charged in any one year is not material; • paragraph 17 of the Statutory guidance notes that Regulation 28 of the 2003 Regulations gives local authorities flexibility in how they calculate MRP, providing the 'calculation' is prudent and in arriving at a prudent provision, local authorities are required to have regard to the guidance; and • you are not relying on a 'change of method' to calculate the MRP and not contradicting paragraph 29 of the statutory guidance.

Significant audit risks

Risks identified in our Audit Plan	Auditor commentary
Minimum Revenue Provision (MRP) continued	Notwithstanding the above, from the perspective of current and future taxpayers, the Council should reconsider its decision to apply the 'correction of prior year MRP' over the short time frame of six years and assess if it would be more equitable to spread the 'correction' over a much longer period.

Significant findings – other issues and risks

This section provides commentary on issues and risks which were identified within our Audit Plan and during the course of the audit and a summary of any significant control deficiencies identified during the year.

Issue	Commentary	Auditor view
IFRS 16 implementation has been delayed by one year Although the implementation of IFRS 16 has been further delayed to 1 April 2022, audited bodies still need to include disclosure in their 2021/22 statements to comply with the requirement of IAS 8 para 31. As a minimum, we would expect audited bodies to disclose the title of the standard, the date of initial application and the nature of the changes in accounting policy for leases within the 2021/22 statements.	Management disclosed in Note 2 to the financial statements the title, date of initial application and the nature of changes in accounting policy which would arise from IFRS 16 implementation.	For 2021/22, management will need to be in a position to provide a monetary estimate of the impact on assets, liabilities, income, expenditure and reserves of the transition to IFRS 16 to allow for auditor assessment of the adequacy of associated disclosures in the financial statements. We will review the estimated impact on the financial statements as at 31 March 2022 as part of the 2021/22 audit. As part of your on-going IFRS 16 preparations for implementing the standard, we would recommend you consider the following: • documenting your arrangements for ensuring the completeness of leases, and • considering the risk of impairment on lease asset values as at 1 April 2022 due to Covid - 19 and the level of uncertainty around the asset values.

Significant findings – other issues and risks continued

Issue	Commentary	Auditor view
Dedicated schools grant reserve The Council is currently forecasting a negative balance within the Dedicated Schools Grant reserve of £9.6 million. CIPFA and the Department for Education (DfE) issued a joint statement which confirms there is no statutory basis for having a negative earmarked DSG reserve. In October 2019 the DfE launched a consultation on changing the conditions of grant and regulations applying to the DSG. In summary, the consultation proposed changes with the intention of requiring DSG deficits to be carried forward to future years' schools' budgets, with no requirement for deficits to be covered by general reserves. Our view is changing the conditions of the grant would not be sufficient in isolation to achieve the Government's intention to require overspends to be carried forward and not charged against general reserves, as this would be at odds with the requirements of proper accounting practice and the Code. DfE's most recent consultation response indicates that CIPFA, MHCLG and DfE are working on issuing guidance about the changes. .	Audit procedures to be undertaken in response to the identified risk include: • reviewing your disclosure of DSG negative year end balance against the latest available guidance; • discussing with you any updates to DSG accounting treatment and disclosures as they are issued by CIPFA, MHCLG and DfE. Management have produced a briefing paper to support their accounting treatment of DSG overspends which they consider to be in accordance with CIPFA Bulletin 05. Management interpreted the bulletin to mean that a Local Authority can carry forward any overspends on DSG as a negative usable reserve rather than deducting from the general fund balance. The £9.3m negative DSG reserve is netted off other earmarked reserves (Note 20 Movements in Earmarked Reserves)	Although we agree that management are complying with CIPFA Bulletin 05, we do not consider that this is consistent with CIPFA Code LAAP bulletin 99 which neither anticipates nor allows for a voluntary earmarked balance to be presented in a deficit position. We however recognise that more clarity is required from CIPFA and note that a statutory override is proposed for 2020/21. We have therefore raised this as a misclassification error between reserves in Appendix C.

Significant findings – other issues and risks continued

Issue	Commentary	Auditor view
Group accounts Medway Council has two subsidiaries (Medway Commercial Group and Medway Development Company) and two joint ventures (Medway Norse Limited and Medway Norse Transport) over which it has controlling interest. Management reported to the January 2020 Audit Committee that group accounts would not be required in 2019/20 as the Council's share of net assets is immaterial to the financial statements. From our review of the supporting papers based on the latest management accounts forecasts of the subsidiaries, we are not minded to disagree with management's judgement. We will continue to reassess management's judgements as the entities latest financial data become available. . .	Audit procedures to be undertaken in response to the identified risk include: • revisiting management's judgement on receipt of the draft or audited accounts for each of your subsidiaries; • reviewing your disclosure of significant judgements.	We note the following in respect of the subsidiary Medway Commercial Group (MCG): • MCG has formally changed it's name to Kyndi Limited • Medway Council loaned MCG £2.5m repayable over 10 years • MCG has now repaid Medway Council for services owed of £4.1m in March 2021 We recommend these arrangements are disclosed in the Event after reporting period note. We will also require specific representation in respect of MCG on-going audit.

Significant findings – key estimates and judgements

Accounting area	Summary of management's policy	Auditor commentary	Assessment
Provisions for NNDR appeals – £5.8m	The Council is responsible for repaying a proportion of successful rateable value appeals. In 2019/20, management calculated the level of provision required based upon the latest information about outstanding rates appeals and previous success rates. We challenged the reduction in long term business rates appeals provision as at 31 March 2020.	Audit procedures being undertaken in response to the identified issue include: • appropriateness of the underlying information used to determine the estimate; • impact of any changes to valuation method; • consistency of estimate against peers/industry practice; • reasonableness of decrease in estimate • adequacy of disclosure of estimate in the financial statements. We noted the Council changed its method of calculating the NNDR appeals Provisions for those raised under the new NNDR list which began in 2017. The method involves engaging with Analyse Local to calculate the NNDR Appeals provision and has resulted in a reduced provision compared with the previous method. Our audit work has identified no issues with the method adopted. We also note long term business rates provision has moved from £7m to nil in the current year due to the end of the 100% retention pilot, hence 50% of the value now related to central government. We challenged the reasonableness of this and understand the disclosure is incorrect and £3.4m of the year end provision should be classified as long term.	● **(Orange)**
Land and Buildings – Council Housing – £161m	The Council owned 2,293 dwellings as at 31 march 2020 and is required to revalue these properties in accordance with DCLG's Stock Valuation for Resource Accounting guidance. The guidance requires the use of beacon methodology, in which a detailed valuation of representative property types is then applied to similar properties. The Council has engaged its internal valuers to complete the valuation of these properties. The year end valuation of Council dwelling stock was £161milllion, a net decrease of £5.7m from 2018/19. Council dwelling were valued as at and 31 March 2020.	Audit procedures being undertaken in response to the identified issue include: • We have assessed management's expert, internal valuer, to be competent capable and objective; • The valuer has correctly prepared the valuation using the stock valuation guidance issued by MHCLG, and has ensured the correct factor has been applied when calculating the Existing Use Value – Social Housing (EUV-SH) value disclosed within the accounts; • All properties were valued as at 01 April 2019 and the valuer issued a follow up report commenting on market changes to the 31 March 2020 to correctly state the value of the portfolio in current terms. Our work is substantially completed. No material issues have arisen in relation to the valuation of the Council's housing stock included within the accounts. Subject to our final review, there are no issues to bring to your attention.	● **(Green)**

Assessment

- ● We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- ● We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
- ● We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
- ● We consider management's process is appropriate and key assumptions are neither optimistic or cautious

Significant findings – key estimates and judgements

Accounting area	Summary of management's policy	Auditor commentary	Assessment
Other Land and Buildings – £312m; **Investment Properties - £16.7m,** **Assets held for sale - £32.8m, and Surplus assets - £57m**	Other land and buildings comprise specialised assets, such as schools and libraries, which are required to be valued at depreciated replacement cost (DRC) at year end, reflecting the cost of a modern equivalent asset necessary to deliver the same service provision. The remainder of other land and buildings are not specialised in nature and are required to be valued at existing use in value (EUV) at year end. Investment property, assets held for sale (AHfS) and surplus assets are required to be valued at fair value. You have used both your internally and externally qualified RICS valuers to complete the valuation of properties on a five yearly cyclical basis. Land and buildings, investment properties, AHfS and surplus assets were valued as at 01 October 2019 and 28 February 2020.	Our review includes: • assessing your In-house valuer is competent, capable and objective. • carrying out completeness and accuracy testing of the underlying information used in determining the estimates, • checking the valuation method remains consistent with the prior year. • confirming the consistency of estimates against the Gerald Eve report on property market trends, and reasonableness of the increases/decreases in the estimates. • agreeing the valuation reports to the fixed asset register and the financial statements. Other than the material valuation uncertainty referred to on page 9, we also note that £0.68m assets have not been valued within the last five years which is not in accordance with the Code and your accounting policy. Our work is complete and there are no issues to be reported to those charged with governance.	● **(Green)**

Assessment

- ● We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- ● We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
- ● We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
- ● We consider management's process is appropriate and key assumptions are neither optimistic or cautious

Significant findings – key estimates and judgements

<table>
<tr><th>Accounting area</th><th>Summary of management's policy</th><th>Auditor commentary</th><th>Assessment</th></tr>
<tr><td>Net pension liability – £265m</td><td>Your net pension liability at 31 March 2020 is £265m. The Council used Barnet Waddingham to provide actuarial valuations of its assets and liabilities derived from these schemes. A full actuarial valuation is required every three years. A full actuarial valuation was carried out as at 31 March 2019 and used in determining the contribution rates with effect from 01 April 2020 to 31 March 2023. Given the significant value of the net pension fund liability, small changes in assumptions can result in significant valuation movements.</td><td>

We have assessed the actuary, Barnet Waddingham, to be competent, capable and objective;
We have performed additional tests in relation to accuracy of contribution figures and benefits paid to gain assurance over the 2019/20 calculation carried out by the actuary;
We have used PwC as our auditor's expert to assess the actuary and assumptions made by the actuary – see table below for out comparison of actuarial assumptions:

<table>
<tr><th>Assumption</th><th>Actuary Value</th><th>PwC range</th><th>Assessment</th></tr>
<tr><td>Discount rate</td><td>2.35%</td><td>2.35%</td><td>●</td></tr>
<tr><td>Pension increase rate</td><td>2.75%</td><td>2.65 – 2.8%</td><td>●</td></tr>
<tr><td>Salary growth</td><td>2.95%</td><td>3 – 4%</td><td>●</td></tr>
<tr><td>Longevity at 65 for pensioners Male</td><td>23.2</td><td>21.4 – 23.3 yrs</td><td>●</td></tr>
<tr><td>Longevity at 65 for pensioners Female</td><td>23.7</td><td>23.7 – 24.7 yrs</td><td>●</td></tr>
</table>

We have confirmed the controls and processes over the completeness and accuracy of the underlying information used to determine the estimate;
We have confirmed there were no significant changes in 2019/20 to the valuation method;
Our work to date confirms that the decrease in the IAS 19 estimate is reasonable.
We identified the council's IAS 19 report appropriately updated the impact of the McCloud judgement for the 2019/20 position.

In respect of the assumptions, we continue to recommend that management keeps these under review for future periods in order to ensure that they remain appropriate to your circumstances.

<u>Our work is complete and there are no issues to be reported to those charged with governance.</u></td><td>● (Green)</td></tr>
</table>

Assessment

- ● We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- ● We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
- ● We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
- ● We consider management's process is appropriate and key assumptions are neither optimistic or cautious

Other findings – matters discussed with management

This section provides commentary on the key matters we discussed with management during the course of the audit.

Significant matter	Commentary	Auditor view
Note 21 PPE additions	Our sample testing of PPE additions identified three errors. They were: • capital addition of an embedded lease was capitalised using the wrong value. This resulted in capital additions being overstated by £5k and Creditors being overstated by the same amount. • capital spend that was only partially capitalised and the balance of £10k was incorrectly charged to revenue expenditure rather than capital. This resulted in capital asset being understated by £10k and revenue expenditure being overstated by an equal amount. • staff costs attributable to capital schemes were capitalised as per IAS16, however the Council were not able to provide a clear basis on how the capitalised amount had been determined. Further testing confirmed the Council had used a variety of methods to work out the salary recharge to capitalise; • using timesheets to identify the time directly attributable to the capital project by the individual; • using charge out rates for the individual, which would be similar to commercial rates third parties would charge the council; or • applying percentages to contracts managed by project leads to the contracts value to determine the capital value of their time. The Council estimation method noted above is a historic practice and may go back several years. This identified concerns that the Council was not capitalising staff time based on the cost to the authority as per IAS16. After further work by the Council, it identified via revenue codes the population this related to which was £3.7m in value. Due to the way the Council has captured this information, establishing the exact capital cost was not possible for all the capital spend. Therefore, the Council asked the departments to estimate the time staff had spent on capital projects to judge what the capital spend would have been. On this basis the Council determined an estimate of over-capitalised salary costs of up to £1.2m and therefore understated revenue expenditure by the same amount. We have reviewed the Council's method for estimating the error and deem it reasonable.	We concluded as follows: • extrapolating this error has a trivial impact on the accounts. • extrapolating this error has a trivial impact on the accounts. • Of the £3.7m capitlaised, the Council identified over-capitalised salary costs up to £1.2m in 2019/20 and therefore understated revenue expenditure by the same amount which currently remains unadjusted. • In addition the capitalised staff costs of £3.4m of the £3.7m was incorrectly classified as income rather than revenue expenditure. The net impact is to overstate expenditure and income by an equal value. The Council has adjusted the CIES in respect of this error. The balance of £0.3m was correctly treated. As estimation method may go back several years, we asked management how it has assured itself of the following: • The impact on the opening balance of assets valued at fair value and at historical costs (Infrastructure assets NBV £137m as at 31 March 2020), and the revenue impact on the General Fund. The audit team noted the need to consider the impact of this issue on the prior period. In doing so both the impact on the Balance Sheet, CIES and the General Fund needed to be considered.

Other findings – matters discussed with management

This section provides commentary on the key matters we discussed with management during the course of the audit.

Significant matter	Commentary	Auditor view
Note 21 PPE additions	Following our discussion with the Council on this issue management produced a paper that set out what the prior period impact was and also noted a further error with regards to the classification of revenue and capital spend. The following key points were noted: • The error identified went back at least 6 years and may go back further. However management noted the maximum period that could be considered for the prior period impact would be the date IFRS accounting standards were implemented, which is 10 years ago. • The error of £1,230k impacted infrastructure assets by £560k and assets that are revalued by £670k. • Management identified in their review that over the same period, they had overcharged revenue on work that should have been capitalised. They identified in 2019/20 that the value of this was £774k and that similar misstatements had occurred in each of the previous 6-10 years. Management noted that this would offset the error (£560k), we identified for infrastructure assets. • The paper then set out that this left the issue sitting with assets that were revalued as part of the rolling revaluation programme on a regular basis, meaning their valuation would be corrected in the CIES and the Balance sheet. • However they did note the impact of the statutory adjustments would mean the General fund would of received a benefit due to this. The Council therefore extrapolated the impact of this over a period of 6 years which is the period they knew for certain the issue existed and another for ten years which is when IFRS standards were adopted. The Council calculated an impact on the General fund in the range of £2.4m to £4.7m. • The Council noted this is not material and does not qualify as a prior period adjustment and has determined not to adjust the accounts.	We concluded as follows: • Considering the adoption of IFRS as a cut off point for the prior period impact is reasonable. As the Council is not clear if this practise existed beyond the past 6 years we have noted the error's potential range, using the extrapolation on both a period of 6 years and 10 years. • In respect of capital spend on Infrastructure assets, the expenditure the Council had put to revenue was capital in nature and this expenditure existed over the same period and this largely negates the impact on Infrastructure assets of the error. • Our review of the (£670k) impact in 2019/20, noted that the Balance sheet valuation of these assets would not be overstated by greater than triviality due to the revaluation of the majority of these assets on an annual basis. • We agree with the Council's assessment that the remainder of the impact for prior years, therefore sits in the General Fund reserves. This effectively means unusable reserves are understated and the usable reserves are overstated. • Our review of the Council's extrapolation found that incorrect figures had been used to produce the extrapolation. We therefore asked management to revisit this and subsequently the total impact was estimated as being between £1.5m and £2.2m. This would be offset by the £670k, giving a potential prior period impact on the general fund in the range of £0.8m to £1.6m. • The auditor is not minded to challenge managements view on the prior period adjustment but has taken this to the unadjusted errors disclosed in Appendix C.

Other findings – matters discussed with management

This section provides commentary on the key matters we discussed with management during the course of the audit.

Significant matter	Commentary	Auditor view
Note 21 PPE valuation	We note that £0.68m assets have not been valued within the last five years which is not in accordance with the Code and your accounting policy.	In our view, these assets are not revalued in accordance with your policy or the Code. Based on our review, we are satisfied that these assets are not materially misstated. We recommended in appendix A the Council put in arrangements for valuing these assets inline with your policy or the Code.
Note 26 Financial instruments	We are following up a number of disclosure inquiries with the finance team which include: • lack of an accounting policy for material financial assets at FVTPL • non inclusion of material cash balances which are financial instruments • fair value movement on financial assets measured at FVOCI as a charge to SDPS • transaction disclosures in current and prior year not in accordance with the Code.	Following discussions with management this note was updated. Our review is complete and there are no further issues to bring to your attention.
Note 30 Bad Debt Provision	Our testing of the expected credit loss (Bad Debt provision) identified the following issues; • In response to our audit challenge, the Council updated the model for calculating expected credit losses for council tax which identified that the provision is understated by £3.6 million. • The Council had a debtor balance with Medway Commercial Group (MCG) with a value of £4.1m of which £2.7m is greater than one year. We note that none of the debt has been impaired. • Furthermore, the Council has not set policy for expected credit losses for Trade receivables.	We reviewed the revised basis for estimating the expected credit losses and were satisfied it was reasonable. Management has elected not to adjust the level of provision for expected credit losses (refer appendix C Unadjusted misstatements). We recommended in appendix A the Council set a policy for expected credit losses for Trade receivables.

Other findings – matters discussed with management - continued

This section provides commentary on the significant matters we discussed with management during the course of the audit.

Significant matter	Commentary	Auditor view
Note 32 Cash and cash equivalents	Our testing identified academies' bank accounts with cash balances that should have been transferred to the respective academies. We made a recommendation in appendix A.	We note from our creditor bank account testing that 4 out of our sample of 5 reconciling items remain uncleared as at 30 September 2020, some 6 months after year end. From our work we noted that the Council were not able to provide evidence of the payments authorisation evidence for 3 of the 4 reconciling items. We made a recommendation in appendix A.
Deficit on provision of services	Our sample testing of revenue expenditure identified internal recharges incorrectly included in both expenditure and income within the Deficit on the Provision of Services. The Council performed an exercise to identify the value of internal recharges incorrectly included. The result was expenditure and income was overstated by £4,411k.	Following a review of the exercise undertaken by management, we are satisfied that revenue expenditure and income is fairly stated after adjusting for the error. The error adjustment has no impact on the reported Deficit on the Provision of Services. We made a recommendation to help management improve the process for capturing internal recharges in appendix A.
Pooled Budgets	Our review of the Pooled Budgets note 12 identified that the council had accounted for the joint working arrangement on a gross basis. This treatment was inconsistent with IFRS 11 and IFRS 15 principles of revenue and expenditure recognition. Following discussions with the councils officers, it was identified that these principles had not been applied to this treatment in the note or the CIES. The Council therefore revisited this disclosure and identified which elements belonged to the council and the CCG within the Better Care Fund.	Following a review of the exercise undertaken by management, we are satisfied that the restated value in 2019/20 of £9.927k is accurate. The council also considered the prior period impact and if there was the need for a prior period adjustment. In doing so they identified the impact in the prior year was to overstate income and expenditure by £9,258k. This had no bottom line impact within the Statement of Accounts. However as the movement was material in the prior year this required the council to restate all impacted notes and provide enhanced disclosures regarding this.

Going concern

Our responsibility

As auditors, we are required to “obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern” (ISA (UK) 570).

Going concern commentary

Management's assessment process

The Council’s financial statements fund have been prepared on a going concern basis, as disclosed in the Narrative report and Statement of Responsibilities for the Statement of Accounts.

Management provided the Medium Term Financial Strategy extending over the three-year period to March 2023. Management’s assessment acknowledges that the financial outlook for the Council is challenging, with a £2m net overspend forecast for 2020/21 after accounting for Covid -19 pandemic and its ensuing impact. The Council has an on-going service transformation programme to align future spending plans to its strategic priorities with the joint goals of bridging this gap and ensuring better outcomes for residents.

As a result of increased expenditure and diminished income, for instance from parking and commercial rents, due to the Covid -19 pandemic, the original 2020/21 budget is now forecast to overspend by over £2m. The majority of this will be offset by government funding and the use of the prior year underspend.

The situation beyond 2020/21 is more uncertain as the longer-term impact of the pandemic on individuals and businesses in the Borough, and by consequence demand for services, remains unclear. Work is underway to prepare the Medium Term Financial Strategy and Capital Strategy, both of which will be presented to the Cabinet in November 2020, with plans being developed to enable Members to evaluate options that may be required to deliver savings to achieve a balanced budget for 2021/22.

Work performed

Our review of going concern disclosures is substantially complete. Our review includes review of management’s disclosures, going concern assessment and Medium Term Financial Strategy, corroborating key inputs and assumptions to our wider knowledge gained through the audit process, and where applicable to supporting documentation. We will consider, based on our understanding of the Council and the wider political and economic climate, whether material uncertainties exist which were not explicitly covered by management’s assessment. We note management prepared a going concern paper for audit purposes to support the going concern basis of the accounts. We recommend a similar paper be prepared for Those Charged with Governance (Audit Committee) in line with good practice.

Our initial conclusion is management’s assessment is based on accurate information and prudent assumptions around future income and expenditure levels, and likely shortfalls based on known events and best available information. We are satisfied that the Council holds sufficient useable reserves to mitigate the risk of any short-term funding shortfalls which may arise throughout the period of management’s assessment. We will complete our review on receipt of management’s cashflow forecast to at least December 2021.

Concluding comments

Subject to the satisfactory conclusion of our work, we are satisfied from the work performed that:

- the going concern basis of preparation is appropriate for the Council’s financial statements
- no events or conditions exist which may give rise to material uncertainties casting significant doubt on the Council’s ability to continue as a going concern
- the disclosures in the Council’s financial statements relating to going concern are adequate.

Subject to the satisfactory conclusion of our work, our draft audit opinion in respect of going concern will be unmodified.

Other matters for communication

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

Issue	Auditor commentary
Matters in relation to fraud	We have previously discussed the risk of fraud with the Audit Committee. We have not been made aware of any incidents in the period and no issues have been identified during the course of our audit procedures.
Matters in relation to related parties	We are not aware of any related parties or related party transactions which have not been disclosed.
Matters in relation to laws and regulations	You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.
Written representations	A letter of representation will be requested for the Council at the conclusion of the audit with specific representation on MCG on-going audit.
Confirmation requests from third parties	We requested from management permission to send confirmation requests to all banking and investment counterparties. This permission was granted and the requests were sent. All of these requests have been returned with positive confirmation.
Disclosures	Our review of disclosures found no material omissions in the financial statements of the Council, however we made a number of recommendations to enhance the quality of disclosures. Changes made to disclosures during the course of the audit are summarised in Appendix C.
Audit evidence and explanations/significant difficulties	All information and explanations requested from management were provided

Other responsibilities under the Code

Issue	Commentary
Other information	We are required to give an opinion on whether the other information published together with the audited financial statements (including the Annual Governance Statement and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. No inconsistencies have been identified.
Matters on which we report by exception	We are required to report on a number of matters by exception in a numbers of areas: • If the Annual Governance Statement does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the other information of which we are aware from our audit • If we have applied any of our statutory powers or duties We have nothing to report on these matters.
Specified procedures for Whole of Government Accounts	We are required to carry out specified procedures (on behalf of the NAO) on the Whole of Government Accounts (WGA) consolidation pack under WGA group audit instructions. As the Council exceeds the specified group reporting threshold of £500m, we examine and report on the consistency of the WGA consolidation pack with the Council's audited financial statements. These procedures will be completed at the conclusion of the audit.
Certification of the closure of the audit	We are unable to certify the closure of the 2019/20 audit until the required procedures in respect of the WGA outlined above have been performed. This will take place following the conclusion of the financial statements audit. This will be reflected in the audit opinion. We note your previous auditor has now certified as closed the 2015/16, 2016/17 and 2017/18 audits on 01 November 2018.

Value for Money

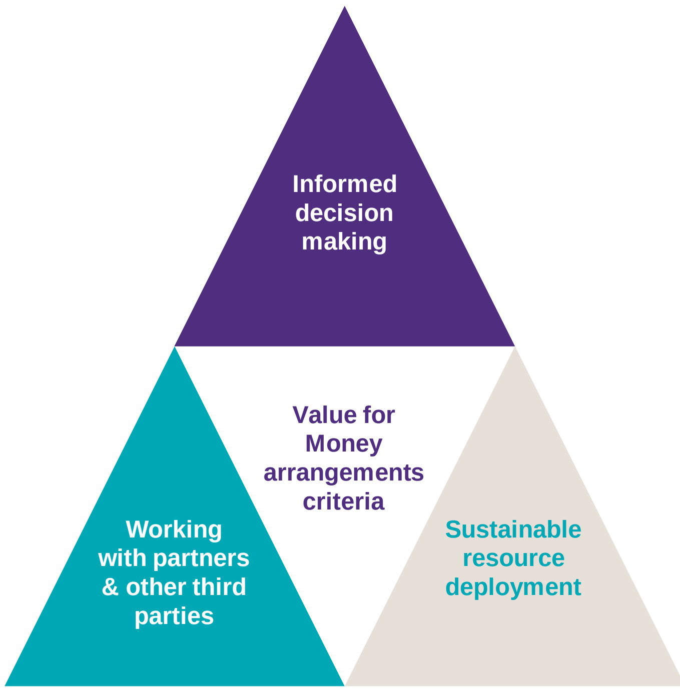
Background to our VFM approach

We are required to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the Value for Money (VFM) conclusion.

We are required to carry out sufficient work to satisfy ourselves that proper arrangements are in place at the Council. In carrying out this work, we are required to follow the NAO's Auditor Guidance Note 3 (AGN 03) issued in April 2020. AGN 03 identifies one single criterion for auditors to evaluate:

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

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



Risk assessment

We carried out an initial risk assessment in January and February 2020 and identified two significant risks in respect of specific areas of proper arrangements using the guidance contained in AGN03. We communicated these risks to you in our Audit Plan dated 05 March 2020.

We have continued our review of relevant documents up to the date of giving our report, and have not identified any further significant risks where we need to perform further work.

We have not identified any new VfM risks in relation to Covid -19, however we have considered and commented on the potential impact of Covid -19 on the Council's future financial sustainability, and plans for addressing the arising issues, as part of our work in addressing the previously identified significant VfM risks around the arrangements in place for Medium Term Financial Planning and change and transformation programmes.

We carried out further work only in respect of the significant risks we identified from our initial and ongoing risk assessment. Where our consideration of the significant risks determined that arrangements were not operating effectively, we have used the examples of proper arrangements from AGN 03 to explain the gaps in proper arrangements that we have reported in our VFM conclusion.

Value for Money

Our work

AGN 03 requires us to disclose our views on significant qualitative aspects of the Council's arrangements for delivering economy, efficiency and effectiveness.

We have focused our work on the significant risks that we identified in the Council's arrangements. In arriving at our conclusion, our main considerations were:

- Financial outturn and sustainability – the Council as other authorities continues to operate under significant financial pressures and achieving the set budget is considered a risk; and
- Ofsted inspection of children's social care services issued an inadequate rating overall.

We have set out more detail on the risks we identified, the results of the work we performed, and the conclusions we drew from this work on pages 26 to 31.

Overall conclusion

Except for the matter we identified in respect of Ofsted's inspection report on the Council's children's social care services, issued on 27 August 2019, which judged services to help and protect children in Medway to be 'inadequate', the Council had proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

We therefore propose to give a qualified 'except for' conclusion.

The text of our proposed report can be found at Appendix E

Recommendations for improvement

We discussed the findings arising from our work with management and agreed recommendations for improvement.

Our recommendations and management's responses to these can be found in the Action Plan at Appendix A

Significant difficulties in undertaking our work

We did not identify any significant difficulties in undertaking our work on your arrangements which we wish to draw to your attention.

Significant matters discussed with management

There were no matters where no other evidence was available or matters of such significance to our conclusion or that we required written representation from management or those charged with governance.

Value for Money

Overview (Financial outturn and sustainability)

The financial resilience of the Council depends on its ability to balance income and expenditure, without over-reliance on reserves to fund the day to day cost of services. Despite challenging conditions, in particular the impact of Covid-19 in the last part of the year, the Council achieved a net underspend of £2.8million in 2019/20, which was transferred to the Council's usable general fund reserves. This underspend was achieved through a strict moratorium on non-essential spend having identified potential pressures earlier in the year.

In February 2020, the Council set a budget for the financial year 2020/21, which included a deficit of £0.3m (which was anticipated to be covered by a favourable movement on the Business Rates side of the Collection Fund). Following the significant financial impact of Covid-19 that became apparent in March 2020 and the lockdown period spanning the first financial quarter, the Council is currently anticipating a budget gap of £2.5m in 2020/21, once the first three tranches of Covid-19 funding and an expectation of the 75% income compensation scheme are taken into account. However, the forth tranche of Covid-19 funding (£6.3m) has not yet been utilised at this stage. This provides comfort that the Council is likely to be able to deliver a balanced budget in 2020/21, subject to further developments in regard to management of the pandemic in the final quarter of the financial year.

The original Medium Term Financial Strategy (MTFS) published in September 2019, anticipated a funding deficit building to £17.3m by 2023/24. The revised MTFS that would normally be prepared in September 2020, has been delayed to November due to Covid-19 uncertainties and was not available at the time of writing. However, draft figures were made available for 2021/22, indicating an increasing gap of £11.7m in 2021/22 rising to £20.4m, by 2022/23. These figures are based on the assumption that the Council's cost base and income generation returns to a 'business as usual' footing from 1st April but could be higher if Covid-19 pressures become embedded in the longer term.

Setting a balanced budget in 2021/22

The Council faces a significant challenge in meeting its statutory duty to set a balanced budget for 2021/22, and will be reliant on adequate financial support being provided by government through the annual funding settlement, or other additional measures.

There is a risk that under current arrangements, should government funding fall short of expectations, the Council may not have sufficient reserves to cover the resulting deficit while also being able to demonstrate ongoing financial sustainability, without significant decisions being made around potential savings and current levels of service provision.

The Council's usable general fund reserves stood at £11.6m at 31 March 2020, in addition to an Earmarked General Fund Balance of £18.8m, which includes £5.3m of Covid-19 funding from central government that is being used to mitigate the overspend in 2020/21. The Council has set a minimum General Fund Balance of £10m, providing some limited flexibility.

Overall conclusion

As for all councils across the country, Covid-19 presents a major challenge to the Council's financial position and its future financial sustainability. However, we are satisfied that the Council has put in place adequate arrangements to understand and plan for its financial sustainability in the short to medium term.

In common with many other local authorities, the Council faces a significant challenge in meeting its statutory duty to set a balanced budget for 2021/22 and is likely to be dependent on further government support, primarily through the funding settlement due to be announced in late November 2020.

We have made a number of recommendations in Appendix A that will help the council to strengthen its financial arrangements in the face of the increased level of financial challenge we consider likely to be faced from 2021/22 onwards.

Value for Money

Financial performance 2019/20

Having identified potential pressures earlier in the year, the Council implemented a strict moratorium on non-essential spend and was able to end the 2019-20 period with a net underspend across directorates of £2.6m. This combined with the share of the Government surplus on the business rates levy (£0.2m) led to a net underspend for the year of £2.8million, which was transferred to the Council's usable general fund reserves. This is against a gross budget of £301.2m.

Significant underspends in directorates were evident in Interest & Financing (£5.3m), Regeneration, Culture, Environment and Transformation (£2.3m) and Business Support Department (£1.0m). The Interest & Financing underspend is due to a review of the Minimum Revenue Provision (MRP) for borrowing undertaken by the Council's external treasury advisors which concluded that the Council had made an over provision for a number of years. We record our comments on this at page 11.

Set against this, Children's and Adult Services (including Public Health), overspent by £6.1m. This overspend included £4.6m in Children's Services (due to recruitment costs, placement costs and Special Educational Needs) and an overspend of £1.3m across the Directorate Management Team (principally due to costs associated with recruitment to and cover for the vacant Assistant Director posts).

In 2019/20, the first tranche of Covid-19 funding (£6.6m) was received and £1.4m of this was allocated to debt provisions for commercial properties, homelessness and adult social care. The balance (£5.3m) was transferred to a Covid-19 Reserve. Note this is separate to the £2.8m transfer to the general fund reserves as a result of the net underspend in 2019/20.

Recommendation

The Council should continue to closely monitor and mitigate the underlying pressures in Adults and Children's Services, making a distinction between this and short term Covid-19 related pressures. The current analysis of in year pressures for 2020/21 indicate that further overspends are forecast (as at Round 2).

Savings performance 2019/20

Planned savings commitments and progress against these was not reported separately in Round 1-3 and outturn reporting to Cabinet, but were delivered as part of the overall budget underspend. Discussions with the Head of Finance Strategy confirms that 100% of the £2m in year savings target was achieved in 2019/20.

Other aspects of budget performance 2019/20

The capital programme budget is presented as a total over 5 years to 2023/24. The forecast position (including the outturn position for 2019/20) is an underspend of £8.4m. The underspend will be carried forward against existing schemes.

The Housing revenue account delivered a small surplus of £658k in the year.

The outturn on the Special Educational Needs (SEN) budget was a pressure of £5.460million. This reflects continued work on the recovery plan agreed with the Department for Education, which has reduced the projected deficit on the High Needs Block of the Dedicated Schools Grant reserve, which now sits at £9.184million.

Recommendation

The Council should continue to monitor capital programme over the medium term. Slippage / underspend is currently reported as a total over a 5 year period. The Council should consider reporting performance against the budget for each year to ensure timely identification of slippage / overspends.

Value for Money

Progress against 2020/21 Budget and the impact of Covid-19

On 20 February 2020, the gross budget of £323.4m for 2020/21 was approved at Full Council. At this point, this gross budget was in excess of the estimated available resources by £0.3m and it was anticipated that there would be a favourable movement on the Business Rates side of the Collection Fund, sufficient to balance the budget in 2020/21. However, by March and April 2020, the impact of COVID-19 was being felt across all service areas.

The round 2 budget report to Cabinet in November, reflecting forecast outturn based on the first 6 months of the year, projected an overspend of £23.9m. This includes a £7.6m overspend in Children's Services (due to increases in placement numbers and support packages), £3.8m in Adult Social Care (due to demographic growth and additional service requirements of Covid-19), £4.8m in Front Line Services (due to reduced parking income) and £3.1m in Culture & Community (due to cancelled / limited events, leisure and tourism).

This overall overspend is partly offset by an estimation of the Government's Covid-19 75% income compensation scheme (£6.0m) and a drawdown from the remaining Covid-19 Reserve of £15.4m, leaving a net pressure of £2.5m.

This £15.4m drawdown from the Covid-19 Reserve represents the balance of the first tranche of Covid-19 funding not used in 2019/20 (£5.3m) as well as the second (£7.6m) and third (£2.5m) tranches. The fourth tranche of £6.3m, has been announced by government, and is available to help manage the 2020/21 position. However, the Council intends to set aside this funding in the Covid-19 reserve to help manage the position in future. It should be noted that this fourth tranche would be sufficient to offset the current net pressure forecast of £2.5m in 2020/21.

In addition, there is an anticipated income shortfall expected (of £18m) on Council Tax and Business Rates for 2020/21. Although this deficit can be recovered over three years (according to a Government announcement), this would still represent a significant pressure on the revenue budget for 2021/22 and beyond.

Recommendation

The Council should seek to separate 'Covid-19' and 'business as usual' pressures in line with good practice observed at other councils. This will support an understanding of underlying service pressures and contribute to the medium term financial strategy process.

Capital budget performance 2019/20

At Round 2 reporting, the approved capital programme for 2020/21 – 2023/24 is £437.1m. The second round of Capital Budget Monitoring for 2020/21 forecasts an underspend of £0.1m during this period. This includes a forecast spend in 2020/21 of £77.1m.

Savings development & delivery process 2020/21 and 2021/22

Performance against savings targets for 2020/21 has been compromised by Covid-19 and is reflected in the overall projected budget outturn. However, planned savings commitments and progress against these is not separately analysed for members in the round 1-3 Cabinet reports.

On request, the outcome of meetings between portfolio holders and services to address budget gap were made available for our review relating to the 2021/22 budget and MTFS process. This is the mechanism through which officers consult with the Leader and Portfolio Holders on budget proposals before they are considered in public. This included a number of savings opportunities identified with targets for 2021/22 (e.g. ICT Mobile data review, Sport, Leisure, Tourism & Heritage: Restructure). However, progress against these was in the form of narrative rather than quantified numerically. This could make it difficult for members to monitor the effectiveness of development of the savings programme. Where the savings target is relatively low, this presents less of a risk. However, the more ambitious targets that could arise in future as part of Covid-19 recovery, will require closer scrutiny and an expedited process.

Recommendation

Savings development and delivery against target should be separated and presented in a way that provides greater clarity to members and allow early identification of slippage and effective action to be taken if necessary. This will be particularly important during planning for the mitigation of projected funding shortfalls in 2020/21 and 2021/22.

Value for Money

Progress in developing the 2021/22 budget

The Council is in the process of developing a balanced budget for 2021/22. Preliminary figures shared with us indicate a projected funding gap of £11.7m, which anticipates reduced revenue from council tax and business rates resulting from economic downturn (informed by actual data from 2020/21). This also assumes that additional central government funding of £13.9m will be received as part of the settlement or through other means in 2021/22, in order to cover ongoing Covid-19 related costs and lost income. A programme of saving development has been initiated, including a programme of meetings between officers and portfolio holders to formulate plans and assess opportunities with Members. The Council is awaiting the announcement of the funding settlement in late November 2020, before considering potentially more draconian measures to reduce costs.

In our view, the initial projections indicate that without further government support as part of the 2021/21 settlement, the Council's ability to meet its statutory duty to set a balanced budget for 2021/22 is highly uncertain. Further clarity will be provided, once the 2021/22 government funding settlement is announced in late November 2020.

We recognise that prior to the announcement of the government funding settlement and further Covid-19 support, developing a balanced budget and saving programme for 2021/22 is highly challenging, due to the high level of uncertainty. However, we observe that a number of other councils have made more explicit use of scenario planning and other analysis in order to project a range of potential outcomes and used this to initiate discussion and enable financial recovery plans and savings plans to be developed for 2021/22, in anticipation of need. In some cases this has included consideration of how a worst case scenario could be managed in extremis. A similar exercise would put the Council in a better position to manage adverse scenarios, such as if the funding settlement were to cover a smaller than anticipated proportion of cost and the lost income sustained as a result of Covid-19.

Recommendation

The Council should expedite planning and development of the 2021/22 budget. Specifically, it should consider the use of a range of financial scenarios to help it to understand a range of possible outcomes and expedite the development of savings and other plans to contribute to closing the potential funding gap that may arise in 2021/22.

Reserves available to manage financial risk

The Council ended the year 2019/20 with a General Fund Balance of £11.6m and an Earmarked General Fund Balance of £18.8m. This included £5.3m of Covid-19 funding from central government (tranche 1 unused in 2019/20), which has subsequently been used to mitigate the 2020/21 forecast overspend. The Council has set a minimum General Fund Balance of £10m, providing some limited flexibility. In theory, both the general fund balance and non-Covid earmarked reserves are available to offset projected future unplanned cost pressure. However, it is likely that any short term use of these reserves would need to be replaced in future years for the Council to be able to demonstrate ongoing financial sustainability.

In our view, while the Council does retain the ability to use reserves to mitigate budget overspends, this is limited and could be quickly consumed if the financial outlook worsens. This is demonstrated in the table below which shows the scenario where further government funding is not available and General Fund and Earmarked General Fund Balances are used to close the gap. This would deplete these reserves to below the minimum level set (£5m) by the end of 2021/22.

Budget gap to 2021/22	£m	Reserves available	£m
Forecast budget gap 2020/21	2.5	Tranche 4 Covid-19 Funding	6.3
Projected budget gap 2021/22	11.7	General Fund Balance	11.6
Covid-19 pressures 2021/22 (if these are not met by Government)	13.9	Earmarked General Fund (excluding Covid-19 grant utilised in year)	13.5
Total	**28.1**	**Total**	**31.4**
		Net Position	**3.3**

Recommendation

Due the high level of uncertainty projected over the medium term, the Council should consider increasing its strategic focus on the protection and build up of reserves. The Council should aim to manage projected funding pressures through other means, such as an expanded savings programme and the creation of budgeted contingencies (which can be transferred to reserves if not used).

Value for Money

Medium Term Financial Strategy (MTFS)

The Council's revised MTFS is usually prepared and approved in September of each year. One of the key aims of the MTFS is to produce a sustainable budget without undue recourse to the use of reserves.

However, due to the uncertainties presented by Covid-19 in 2020, the MTFS has been delayed to November and was not available at the time of writing. Draft figures were available, which suggest a draft budget gap of £11.7m in 2021/22 and £20.4m in 2022/23. However, this does not include ongoing Covid-19 pressures. The Council's ongoing-financial sustainability over the medium term is at present un-clear and likely to be dependent on further financial support from government.

The MTFS is prepared to reflect the priorities and corporate ways of working set out in the Council Plan. The key priorities are:

- People – Supporting Medway's people to realise their potential,
- Place – Medway; a place to be proud of, and
- Growth – Maximising regeneration and economic growth.

The Council's three corporate 'ways of working' support the delivery of these priorities:

- Giving value for money,
- Finding the best digital innovation and using it to meet residents' needs, and
- Working in partnership where this benefits our residents.

Recommendation

It will be important that Council officers and members agree a financially sustainable medium term financial plan recognising that, without significant further support from government, this could require difficult decisions to be made around future service priorities.

Financial governance – monitoring

The Council prepares quarterly financial reports to Cabinet on revenue and capital performance and each department provides a detailed commentary on their performance, This keeps Members informed of the Council's financial performance and budget gaps arising. Covid-19 has increased the frequency of conversations around the Council's finances but it is felt the resources are not currently available to increase the frequency of reporting to Cabinet (to e.g. monthly).

Recommendation

We note that financial monitoring reports are shared with Cabinet on a broadly quarterly basis. Given the present high level of financial uncertainty and the unusual circumstances presented by Covid-19, including the potential need to make decisions quickly, the Council should consider the cost-benefit of more regular financial reporting to Cabinet on a temporary basis.

Value for Money

Overview (Ofsted inspection of children's social care services)

Ofsted's inspection report on the Council's children's social care services, issued on 27 August 2019 judged its services to help and protect children in Medway to be 'inadequate'. This matter is evidence of weaknesses in proper arrangements for understanding and using appropriate financial and performance information to support informed decision making and performance management and for planning, organising and developing the workforce effectively to deliver strategic priorities.

Following the inspection, the Council introduced quarterly updates on improvement activity. The reports were reported quarterly to the Children and Young People Overview and Scrutiny Committee (CYPOSC). An Improvement Board also meets monthly to oversee progress on the Improvement Plan. The improvement Plan was later updated in July 2020.

Ofsted monitoring visits scheduled in March and June 2020 were postponed due to Covid19 restrictions before an off-site visit took place in August 2020. The inspectors reviewed the progress made by the 'front door' of the service, focusing on the interface with early help services, the quality of initial decision-making, the timeliness of service provision and the quality of initial assessment and planning.

We note this first visit is not published but the findings were shared with the Council to inform ongoing improvement priorities. A summary of the Ofsted visit was reported to CYPOSC in October 2020 and some of the messages include:

- recognition that targeted investment in the service and a planned realignment of teams has laid the foundations for practice to change and improve;
- continuity of senior management team in post and additional investment in staffing has contributed to reducing caseloads to manageable levels in the assessment teams;
- additional 35 social work posts created across the service increased the capacity to complete work with families when they are referred to children's services.

However, the report back to CTPOSC also identified areas where further work was still needed including:

- quality of management oversight and direction was not yet consistently contributing to effective planning;
- Acknowledgement that recruitment and retention of social workers remains problematic which is being addressed through the introduction of a more structured career pathway and a firmer focus on creating a more positive working environment.

Overall conclusion

Per NAO's Auditor Guidance Note 3 (AGN 03) issued in April 2020, an inadequate inspection report is indicative of improper arrangements to secure economy, efficiency and effectiveness in your use of resources.

We therefore propose to give a qualified 'except for' conclusion.

Independence and ethics

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

We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard.

Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in May 2020 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

Details of fees charged are detailed in Appendix D

Independence and ethics

Audit-related and Non-audit services

For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The following non-audit services were identified which were charged from the beginning of the financial year to the current date, as well as the threats to our independence and safeguards that have been applied to mitigate these threats.

	Fees £	Threats identified	Safeguards
Audit related			
Agreed upon procedures relating to pooling of housing capital receipts	3,200	Self-Interest (because this is a recurring fee) Self review (because GT provides audit services)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is £3,200 in comparison to the total fee for the audit of £131,087 and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level. To mitigate against the self review threat, this work will take place after the audit is completed. The amounts involved are not material to our opinion meaning that the likelihood of material errors in the financial statements arising as a result of this work is low. The Council has informed management who will decide whether to amend returns for our findings, and agree the accuracy of our reports.
Agreed upon procedures relating to the Teachers' Pensions End of Year Certificate	4,200	Self-Interest (because this is a recurring fee) Self review (because GT provides audit services)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is £4,200 in comparison to the total fee for the audit of £131,087 and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level. To mitigate against the self review threat, this work will take place after the audit is completed. The amounts involved are not material to our opinion meaning that the likelihood of material errors in the financial statements arising as a result of this work is low. The Council has informed management who will decide whether to amend returns for our findings, and agree the accuracy of our reports.
Certification of Housing Benefit Subsidy Claim	20,000	Self-Interest (because this is a recurring fee) Self review (because GT provides audit services)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is £20,000 in comparison to the total fee for the audit of £131,087 and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level. To mitigate against the self review threat, this work will take place after the audit is completed. The amounts involved are not material to our opinion meaning that the likelihood of material errors in the financial statements arising as a result of this work is low. The Council has informed management who will decide whether to amend returns for our findings, and agree the accuracy of our reports.

Action plan

We have identified a number of recommendations for the Council as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2020/21 audit. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

Assessment	Issue and risk	Recommendations
High	**Salary Capitalisation** The Council applies a variety of methods to work out the salary recharge to capital that is inconsistent with expected accounting practice. The Code requires staff costs that are capitalised should always be actual costs to the organisation, without any 'profit' or overhead. Additionally, the method for capturing direct costs was not possible and the Council had to estimate the time staff had spent on capital projects to judge what the capital spend would have been. This causes a risk that ineligible salary costs are capitalised.	The arrangements for salary recharges should be strengthened as follows: • Ensure all salary recharges to capital is consistent with the Code.**, and** • Implement a system that will accurately capture direct salary costs to be capitalised to specific projects. **Management response** We have reviewed the arrangements to charge salary costs to capital and introduced a new approach to ensure we comply with the Code moving forward.
High	**Bad Debt Provision** The Council is required to consider the expected credit loss across its variety of Debtors. Within the Council tax bad debt provision, we identified significant deficiencies in the model used to determine the provision. As a result of this work, the Council reviewed its model and provided us assurance that the estimate was not materially misstated. We also note that the Council had no policy in place for determining expected credit loss for Trade debtors. Although we were satisfied the provision was not unreasonable for this financial year, following further work by the Council, it was clear the council had not been applying the expected credit loss model per IFRS 9 when assessing there provision for trade debtors.	Ensure the Bad debt provision is regularly reviewed and the models applied are reasonable and consistent with IFRS9. The Council should regularly reassess the collectability of debts and rereview the expected credit loss for each class of debtor. **Management response** We have reviewed the method of calculation for our bad debt provisions with a more robust calculation used to inform the budget for 2020/21.

Controls

- High
- Medium
- Low

Action plan - continued

Assessment	Issue and risk	Recommendations
● **Medium**	**School bank accounts (Academies)** Our testing identified academies bank accounts with cash balances that should have been transferred to the respective academies. Risk that academies balances and reserves are incorrectly recognised as Council reserves.	Cash balances of schools with academy status should be derecognised and transferred to the respective academy schools and the bank accounts should be closed as soon as is practicable to do so. **Management response** Agreed, this will be actioned before the 2020/21 financial year end, so will be reflected correctly in the 2020/21 Statements.
● **Medium**	**Journals** On receipt of journals from directorates into the 'receipt inbox', members of the Finance team carry out a review of the journals for appropriateness, separation of duties and authorisation within directorates, prior to approving the journals within the 'ready for processing' inbox for other members of the team to post the journal into the ledger. No audit evidence could be provided to demonstrate that a key management control was operating as designed increasing the risk or error and misclassification.	Management should evidence the intended control is operating as designed. **Management response** Agreed, we are working to implement an arrangement that provides satisfactory evidence without a disproportionally high administrative burden.
● **Medium**	**PPE valuations** We note that £0.68m assets have not been valued within the last five years which is not in accordance with the Code and your accounting policy.	Ensure all PPE not revalued within the 5-year rolling cycle are valued during 2020/21 to ensure they are comply with your valuation policy and the Code. **Management response** Agreed, we will ensure all assets that have not been revalued within the 5 year programme are included in the valuations carried out for the 2020/21 audit.

Controls

- ● High
- ● Medium
- ● Low

Action plan - continued

Assessment	Issue and risk	Recommendations
Medium	**Cash and bank (reconciling items)** We note from our creditor bank account testing that 4 out of our sample of 5 reconciling items remain uncleared as of 30 September 2020, some 6 months after year end. Auditor update We note that the Treasury and Exchequer team were unable to provide evidence of who had authorised payment in 3 out of the 4 reconciling items. There is a risk that payments may be authorised without appropriate approval.	We recommend Treasury and Exchequer processing agree internally a target date for reviewing and clearing all reconciling items. Furthermore, payments should not be processed without appropriate authorisation **Management response** Agreed, we will implement arrangements to better monitor unreconciled items.
Medium	**Going concern** Management prepare a going concern paper for audit purposes to support the going concern basis of the accounts. A similar paper is prepared for Those Charged with Governance (Audit Committee). Such a paper is considered to be good practice.	Prepare a paper annually for Corporate Governance and Audit Committee setting out the basis for the going concern preparation of the financial statements and provide this with the audit working papers. **Management response** Agreed, we will consider how to incorporate this statement into our preparations for the 2021/22 Statements and audit.
Medium	**Minimum Revenue Provision** The impact of this change for 2019/20 is that under a 'corrected' calculation of your capital financing requirement (includes Adjustment A that had been excluded from 2015/16 and the removal of double counting of SCA approvals) the MRP on an annuity basis would be £3.371m. The actual MRP charge in 2019/20 is £1k. The Council intend to charge to the accounts £1k for the following 5 years. The 'calculated' MRP charge based on its adopted methodology for the period 2019/20 to 2025/26 is £19.96m.	The Council should reconsider its decision to apply the 'correction of prior year MRP' over the short time frame of six years and assess if it would be more equitable to spread the 'correction' over a much longer period. **Management response** We have again considered our decision and remain of the opinion that we should correct the prior year issue as quickly as possible
Medium	**Creditors (Note 33)** Our sample testing of creditors identified two errors as follows: • Collection fund income that was incorrectly classified as deferred income, and • Creditor balance with no supporting evidence. Management believe the creditor was several years old and should have been written off. Risk that creditor balance may be misstated.	Ensure all Balance sheet codes are regularly monitored and historic items are cleared /written off on a timely basis. **Management response** We will build a review of all balance sheet codes into the closedown timetable for 2021/22 statements.

Controls

- High
- Medium
- Low

Action plan - continued

Assessment	Issue and risk	Recommendations
Medium	**MCG Financial Oversight** As part of our review and testing of receivables as at 31 March 2020, we note a debtor of £4.1m with MCG of which £2.7m related to debtors greater than one year old. We challenged management if trade receivables greater than one year should be impaired in line with the Council's policy. Management confirmed there was no current policy for impairment of trade receivables greater than one year. Risk that expected credit losses of trade receivables greater than one year are understated.	Develop a policy for estimating the expected credit losses for trade receivables greater than one year. The policy should include consideration for the likely recoverably of the debt and supported by evidence. The policy should be consistently applied and monitored consistently. **Management response** Finance Strategy and Corporate Debt teams will work together to develop and maintain a policy to estimate credit losses.
Medium	**Disclosures** Our work identified a number of disclosure errors within the draft accounts (refer Appendix C) which included: This created additional audit work and amendments within the Council's accounts.	Further strengthen the quality review arrangements of the draft financial statements to improve quality of reporting and minimise the disclosure errors. **Management response** The significant work required from the team to supporting the Council's response to the Covid-19 pandemic impacted on the resources available to do some tasks, including our normal robust quality control processes. We anticipate a return to more normal workloads in the coming year enabling us to return to the typical level of internal scrutiny our statements are put through before publication.
Medium	**Identifying Internal recharges** Our testing identified elements of internal recharges had been incorrectly included in CIES income and expenditure. This resulted both income and expenditure had been overstated. This was due to departments not posting journals in a way that allowed internal recharges to be identified consistently and accurately. This creates a risk going forward that income and expenditure will be overstated in the Council's financial statements.	The process for capturing internal recharges should be clearly set in the Council's standing financial instructions and: • communicated to all finance staff, and • compliance are monitored regularly. **Management response** We will carry out a piece of work to analyse all charging between internal services, and ensure all are coded appropriately so they can be excluded from the CIES. Compliance with any amended coding will be confirmed through the budget monitoring process.
Low	**Journals** Our review of the trial balance identified a journal posted after the draft statements were produced. This was a Journal that was posted in error reclassifying £5,000k between short term creditors, short term debtors and short term borrowings. A subsequent review by the finance team identified this Journal was posted in error. Risk that post journal amendments to the accounts are inappropriately posted in the trial balance	Recommend you put in place controls that restrict the posting of journals after the accounts have been produced to a responsible officer e.g. Financial Controller. **Management response** We have put in place arrangements to ensure journals can only be authorised by the Chief Finance Officer, Head of Finance Strategy or the Finance Business Partner – Corporate Reporting after the draft statements are produced, however we will also run reports to identify any journals posted in error after that date before the statements are certified.

Action plan - continued

Assessment	Issue and risk	Recommendations
Low	**Collection Fund Creditors and Receivables** At the year end, the Council closes down its accounts and cash position based on Integra. As at 31 March 2020, the Council had collected £1.9m more business rates than was shown on Northgate. The impact is the Council's Collection Fund Receivables is reduced as a result. However, the Council at year end adjusted its Collection Fund Receivables/Creditors based on the Northgate system rather than Integra. The latter due to timing differences has not reflected the reduction in the debtors position. To balance Integra, the Council credited Collection Fund creditors with an equal value resulting in both debtors and creditors being overstated by £1.9m. The treatment above is a balance movement with no impact on general reserves.	The Council should closedown its Collection Fund debtors and creditors based on the Integra system and support its position with a system reconciliation with the Northgate billing system, as at 31 March. **Management response** It has not been possible to close on Integra for 2020/21, but we will endeavour to ensure we can do this for 2021/22.
Low	**IFRS 16 Leases (Note 2)** The implementation of IFRS 16 has been further delayed to 1 April 2022. The Council's IFRS 16 disclosure in 2021/22 will need to include the estimated impact on the financial statements as at 31 March 2022. We will review the estimated impact on the assets, liabilities, income, expenditure and reserves within the financial statements as at 31 March 2022 as part of the 2021/22 audit.	As part of your on-going IFRS 16 preparations for implementing the standard, you should: • document the Council's arrangements for ensuring the completeness of leases, and • consider the risk of impairment on lease asset values as at 1 April 2022 due to Covid - 19 and the level of uncertainty around the asset values. **Management response** • Our work to implement this standard is ongoing and we will incorporate these actions into that work.
Low	**Cash Accounts not correctly input within the General Ledger** We identified a number of Bank accounts that were not disclosed in the General ledger, that were in the councils main bank statement. We tested 5 of these accounts and identified that 3 were third party accounts and correctly excluded. However two were noted by the council as accounts that the council owned and should be included within their Statement of accounts. The balance of these two accounts was £58k. This creates the possible risk of misappropriation of assets or the failure to effectively oversee and monitor the Council's bank accounts.	Recommend the council reviews all bank accounts held in the main account to ensure all bank accounts are correctly captured within the general ledger. **Management response** This review is underway.

Controls

- High
- Medium
- Low

Action plan from VfM review

We have identified a number of recommendations for the Council as a result of issues identified during the course of our VFM review. We will discuss and agree our recommendations with management and we will report on progress on these recommendations during the course of the 2020/21 audit.

Recommendations	Management responses
The Council should continue to closely monitor and mitigate the underlying pressures in Adults and Children's Services, making a distinction between this and short term Covid-19 related pressures. The current analysis of in year pressures for 2020/21 indicate that further overspends are forecast (as at Round 2).	We have distinguished in the Medium Term Financial Strategy between inherent pressures in social care and education, from those arising as a result of Covid-19. Our position is that the 2020/21 budget was robust and therefore all pressures arising are attributable to the pandemic.
The Council should continue to monitor capital programme over the medium term. Slippage / underspend is currently reported as a total over a 5 year period. The Council should consider reporting performance against the budget for each year to ensure timely identification of slippage / overspends.	We monitor our capital programme over the life of the schemes to provide services with the maximum flexibility in managing programme delivery within the budget agreed. We would not consider that forecasting overspends against activity planned for each year of the programme would add any value, and would generate significant additional work in preparing annual budgets.
The Council should seek to separate 'Covid-19' and 'business as usual' pressures in line with good practice observed at other councils. This will support an understanding of underlying service pressures and contribute to the medium term financial strategy process.	We have distinguished in the Medium Term Financial Strategy between inherent pressures in social care and education, from those arising as a result of Covid-19. Our position is that the 2020/21 budget was robust and therefore all pressures arising are attributable to the pandemic.
Savings development and delivery against target should be separated and presented in a way that provides greater clarity to members and allow early identification of slippage and effective action to be taken if necessary. This will be particularly important during planning for the mitigation of projected funding shortfalls in 2020/21 and 2021/22.	We will consider this recommendation the preparation of monitoring reports on Business Change activity in future
The Council should expedite planning and development of the 2021/22 budget. Specifically, it should consider the use of a range of financial scenarios to help it to understand a range of possible outcomes and expedite the development of savings and other plans to contribute to closing the potential funding gap that may arise in 2021/22.	We have published our draft budget proposals, and await the announcement of the Chancellor on local government funding for 2021/22 on 25 November. The Medium Term Financial Strategy includes our best estimate of the likely funding, alongside the impact anticipated should the government not fund the Covid-19 pressures as it has in 2020/21
Due the high level of uncertainty projected over the medium term, the Council should consider increasing its strategic focus on the protection and build up of reserves. The Council should aim to manage projected funding pressures through other means, such as an expanded savings programme and the creation of budgeted contingencies (which can be transferred to reserves if not used).	Our reserves strategy, as set out in the MTFS, is clear that aim to prepare a balanced budget without recourse to reserves, and our decision to correct the prior year over-provision of MRP as quickly as possible will allow us to make contributions to reserves every year over the medium term. We are working on the development of our Business Change programme for 2021/22 to deliver savings including a new Transformation Programme funded from the flexible use of capital receipts

Action plan from VfM review - continued

Recommendations	Management responses
It will be important that Council officers and members agree a financially sustainable medium term financial plan recognising that, without significant further support from government, this could require difficult decisions to be made around future service priorities.	Implemented
We note that financial monitoring reports are shared with Cabinet on a broadly quarterly basis. Given the present high level of financial uncertainty and the unusual circumstances presented by Covid-19, including the potential need to make decisions quickly, the Council should consider the cost-benefit of more regular financial reporting to Cabinet on a temporary basis.	Our areas of highest volatility and pressure, social care for children and adults, are monitored more frequently with monthly updates provided to Portfolio holders through Dashboard meetings. We are also currently undertaking more frequent high level reviews of our forecasts to submit the monthly Covid-19 returns to the government. We do not have sufficient capacity in the Finance team to support more frequent monitoring of the whole budget and do not consider this risk would warrant growth in the service required to deliver that

Follow up of prior year recommendations

We identified the following issues in the audit of the Council 2018/19 financial statements, which resulted in 4 recommendations being reported in our 2018/19 Audit Findings report.

Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
✓	**Revenue expenditure funded from Capital under Statute (REFCUS)** We noted the cost of the digital transformation team of £2.67m (last year of the three-year programme) has been funded from REFCUS rather than recorded in the relevant service revenue line in the Comprehensive Income and Expenditure Statement We recommended in future that management review all expenditure funded through Revenue expenditure funded from Capital under Statute against the Code requirement.	We have reviewed our approach to REFCUS and presented this in a separate document to Grant Thornton. **Auditor response** Action complete.
x (partial)	**IT general controls** Our review of IT general controls resulted in 4 medium priority recommendations around the following areas: • Lack of segregation of duties between security administration and business management • Proactive reviews of logical access within Northgate iWorld • Lack of documented batch administration policies and procedures • Change control over Northgate iWorld and Integra batch jobs and schedules.	• Investigations into removing security access are ongoing as requires a whole new profile being built to enable required access for the whole of the system excluding security admin • Access requirements are amended in accordance with upgrade requirements • There are detailed procedure notes on batch/individual jobs • Implemented for IWorld. **Auditor response** Action partially complete, progress to be followed up during 2020/21.

Assessment

✓ Action completed

X Not yet addressed

Follow up of prior year recommendations - continued

Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
x (partial)	**Officers Remuneration disclosure** We reported a significant proportion of the senior officer remuneration, remuneration bands >£50k and exit package notes were inconsistent with underlying evidence. The disclosure was restated in its entirety. We recommended your 2019/20 closedown, HR/Payroll related disclosure should be subject to senior officer review for consistency with supporting evidence.	Payroll reports have been undergoing a review which is still ongoing as: • reports are converted to the new reporting tool within Resourcelink • new reports are designed as processes are also being reviewed. The aim is that reports will be available online for: • Payroll staff • Personnel staff • Management across the Council Priority on the reports to be converted have been in respect of Children's Services in order to provide a set of reports for Members. This followed a review of the structure in the system so that these reports could be produced. Now we are moving on to the rest of the Council with Adults targeted next and then the other departments. **Auditor response** Action partially complete, progress to be followed up during 2020/21.
✓	**PPE valuations** Additional discussions and investigations took place to agree your Internal valuers point estimates which were at the upper end of potential value movements when local circumstances were taken into account (particularly for schools). We recommended management should strengthen future working papers in this area to provide a detailed assessment that can be audited	The impairment review has been completed with a more detailed analysis than previous years, This has resulted in far more properties having to be revalued this year than in previous years. **Auditor response** Action complete.

Assessment

✓ Action completed

X Not yet addressed

Audit adjustments

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the key statements and the reported net expenditure for the year ending 31 March 2020.

Detail	CIES £'000	Balance Sheet £'000	Impact on total net expenditure £'000
Cash and school balances - identified academies bank accounts with cash balances that should have been transferred to the respective academies. DR Debtors CR Cash	Nil	241 (241)	nil
Journal miscoding between creditors and debtors with 1.3m bad debt provision of the NNDR collectability provision being transferred to creditors incorrectly. DR Creditors CR Debtors	nil	1,300 (1,300)	nil
Note 26 Financial Instruments - Our testing of Council borrowings identified short term borrowing incorrectly classified as long term borrowings. DR Long Term Borrowings CR Short Term Borrowings	nil	2,520 (2,520)	nil
Note 35 Provisions – £3.4m long term NNDR provision was incorrectly classified as short term (WIP) DR Short Term Provisions CR Long Term Provisions	nil	3,428 (3,428)	nil
Note 34 Creditors - Grant Received in Advance was incorrectly classified as year end creditors DR Short Term Creditors CR Grants Received in Advance	nil	5,762 (5,762)	nil
CIES – Our testing identified internal recharges had been incorrectly included in CIES Income and expenditure. This has meant both income and expenditure has been overstated. DR Income CR Expenditure	4,411 (4,411)	nil	nil
Pooled Budgets- In both the current and prior year we identified the council had overstated its income and expenditure in relation to the Better Care fund. This had no bottom line impact but was material and therefore a Prior Period adjustment was required. The impact in 2019/20 was 9,927K and in 2018/19 £9,258k. Both amendments have been made in the accounts. DR Income CR Expenditure	(9,927) 9,927	nil	nil
PPE Additions - Staff costs within PPE additions was incorrectly classified as revenue rather than capital expenditure. The net impact is to overstate expenditure and income by an equal value. DR Income CR Expenditure	3,405 (3,405)	nil	nil
Investment Income - Finance and Investment Income was understated by £479K and Business Support Development had overstated its income in year. DR Income CR Income	479 (479)	nil	nil
Overall impact	**Nil**	**Nil**	**Nil**

Audit unadjusted errors

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

Impact of unadjusted misstatements

All unadjusted misstatements are set out in detail below along with the impact on the key statements and the reported net expenditure for the year ending 31 March 2020.

Detail	CIES £'000	Balance Sheet £' 000	Impact on General Fund £'000
Council Tax Bad Debt Provision - the model used to estimate the council tax bad debt provision was updated during the year. The revision resulted in the Council's share of Provisions being understated by £3,664k. DR Expenditure CR Debtors	(3,664)	(3,664)	(3,664)
Collection Fund Creditors - we identified three errors within the Collection Fund Creditors as follows	nil	1,657	nil
- difference between Integra and the Northgate Collection Fund system resulting in creditors and debtors being overstated (£1,923k)		(1,657)	
- misclassification of deferred income and other debtors being overstated (£201k)			
- input error from the collection fund model Collection Fund Creditors and Debtors were understated (£467k)			
DR Creditors CR Debtors			
PPE Additions – error identified in over capitalisation of staff costs DR Expenditure CR PPE	(1,230)	(1,230)	(1,230)
PPE Additions – error identified following discussions with Council DR PPE CR Expenditure	560	560	560
PPE Additions – Consideration of the prior period impact of overcapitalisation on the General Fund This was estimated by the council and therefore a range has been provided.			(821) To (1,565)
Overall impact	**(4,334)**	**(4,334)**	**(5,155) To (5,899)**

Audit adjustments – continued – Prior Year

Impact of prior year unadjusted misstatements

The table below provides details of adjustments identified during the prior year audit which had not been made within the final set of 2018/19 financial statements

Detail	Comprehensive Income and Expenditure Statement £'000	Balance Sheet £' 000	Impact on total net expenditure £'000	Action taken in 2019/20
Potential impact of the McCloud judgement	nil	(5,546)	5,546	We reviewed your IAS 19 report and identified that the impact of the McCLoud judgement had been appropriately taken into account in the 2019/20 financial statements.
Negative Designated Schools Grant	nil	4,139 (4,139)	nil	Our view is that this is a classification error. Refer to Page 13 for details.
Revenue expenditure funded from Capital under Statute (REFCUS)	2,667 (2,667)	nil	nil	Testing of REFCUS has not identified any issue in 2019/20
Overall impact	**nil**	**(5,546)**	**5,546**	

Audit adjustments - disclosures

Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified to date which management has agreed to amend in the final set of financial statements.

Disclosure amendment	Detail	Adjustment agreed?
Balance sheet	Insert at the foot of the Balance Sheet the date accounts was authorised for issue per Code requirements (para 3.8.2.11)	✓
CIES	The CIES has been updated to disclose the impact of the Prior period adjustment identified in relation to the Better care Fund. Disclosing the nature of the adjustment and its impact.	Agreed to amend
MIRS and Note 20	Within Earmarked Reserves there was a reserve titled "General Reserve", which had an opening balance of £4,039K. Earmarked Reserves must be held for a specific purpose and this was therefore identified as an error and adjusted to the General Fund.	✓
Note 1 Accounting policies	Note 1 does not include all accounting policies applicable to the accounts. Recommend: • Note 1 of the accounts should explain to the reader why certain items are included here but others are not and where the other policies are to be found, and • Where other policies are included with notes to the accounts, they should be identified specifically as 'accounting policy' in all instances	✓
Note 3 Critical judgements	It is not clear what the judgements actually are for joint workings and revenue from contracts. Review and update your critical judgements disclosures	✓
Note 4 Estimation uncertainties	Items should only be disclosed where there is a risk of material adjustment within the next year; and each disclosure should meet the requirement of IAS 1 such as disclosing the nature of the assumptions giving rise to uncertainty and disclosure of the range of reasonably possible outcomes. Review and update your estimation uncertainties disclosures particularly for business rates and fair value measurement of Investment Properties.	✓
Note 4 Estimation uncertainties	The Council's professional PPE valuer has disclosed a material valuation uncertainty due to the level of uncertainty in the markets since the outbreak of Covid-19. Similarly, we are aware that the Kent Pension Fund intends to disclose a 'material valuation uncertainty' in relation to the directly held property and pooled property funds within the assets of the pension fund. Your share of these assets are material. Recommend you include within Note 4 PPE and Pension material valuation uncertainty disclosure in line with the requirement of the Code {paragraphs 3.4.2.90 – 91}.	✓
Note 7 Segmental income	Disclosure needs to be updated to reflect IFRS 15. Code 3.4.2.101 specifies a) revenues from external customers, b) revenues from transactions with other operating segments of the Council.	✓
Note 12 Pooled Budgets and other I and E notes	As noted above we identified the council had overstated its share of the Better Care fund's income and expenditure, due to not following IFRS 10 with regards to control of the funds. This has lead to required amendments in disclosures of Pooled Budgets and other I and E notes for both years in the accounts.	Agreed to amend

Audit adjustments - disclosures continued

Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified to date which management has agreed to amend in the final set of financial statements.

Disclosure amendment	Detail	Adjustment agreed?
Note 14 Employee renumeration	A proportion of remuneration bands >£50k and exit package notes were inconsistent with underlying evidence. The disclosure will be updated	✓
Note 15 External audit costs	Fees to Grant Thornton (core audit and grant certification fees) should be recorded on an accrual rather that cash basis for prior and current year to be consistent with the Audit Plan. Also the narrative disclosure has not been updated from prior year. The fees and disclosure will be updated.	✓
Note 16 Dedicated Schools Grant	Enhanced disclosures were required to explain the negative reserves carried forward within the DSG Reserve.	✓
Note 20 Movements in Earmarked Reserves	Management carry forward of DSG overspends as a negative usable reserve rather than deducting from the general fund balance. The £9.3m negative DSG reserve is netted off other earmarked reserves. Grant Thornton remain of the view that DSG overspends should be netted off against general fund and not earmarked reserves.	x
Note 21 PPE (Surplus assets)	Surplus assets of £40.7m includes Pentagon site which in our view has been incorrectly disclosed. These should be disclosed as Other land and building. Additionally, £0.68m assets have not been valued within the last five years which is not in accordance with the Code and your accounting policy. We have raised a recommendation in respect of this in the action plan.	✓
Note 21 PPE (Schools)	The disclosure note includes accounting policies in respect of schools and academies. This policy is unrelated to PPE accounting and may better fit with your DSG disclosures in Note 16.	✓
Note 21 PPE (Revaluation)	Note 21 Revaluations should explain how assets not revalued at 31 March 2020 are assessed for accuracy.	Agreed to amend
Note 21 PPE (Capital Commitments)	Not all capital commitments relating to 2019/20 were identified.	Agreed to amend
Note 25 – Assets Held For Sale	Revaluation gain was incorrectly put through the PPE note and instead put through Assets Held for sale. When assets are reclassified they should be revalued in their previous class before being transferred out.	✓
Note 26 Financial Instruments	A number of the narrative disclosures and tables need to be updated to comply with IFRS 9 terminology e.g. available for sale is no longer in use and new terms such as expected credit loss model has not been disclosed. Non inclusion of material cash balances which are financial assets table Misclassifications of which financial assets were held at fair value and which were held at amortised cost.	✓

Audit adjustments - disclosures continued

Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified to date which management has agreed to amend in the final set of financial statements.

Disclosure amendment	Detail	Adjustment agreed?
Note 27 Nature and Extent of risks arising from FI	The prior year comparator should be disclosed in the note. Narrative below the table indicates the expected credit loss model required by IFRS 9 may not have been applied	✓
Note 29 Leases	Finance leases - The analysis of minimum lease payments is inconsistent with analysis of within 1 year, 1 – 5 years and later than 5 years Operating leases – refers to an erroneous figure in 2018/19. The disclosure should also state a) what changed from what to what, b) quantify the error, c) if the error is disclosure only or impacts other notes or core statements.	✓
Note 30 Debtors	Material 'other receivable amounts' of £21.1m should be sub categorised per Code 3.4.2.63 Terminology should be updated for expected loss model for financial instruments IFRS 9	✓
Note 33 Creditors	Material 'other payables' of £43.2m should be sub categorised per Code 3.4.2.63	✓
Note 36 Unusable reserves	Financial Instruments Revaluation Reserve – The accounting via the MIRS for fair value for pooled investment funds classed as FVTPL is inconsistent with CIPFA Code. Expectation is a specific reserve should be set up for the Pooled investment adjustment account.	✓
Note 39 Cash Flow Statement	Investing activities – material 'other receipts from investing activities' of £28.9m should be analysed below the table	✓
Note 42 Related parties (RP)	Review RP disclosures to ensure they meet definition of a related party as defined by IAS26 and Code 3.9.2.7 ie where Members and management defined as 'key personnel' where they (or their close family member) controls another party that that party is a related party. Reference to Medway Norse Transport should be referred to as a Joint Venture to be consistent with Note 18.	✓
Note 45 Events after the reporting period	Disclosure has been added to identify Medway Commercial Group's name changed after the year end. In addition it notes the details of the loan entered into with the Council and Medway Commercial Group. (WIP)	✓
Other	A number of minor presentational amendments have been made to the accounts	✓

A number of other minor presentational amendments including adjustment of prior period comparatives to match the audited 2018/19 financial statements were made during the audit.

Fees

We confirm below our final fees charged for the audit and provision of non-audit services.

Audit fees	Proposed fee	Final fee
Council Audit Scale Fee	£110,000	TBC
Increased Regulatory expectations per Audit Plan	£21,087	TBC
Increased work due to COVID-19	TBC	TBC
Fees for additional issues and work carried out on audit	TBC	TBC
Total audit fees (excluding VAT)	**£131,087**	**TBC**

Non-audit fees for other services	Proposed fee	Final fee
Audit Related Services:		
• Housing benefit subsidy claim	20,000	29,150
• Pooling housing capital receipts grant	3,200	3,500
• Teachers' pensions end of year certificate	4,200	TBC
Non-Audit Services: None	Nil	Nil
Total non- audit fees (excluding VAT)	**£27,400**	**TBC**

The fees reconcile to the financial statements audit fee disclosures in Note 15.

	Accounts	Grants
– Scale fee / contract fee	£110k	£20k
– Regulatory fees per Audit Plan	£21k	£8k
– **Total propose fees above**	**£131k**	**£28k**

The number of audit adjustments and issues identified has contributed to additional audit time in undertaking the audit. This will result in a fee variance which will be discussed with the Chief Finance Officer on completion of the audit. As this work is still ongoing we are unable to quantify the additional fee for the following at this date.

- additional time auditing the Council (see next page), and
- additional time taken to audit PPE additions, provisions, cash, MRP, NNDR provisions, MCG, internal recharges and disclosures.

Please note that these proposed additional fees are subject to approval by PSAA in line with the Terms of Appointment.

Fees

Over the past six months the current Covid-19 pandemic has had a significant impact on all of our lives, both at work and at home. The impact of Covid-19 on the audit of the financial statements for 2019/20 has been multifaceted. This includes:

- Revisiting planning - we have needed to revisit our planning and refresh risk assessments, materiality and testing levels. This has resulted in the identification of a significant risk at the financial statements level in respect of Covid-19 necessitating the issuing of an addendum to our original audit plan as well as additional work on areas such as going concern and disclosures in accordance with IAS1 particularly in respect to material uncertainties.
- Management's assumptions and estimates - there is increased uncertainty over many estimates including pension and other investment valuations. Many of these valuations are impacted by the reduction in economic activity and we are required to understand and challenge the assumptions applied by management.
- Financial resilience assessment – we have been required to consider the financial resilience of audited bodies. Our experience to date indicates that Covid-19 has impacted on the financial resilience of all local government bodies. This has increased the amount of work that we need to undertake on the sustainable resource deployment element of the VFM criteria necessitating enhanced and more detailed reporting in our ISA260.
- Remote working – the most significant impact in terms of delivery is the move to remote working. We, as other auditors, have experienced delays and inefficiencies as a result of remote working, including the delays in receiving accounts, quality of working papers, and delays in responses. These are understandable and arise from the availability of the relevant information and/or the availability of key staff (due to shielding or other additional Covid-19 related demands). In many instances the delays are caused by our inability to sit with an officer to discuss a query or working paper. Gaining an understanding via Teams or phone is more time-consuming.

We have been discussing this issue with PSAA over the last few months and note these issues are similar to those experienced in the commercial sector and NHS. In both sectors there has been a recognition that audits will take longer with commercial audit deadlines being extended by 4 months and NHS deadline by a month. The FRC has also issued guidance to companies and auditors setting out its expectation that audit standards remain high and of additional work needed across all audits. The link attached https://www.frc.org.uk/covid-19-guidance-and-advice (see guidance for auditors) sets out the expectations of the FRC.

Please note that these proposed additional fees are subject to approval by PSAA in line with the Terms of Appointment.