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South Ayrshire Council

South Ayrshire Council

Planning report to the Audit and Governance Panel on the audit for the year ending 31 March 2019

Issued 12 March 2019 for the meeting on 20 March 2019

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Introduction
The key messages in this report:

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

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

We have pleasure in presenting our planning report to the Audit and Governance Panel of South Ayrshire Council (the "Council") for the year ending 31 March 2019. We would like to draw your attention to the key messages of this audit plan:

Audit Plan

We have updated our understanding of the Council including discussion with management and review of relevant documentation from across the Council.

Based on these procedures, we have developed this plan in collaboration with the Council to ensure that we provide an effective audit service that meets your expectations and focuses on the most significant areas of importance and risk to the Council.

Key Risks

We have taken an initial view as to the significant audit risks the Council faces. These are presented as a summary dashboard on page 17.

- In accordance with auditing standards, we have identified a significant risk associated with income. This risk is pinpointed to the recognition of grant income (excluding General Revenue Grant and Housing Benefit Subsidy Grant) as this involves a degree of complexity and management judgement in determining whether or not grant conditions have been met and the income can be recognised in the year. In 2017/18 the total grant income received excluding the General Revenue Grant and the Housing Benefits Subsidy Grant was £27,759k.

- In accordance with auditing standards, management override of controls has also been identified as a significant audit risk.

Introduction (continued)

The key messages in this report (continued):

Audit Dimensions

The Code of Audit Practice sets our four audit dimensions which set a common framework for all public sector audits in Scotland. Our audit work will consider how the Council is addressing these and report our conclusions in our annual report to the Audit and Governance Panel in September 2019. In particular, our work will focus on:

Financial sustainability - The Council continues to face significant medium- and long- term financial challenges. This is supported by the fact that one of the Council Strategic Risks is financial constraint. The overall 2018/19 forecast position as at 31 December 2018 projects a net general services underspend (excluding the Health and Social Care Directorate (HSCP)) of £3,586k in its revenue budget, which includes an underspend against all directorates. Whilst this demonstrates that the Council is on course to achieve financial balance in 2018/19, the 2018-22 Financial Strategy indicates a medium term revenue budget gap of £31,600k, demonstrating financial challenge.

Furthermore, while the other Directorates are projecting a net general services underspend, the HSCP is projecting an overspend of £3,891k. The HSCP and IJB are still areas of concern given the significant demand pressures, and are areas that we will continue to monitor.

The Council anticipates that there will be further significant cash reductions in the General Revenue Grant from the Scottish Government over the forthcoming years, and simultaneously the Council will have to manage an ever increasing demand for Council services and manage cost pressures that apply to the models of service delivery.

A long-term strategy has yet to be developed, which is something we recommended in our 2017/18 annual audit report that the Council progress to clearly understand the long-term outlook faced by the Council in terms of demand for services and risks. We will monitor how this is progressing during 2018/19.

The Council's transformation strategy "Transform South Ayrshire" has historically been focused on IT projects. Following the recent senior management restructure, a refreshed transformation plan is to be progressed under the new Directorates. We will review the refreshed transformation strategy to ensure that it meets best practice requirements and to ensure that it addresses how the required savings of £31,600k over the next three years (per the 2018-2022 Financial Strategy) can be achieved.

Financial management - we will review the budget and monitoring reports produced during the year and liaise with internal audit in relation to their work on the financial control environment to assess whether financial management and budget setting is effective.

From our audit work in 2017/18 we found that the Council had robust financial management procedures in place. We recommended that priority-based budgeting be incorporated into the annual budget setting processes. We will review the 2019/20 budget to ascertain whether this incorporates priority-based budgeting.

Introduction (continued)

The key messages in this report (continued):

Governance and transparency **-** From our review of Council papers and attendance at Audit and Governance Panels we will assess the effectiveness of governance arrangements and Audit and Governance Panel and associated seminar attendance. We will also review the governance arrangements in relation to the Integrated Joint Board ("IJB"). Within the IJB, there is a risk that the governance arrangements between the Council and the IJB (and the partner NHS Board) are not effective.

In our 2017/18 annual audit report, we recommended that the Council improve community involvement via increased community empowerment, community takeover and participatory budgeting. We will review progress in developing the engagement strategy and implementation of this.

Value for money **-** From our 2017/18 audit work we concluded that the Council had a well established performance management framework in place, with performance considered quarterly by management and the Council, as well as being publicly available on the Council's website. During 2018/19 we will review whether performance is appropriately discussed within the Management Commentary in the Annual Accounts.

We will also follow up on the progress being made to address our recommendation that the Council consider external peer reviews on services to ensure there is enough challenge/scrutiny to ensure improvement of services.

Our audit work on the four audit dimensions incorporates the specific risks highlighted by Audit Scotland, in particular, the impact of EU withdrawal, the changing landscape for public financial management, dependency on key suppliers, care income and increased focus on openness and transparency.

Best Value and Strategic Audit Priorities

As part of our best value work, we will consider the five Strategic Audit Priorities agreed by the Accounts Commission and update our assessment of the Council's performance established from our audit work over the last two years against these priorities.

Introduction (continued)

The key messages in this report (continued):

Regulatory Change

New accounting standards on revenue and financial instruments will apply for 2018/19, and for leases from 2020/21. While we do not expect these standards to have a significant impact on Councils, we recommend that the Council review the impact of IFRS 9 and 15 early in the year, including calculating any adjustments that will be required as at 31 March 2018 for transition. We would suggest that the Audit and Governance Panel receive reporting in year from management on the implementation of the new standard, and we will report specifically on the findings from our audit work in this area.

We have reported on other regulatory changes in our sector updates in our separate Technical Update report.

Our Commitment to Quality

We are committed to providing the highest quality audit, with input from our market leading specialists, sophisticated data analytics and our wealth of experience.

Adding value

Our aim is to add value to the Council through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the Council promote improved standards of governance, better management and decision making and more effective use of resources.

Pat Kenny
Audit director

Responsibilities of the Audit and Governance Panel

Helping you fulfil your responsibilities

The primary purpose of the Auditor's interaction with the Audit and Governance Panel:

- Clearly communicate the planned scope of the financial statements audit
- Provide timely observations arising from the audit that are significant and relevant to the Audit and Governance Panel's responsibility to oversee the financial reporting process
- In addition, we seek to provide the Audit and Governance Panel with additional information to help fulfil your broader responsibilities

We use this symbol throughout this document to highlight areas of our audit where the Audit and Governance Panel need to focus their attentions.

As a result of regulatory change in recent years, the role of the Audit and Governance Panel has significantly expanded. We set out here a summary of the core areas of Audit and Governance Panel responsibility to provide a reference in respect of these broader responsibilities and highlight throughout the document where there is key information which helps the Audit and Governance Panel in fulfilling its remit.

Oversight of external audit

- At the start of each annual audit cycle, ensure that the scope of the external audit is appropriate.

- Implement a policy on use of the external auditor for non-audit services and approve these services if they arise.

Integrity of reporting

- Make an impact assessment of key judgements and the level of management challenge.

- Review the external audit findings, key judgements and level of misstatements.

- Assess the quality and capacity of the internal team.

- Assess the completeness of disclosures, including consistency with disclosures on business model and strategy and, where requested by the Council, provide advice in respect of the fair, balanced and understandable statement.

- Assess and advise the Council on the appropriateness of the Annual Governance Statement.

Internal controls and risks

- Review the internal control and risk management systems.

- Explain what actions have been, or are being taken to remedy any significant failings or weaknesses.

- Oversee the work of the Council's local counter fraud service.

Oversight of internal audit

- Consider annually whether the scope of the internal audit programme is adequate.

- Monitor and review the effectiveness of the internal audit activities.

Whistle-blowing and fraud

- Ensure that appropriate arrangements are in place for the proportionate and independent investigation of any concerns that are raised by staff in connection with improprieties.

Our audit explained

We tailor our audit to your Council and your strategy

Identify changes in your Council and environment

The Council continues to face significant financial pressures due to an increase in costs and demand for services as well as a risk of reduced available funding.

The integration of health and social care also continues to be a challenge, as discussed in page 11.

Scoping

Our scope is in line with the Code of Audit Practice issued by Audit Scotland.

More detail is given on pages 13-15.

In our final report

In our final report to you we will conclude on the significant risks identified in this paper and report to you our other findings.

1. Identify Changes in your business and environment
2. Determine materiality
3. Scoping
4. Significant risk assessment
5. Conclude on significant risk areas
6. Other findings
7. Our audit report

Determine materiality

We have determined a group materiality of £6,692k (2017/18: £6,786k) with a performance materiality of £5,019k (2017/18: £5,090k). This is based on gross expenditure adjusted for net contributions made to the IJB in line with prior year. For the audit of the Council only, a materiality of £6,625k (2017/18: £6,745k) has been determined, with performance materiality of £4,968k (2017/18: 5,058k).

We will report to you any misstatements above £250k (2017/18: £250k). More detail is given on page 12.

Significant risk assessment

We have identified significant audit risks in relation to the Council. More detail is given on pages 16-19. These significant risks are consistent with those identified in our prior year audit.

Quality and Independence

We confirm all Deloitte network firms are independent of the Council. We take our independence and the quality of the audit work we perform very seriously. Audit quality is our number one priority.

Continuous communication and reporting

Planned timing of the audit

Planning	Interim	Year end fieldwork	Reporting
• Planning meetings to inform risk assessment and identify judgemental accounting issues. • Update understanding of key business cycles and changes to financial reporting. • Document design and implementation of key controls for significant risks. • Review of key Council documents including Committee minutes. • Planning work for wider scope responsibilities.	• Initiate substantive procedures addressing significant risk around management override of control. • Update risk assessments for any developments since the planning phase before fieldwork begins. • Initiate wider scope procedures. • Completion of NFI questionnaire.	• Review of draft accounts. • Substantive testing of all material areas. • Finalisation of work in support of wider scope responsibilities. • Detailed review of annual accounts and report, including the Annual Governance Statement. • Review of final internal audit reports and opinion. • Completion of testing on significant audit risks. • Submission of certified grant claims.	• Final Audit and Governance Panel meeting. • Issue final Annual Report to the Council and the Controller of Audit. • Issue audit report and submission of audited financial statements to Audit Scotland (including charitable trusts). • Completion of Minimum Data Set. • Audit feedback meeting.
2018/19 Audit Plan	Final report to the AGP		
November-January	**February-June**	**July - August**	**September**

Ongoing communication and feedback

Audit Team

Pat Kenny, Audit Director

Karlyn Watt, Senior Manager

James Corrigan, Manager

Coenraad Balfoort, Field Manager

An audit tailored to you

Focusing on your business and strategy

	Impact on our audit
Future financial strategy and sustainability	The Council continues to face significant financial challenges in the medium to longer term. This is supported by the fact that a Strategic Risk around financial constraint is included on the Register. We note, however, that this is not reflected in the short term, as the 2018/19 forecast position as at 30 September 2018 for general services (excluding the HSCP) is £3,586k below its revenue budget, which includes an underspend against all directorates. The one area projecting an overspend is HSCP (£3,891k), which results in an overall projected overspend position which may be met initially from reserves and reimbursed by HSCP in future years. Whilst using reserves in the short term to bridge funding gaps is possible this year, it is not sustainable in the longer term. This is supported by the 2018-22 Financial Strategy which indicates a medium-term revenue budget gap of £31,600k demonstrating a challenge to the medium- to longer-term financial sustainability of the Council. The Council anticipates that there will be further significant cash reductions in the General Revenue Grant from the Scottish Government over the forthcoming years. The Council will have to find solutions to the emerging funding gap and there is a risk that they will not be able to achieve the savings required. Simultaneously the Council will have to manage an ever increasing demand for Council services and manage cost pressures that apply to the models of service delivery. We noted as part of our 2017/18 audit that the Council's transformation strategy "Transform South Ayrshire" will be refreshed under the new Directorates to move away from the original focus of just IT. We will review the refreshed transformation strategy to ensure that it meets best practice requirements and to ensure that it addresses how the required savings can be made.

New significant risk

Continuing significant risk

Considered as part of wider scope audit requirements

An audit tailored to you
Focusing on your business and strategy (continued)

	Impact on our audit
Health and social care integration	2017/18 was the third full financial year of the HSCP between NHS Ayrshire and Arran and the Council through the IJB. While an underspend was achieved by the HSCP in 2017/18, there is a risk in 2018/19 and future years that the partnership will not be able to achieve financial balance, as demonstrated by the projected overspend for 2018/19 of £3,891k, as reported in their budget monitoring report to 31 December 2018 presented to the Council's Leadership Panel on 12 February 2019. We note that this projected overspend is in relation to the services that the Council have been commissioned to provide for the HSCP as reported in the revenue budget monitoring report. However, the full IJB position, per the report that was presented to the IJB on 13 February 2019 is an overspend of £3,887k. This projected overspend position includes £337k of achievable Recovery Plan actions as agreed at the IJB on 3 October 2018. While the paper to the IJB on 12 December 2018 confirmed that a further recovery plan was due to be presented to the IJB to set out how they intend to achieve a break even position by 31 March 2019, it is acknowledged that the possibility of this being achieved is highly unlikely and that the IJB will require additional funding from the funding parties. Therefore, it is critical that the Council continues to work closely with the IJB and the NHS Board to focus on identifying further sources of recurring savings through efficiencies or service redesign for future years' financial sustainability. We will continue to review the work being done both at the Council and the IJB to address these funding gaps, including whether progress is being made towards developing a fully integrated budget that incorporates the set aside budget.

New significant risk

Continuing significant risk

Considered as part of wider scope audit requirements

Materiality

Our approach to materiality

Basis of our materiality benchmark

- The audit director has determined materiality for the group as £6,692k (2017/18: £6,786k) and performance materiality of £5,019k (2017/18: £5,090k), based on professional judgement and risk factors specific to the Council, the requirement of auditing standards and the financial measures most relevant to users of the financial statements.
- We have used 1.6% of last year's benchmark flexed for the percentage movement between last year's P12 gross expenditure outturn and the 2018/19 forecast gross expenditure per the latest budget monitoring report, adjusted for net contributions to the IJB as the benchmark for determining materiality and applying 75% as performance materiality.
- This approach is consistent with our prior year materiality calculation.
- For the audit of South Ayrshire Council (Council only) a materiality of £6,625k (2017/18: £6,745k) has been determined, and performance materiality of £4,968k (2017/18: 5,058k).

Reporting to those charged with governance

- We will report to you all misstatements found in excess of our clearly trivial threshold which is £250k (2017/18: £250k) for both the group and Council only.
- Our approach to determining the materiality benchmark is consistent with Audit Scotland guidance which states that the threshold for clearly trivial above which we should accumulate misstatements for reporting and correction to audit committees must not exceed £250k.

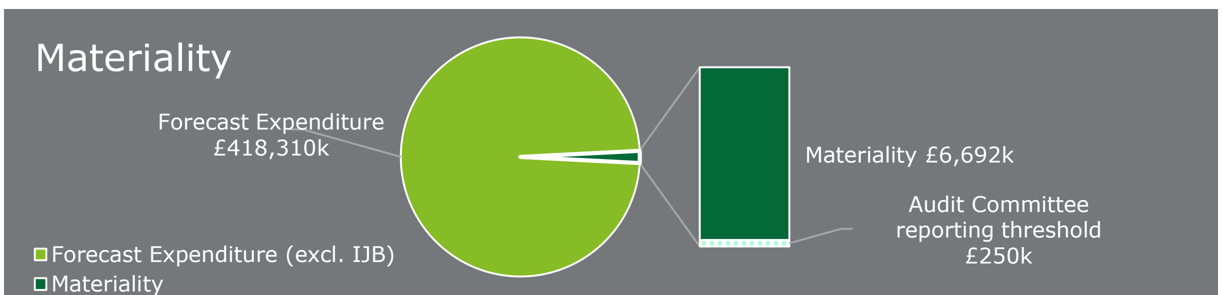
Our annual audit report to the AGP

We will:

- Report the group materiality, Council only materiality and the range we use for component materialities;
- provide comparative data and explain any changes in materiality, compared to prior year, if appropriate; and
- explain any normalised or adjusted benchmarks we use, if appropriate.

Group scoping

In addition to performing full audit procedures for South Ayrshire Council, we will also perform a full audit to component materiality as auditors of the Integration Joint Board, Ayrshire Valuation Joint Board, and charitable trusts. The Strathclyde Partnership for Transport is the only other material component and we will liaise with its auditors to gain assurance over the balances consolidated. All other components are immaterial and will be covered by desktop reviews at the group level.



Although materiality is the judgement of the Audit Director, the Audit and Governance Panel must satisfy themselves that the level of materiality chosen is appropriate for the scope of the audit.

Scope of work and approach

Our key areas of responsibility under the Code of Audit Practice

Core audit work	Planned output	Timeline
Perform an ISA (UK) compliant audit of the annual accounts	• Annual audit plan • Interim report (if required) • Independent auditor's report	• 20 February 2019 • April 2019 • September 2019
Audit and report on the audit dimensions	• Annual audit plan • Annual audit report	• 20 February 2019 • September 2019
Contribute to performance audits (including performance audit reports, overview reports and impact reports)	• Minimum datasets • Data returns	• September 2019 • As required
Share audit intelligence with Audit Scotland including highlighting potential statutory reports	• Current issues returns	• January, March, August and October 2019
Provide assurance on Whole of Government Accounts (WGA)	• Assurance statement on WGA returns	• September 2019
Carry out preliminary enquiries into referred correspondence	• None	• N/A
Provide information on cases of fraud	• Fraud returns	• November 2018, February, May and August 2019
Provide information on cases of money laundering	• Audit Scotland to advise	• As required
Contribute to National Fraud Initiative (NFI) report	• NFI audit questionnaire • Reference, if necessary, in annual audit report	• June 2019
Contribute to technical guidance notes	• Consultation comments on draft technical guidance notes	• As required
Contribute to technical databases	• Database returns	• July 2019

Scope of work and approach (continued)

Our key areas of responsibility under the Code of Audit Practice (continued)

Core audit work	Planned output	Timeline
Audit and report on Best Value	• Annual audit report	• September 2019
Consider and report on the Strategic Audit Priorities	• Annual audit plan • Annual audit report	• 20 February 2019 • September 2019
Lead the Shared Risk Assessment	• Any locally agreed output	• As required
Carry out Statutory Performance Information work	• Annual audit plan • Annual audit report	• 20 February 2019 • September 2019
Certify grant claims	• Certificate in support of grant claims	• As required
Liaise with housing benefit performance auditor	• None	• N/A

Scope of work and approach (continued)
Our approach

Liaison with internal audit

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

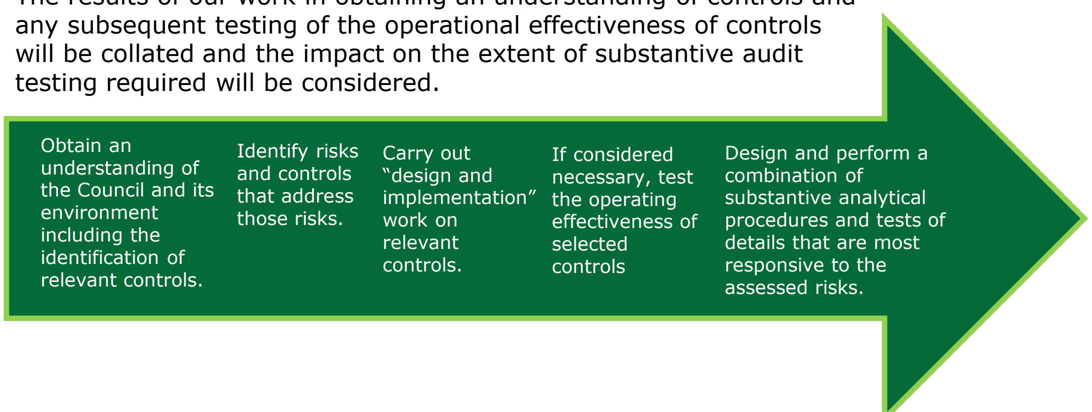
We will review their reports and meet with them to discuss their work. We will discuss the work plan for internal audit, and where they have identified specific material deficiencies in the control environment we consider adjusting our testing so that the audit risk is covered by our work.

Using these discussions to inform our risk assessment, we can work together with internal audit to develop an approach that avoids inefficiencies and overlaps, therefore avoiding any unnecessary duplication of audit requirements on the Council's staff.

Approach to controls testing

Our risk assessment procedures will include obtaining an understanding of controls considered to be 'relevant to the audit'. This involves evaluating the design of the controls and determining whether they have been implemented ("D&I").

The results of our work in obtaining an understanding of controls and any subsequent testing of the operational effectiveness of controls will be collated and the impact on the extent of substantive audit testing required will be considered.



Promoting high quality reporting to stakeholders

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

We will utilise the Code of practice on local authority accounts in the UK disclosure checklist to support the Council in preparing high quality drafts of the annual report and financial statements, which we would recommend the Council complete during drafting.

The Disclosure Checklist reflects the cutting clutter agenda and includes a "not material" column. We would encourage the Council to exclude disclosure if the information is not material.

Audit Scotland has published good practice guides in relation to the Annual Report and the Governance Statement to support the Council in preparing high quality drafts of the Annual Report and financial statements, which we would recommend the Council consider during drafting.

Significant risks

Our risk assessment process

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

- the significant risks and uncertainties previously reported in the annual report and financial statements;
- the IAS 1 critical accounting estimates previously reported in the annual report and financial statements;
- our assessment of materiality;
- the changes that have occurred in the business and the environment it operates in since the last annual report and financial statements; and
- the Council's actual and planned performance on financial and other governance metrics compared to its peers.

Principal risk and uncertainties

- Financial pressure including risk of reduced funding from Scottish Government
- Service and cost pressures
- Other budgetary pressures, e.g. pay pressures and inflationary pressures

IAS 1 Critical accounting estimates

- Impairment and fair value measurement of property, plant and equipment
- Public Private Partnerships (PPP)
- Provisions and contingent liabilities
- Leases
- Pensions liability
- Bad debts

Changes in your business and environment

- EU withdrawal is the biggest potential change in the environment (as discussed further on page 24)

The next page summarises the significant risks that we will focus on during our audit. All the risks mentioned in the prior year Audit and Governance Panel report are included as significant risks in this year's audit plan.

Significant risks
Dashboard

Risk	Material?	Fraud risk identified?	Planned approach to controls testing	Level of management judgement	Page no.
Recognition of grant income	✓	✓	Design and implementation	⚠	18
Management override of controls	✓	✓	Design and implementation	⚠	19

⚠ Some degree of management judgement

⚠ Limited management judgement

Significant risks (continued)

Risk 1 – Recognition of grant income

Risk identified

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

Key components of income for the Council are summarised in the table to the right. The General Revenue Grant and non-domestic rates income which are directed by the Scottish Government are not considered as significant risks as the process for receipt of this income is not complex and can be verified 100%. Council tax and housing rent income are set through the annual budget process with no management judgement and therefore have a low risk of fraud. Similarly, Other Service Income includes fees and charges across all Services, which are set through formal approval processes, with no history of fraud or error. Finally, income from the Department of Works and Pensions (DWP) are claimed in full via an annual subsidy claim and are subject to separate grant certification procedures, which we will rely on.

The significant risk is pinpointed to the recognition of grant income, comprising capital grants and contributions and service specific grants.

Grant income is a significant risk due to:

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

Type of income	Grant Income 2017/18 (£k)	Sig risk?	Other Service Income 2017/18 (£k)	Sig risk?
Taxation and Non-Specific Grant Income				
General revenue grant	156,390		-	
Receipted capital income	**14,810**	✓	-	
Non-domestic rates income	39,756		-	
Council tax income	52,039		-	
Service Income				
Chief Executive's Strategic Office	-		4	
Education Services	**5,817**	✓	905	
Economy, Neighbourhood & Environment	**3,180**	✓	31,208	
Housing Revenue Account	-		32,243	
Health & Social Care	**3,690**	✓	95,424	
RGO (excl DWP)	**262**	✓	5,862	
RGO – DWP	34,881		-	
Miscellaneous Services	-		2,392	

Our response

We will perform the following:

- assess management's controls around recognition of grant income; and
- test a sample of capital grants and contributions and grant income credited to Service Income and confirm these have been recognised in accordance with any conditions applicable.

Significant risks (continued)

Risk 2 – Management override of controls

We will use computer assisted audit techniques, including Spotlight, to support our work on the risk of management override

Risk identified	In accordance with ISA 240 (UK) management override is a significant risk. This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Council's controls for specific transactions. The key judgements in the financial statements are those which we have selected to be the significant audit risks around recognition of grant income. This is inherently the areas in which management has the potential to use their judgement to influence the financial statements.
Planned audit challenge	In considering the risk of management override, we plan to perform the following audit procedures that directly address this risk: **Journal testing** • We will test the design and implementation of controls over journal entry processing. • Using our Spotlight data analytics tool, we will risk assess journals and select items for detailed follow-up testing. The journal entries will be selected using computer-assisted profiling based on areas which we consider to be of increased interest. • We will test the appropriateness of journal entries recorded in the general ledger, and other adjustments made in the preparation of financial reporting. **Accounting estimates** • We will test the design and implementation of controls over key accounting estimates and judgements. • We will review accounting estimates for biases that could result in material misstatements due to fraud. This will include both a retrospective review of 31 March 2018 estimates and a review of the corresponding estimates as at 31 March 2019. **Significant and unusual transactions** • We will obtain an understanding of the business rationale of significant transactions that we become aware of that are outside of the normal course of business for the entity, or that otherwise appear to be unusual, given our understanding of the entity and its environment.

Wider scope requirements

Audit dimensions

The Code of Audit Practice sets out four audit dimensions which set a common framework for all public sector audits in Scotland. We will consider how the Council is addressing these areas, including any risks to their achievement, as part of our audit work as follows:

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.	• The financial planning systems in place across the shorter and longer terms. • The arrangements to address any identified funding gaps. • The affordability and effectiveness of funding and investment decisions made. • Workforce planning.	We recommended in our 2017/18 audit report that future transformation plans apply best practice as set out in our report. We noted that the Council's transformation strategy "Transform South Ayrshire" is currently being refreshed under the new Directorates to move away from the original focus of IT. We will review the refreshed transformation strategy to assess whether it meets best practice requirements and to assess whether it addresses how the required savings can be made through transformation. **Audit Risk:** The strategy does not adequately set out how the transformation will achieve the savings needed to address the emerging medium to longer term funding gap and to meet increased demand on Council services. In view of the Scottish Government's Medium Term Financial Strategy (MTFS) (discussed further on page 25) we will consider the extent to which the Council has reviewed the potential implications of the MTFS for its own financial planning and whether it is taking these into account in its arrangement for financial management and financial sustainability. **Audit Risk:** The Council's long-term financial planning is inconsistent with the Scottish Government's five-year plan.

Wider scope requirements (continued)

Audit dimensions (continued)

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.	• Systems of internal control. • Budgetary control system. • Financial capacity and skills, including plans for replacing the recently departed Head of Finance. • Arrangements for the prevention and detection of fraud.	We recommended in our 2017/18 audit report that outcome-based budgeting be incorporated into the annual budget-setting processes. We will review the 2019/20 budget to assess the progress made. **Audit Risk:** Given ongoing demand pressures and decreasing funding, as projected under all three scenarios in the 2018-22 Financial Strategy, there is a risk that if budgets aren't prioritised, funding is not directed to the areas that need it most. In view of the Scottish Government's new budget process (discussed further on page 25) we will confirm that underlying financial performance including any in-year changes to funding agreed with the Scottish Government, is transparently presented. **Audit Risk:** The underlying financial performance of the Council is not transparently reported. Our fraud responsibilities and representations are detailed on pages 36 and 37.

Wider scope requirements (continued)

Audit dimensions (continued)

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making, and transparent reporting of financial and performance information.	• Governance arrangements. • Scrutiny, challenge and transparency on decision making and financial and performance reports. • Quality and timeliness of financial and performance reporting.	We recommended in our 2017/18 audit report that the staffing of internal audit be embedded. We will liaise with internal audit during the audit, which will include reviewing progress against the annual internal audit plan. **Audit Risk:** If the team are not embedded there is a risk that the internal audit plan will fall behind schedule or not be achieved, resulting in insufficient work being completed in the period to provide assurance over the internal control environment of the Council. We also recommended in our 2017/18 audit report that the Council improve community involvement via increased community empowerment, community takeover and participatory budgeting. We will review progress in developing the engagement strategy and implementation of this. **Audit Risk:** If community empowerment, community takeover and participatory budgeting is not improved, there is the risk of a lack of transparency around decision-making. In view of the increased focus on how public money is used and what is achieved (as discussed further on page 27), we will consider how the Council has reviewed its approach to openness and transparency. **Audit Risk:** The Council's approach is not keeping pace with public expectation and good practice.

Wider scope requirements (continued)

Audit dimensions (continued)

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
Value for money is concerned with using resources effectively and continually improving services.	• Value for money in the use of resources. • Link between money spent and outputs and the outcomes delivered. • Improvement of outcomes. • Focus on and pace of improvement.	In our 2017/18 audit report we recommended that the Council consider external peer reviews on services to ensure there is enough challenge/scrutiny to ensure improvement of services. We will monitor progress against this recommendation during our audit. **Audit Risk:** Services are not performing at the optimal level of efficiency and effectiveness. In view of the Scottish Government's new budget process (discussed further on page 25) we will consider the extent to which the Council performance report provides an accessible account of the Council's overall performance and impact of its public spending. **Audit Risk:** The Council does not clearly report on its contribution towards the national outcomes.

Wider scope requirements (continued)

Specific risks

As part of the 2018/19 planning guidance, Audit Scotland have identified the following areas as significant risks faced by the public sector. Any specific risks in relation to these areas for the Council have been included in our audit risk under the audit dimensions, discussed on the previous pages. We will continue to monitor these areas as part of our audit work.

Risk	
EU withdrawal	There are uncertainties surrounding the terms of the UK's withdrawal from the European Union in March 2019. Some arrangements have been provisionally agreed, such as a transition period to the end of 2020, although they are dependent on a final deal being reached between the UK Government and the remaining EU countries. The outcome of negotiations should become clearer in the months up to March 2019. Whatever the outcome, EU withdrawal will inevitably have implications for devolved government in Scotland and for audited bodies. Audit Scotland has identified three areas where EU withdrawal may have the most significant impact as summarised below: • **Workforce** – Many public services are dependent on workers from EU countries, including health, social care and education. A decline in migration from the EU could potentially result in vacancies and skills' gaps in some areas of the public sector. There is a risk that this could impact on some public bodies' ability to deliver 'business as usual' particularly given existing workforce and service pressures. • **Funding –** Funding from the EU makes an important contribution to the Scottish public sector. The main sources of funding provide support to farmers and rural businesses, projects to encourage economic growth and support for research and education. The UK Government has made guarantees to meet some funding commitments to the end of existing programmes, but there are uncertainties about what any replacement funding may look like. • **Regulation –** The EU Withdrawal Bill will transpose existing EU law into UK law immediately after the UK leaves the EU. Legislation in many devolved areas will transfer to the Scottish Parliament. The UK government has identified 24 devolved policy areas where it seeks to retain temporary control until UK-wide common legislative frameworks are developed. This is currently an area of contention between the Scottish and UK Governments and is under consideration by the Supreme Court. In addition, some public bodies may be affected directly by changes to trade and customs' rules, which could impact on supply chains and the procurement of goods or services from EU countries. This could influence the availability and cost of supplies and services (e.g. specialist medical equipment or drugs) with potential implications for public bodies' finances and their ability to deliver specific services. While there are considerable uncertainties about the detailed implications of EU withdrawal, at a minimum by the end of 2018/19, we would expect public bodies to have assessed the potential impact of EU withdrawal on their operations and identified any specific risks and how they will respond to them. We will assess how the Council has prepared for EU withdrawal and how it continues to respond to any emerging risk after March 2019. Some suggested key questions for the AGP are included in our separate Sector Update paper. In addition, in accordance with the FRC guidance, the Council should consider the ***disclosure within its annual report***, and distinguish the specific and direct challenges that it faces from the broader economic uncertainties. In some circumstances this many mean ***recognising or re-measuring*** certain items in the Balance Sheet. A comprehensive **post balance sheet events review** must be reflected in accounts and disclosures.

Wider scope requirements (continued)

Specific risks (continued)

Risk	
Changing landscape for public financial management	Scottish public finances are fundamentally changing, with significant tax-raising powers, new powers over borrowing and reserves, and responsibility for 11 social security benefits worth over £3 billion a year. This provides the Scottish Parliament with more policy choices but also means that the Scottish budget is subject to greater volatility, uncertainty and complexity. Parliamentary scrutiny of the public finances is increasingly important in this changing landscape. A new Scottish budget process has been introduced, which is based on a year-round continuous cycle of budget setting, scrutiny and evaluation. This involves parliamentary committees looking back to explore what public spending has achieved, looking forward to longer-term objectives and challenges, and considering what this should mean for future budgets. As part of the new budget process, the Scottish Government published an initial five-year Medium Term Financial Strategy (MTFS) in May 2018. This five-year outlook for the Scottish budget provides useful context for audited bodies' financial planning. As part of our wider scope audit work on financial management and financial sustainability (discussed further on pages 20 to 21), we will consider how the Council has reviewed the potential implications of the MTFS for its own finances, including longer-term financial planning. The new budget process places greater emphasis on assessing outcomes and the impact of spending. There is an expectation that the Scottish Government and public bodies will report on their contributions towards the national outcomes in their published plans and performance reports, including their annual reports. Increased complexity and volatility is also likely to mean that the Scottish Government will be increasingly active in managing its overall budget position in-year, engaging with public bodies closely on their anticipated funding requirements. As part of our wider scope audit work on financial sustainability and value for money (discussed further on pages 20 and 23) we will consider the extent to which the Council's performance report provides an accessible account of the body's overall performance and impact of its public spending. We will also confirm that underlying financial performance, including any in-year changes to funding agreed with the Scottish Government, is transparently presented.

Wider scope requirements (continued)

Specific risks (continued)

Risk	
Care income, financial assessments and financial guardianship	The experience of a few local government audits indicates there may be wider issues with the systems and processes for collecting care income, undertaking financial assessments on individuals receiving care and financial guardianship. In some cases, responsibility for financial assessment on those receiving care has transferred from social care to finance and this has revealed issues with backlogs of financial assessment and under-recovery of care charges over long periods. Each individual case may have different circumstances contributing to a delay and some of these delays are not within the councils' control, but there are examples where inadequate focus on this area has led to delays that are attributable to the council. After taking legal advice, Audit Scotland does not believe these statutory debts are subject to prescription periods, so are generally collectable even where delays are considerable. In some cases, the Council will take charge over property, where income is insufficient to meet care costs. We will undertake a review of the arrangements for financial assessment of those requiring care and assess whether these are subject to a significant backlog and the reporting of this. Audit Scotland has also identified that officers within the Council may be operating as financial guardians for individuals with a lack of capacity to act in their own interest. This financial guardianship role is distinct from a welfare guardian (usually the chief social work officer) and is subject to approval by a Sherriff. Financial guardianship by a council officer is the solution of last resort when no other member of a family, friend, neighbour or local solicitor is willing to act in this role. This may give risk to a potential conflict of interest when finance officers are in a senior position and the council is issuing invoices to a person for their care and the officer is also acting as financial guardian for the individual. We will be requested to complete a questionnaire to provide intelligence on the extent to which officers undertake financial guardianship roles and the reasons for this.

Wider scope requirements (continued)

Specific risks (continued)

Risk	
Dependency on key suppliers	It has become clear that the collapse of Carillion has had a significant impact across the public sector. This has brought into focus the risk of key supplier failure and the risk of underperformance in suppliers that are experiencing difficult trading conditions. The risk exists on two levels: • individual public sector bodies are dependent on key suppliers; and • the Scottish public sector as a whole is subject to significant systemic risk. We will determine as part of our detailed risk assessment the extent to which the Council is dependent on key supplier relationships. Where dependency is significant, we will consider this as part of our audit work and report back to the Audit and Governance Panel. We will also be requested to complete a short questionnaire to establish the extent, value and nature of key supplier dependencies that can inform the national position.
Openness and transparency	There is an increasing focus on how public money is used and what is achieved. In that regard, openness and transparency supports understanding and scrutiny. We will consider this as part of our wider scope work on governance (discussed further on page 22). We would expect to see public bodies reviewing their approach to openness and transparency to ensure they are keeping pace with public expectations and good practice. Evidence of progress might include: • increased public availability of Council, AGP, and other appropriate committee papers; • more insight into why some business is conducted in private; and • development of the form and content of annual reports.

Wider scope requirements (continued)

Other responsibilities

Best Value

In June 2016 the Accounts Commission formally agreed the overall framework for a new approach to auditing Best Value (BV). This framework introduced a five year approach to auditing BV. 2018/19 represents year three of the BV audit plan. Under this approach, the Controller of Audit will provide a Best Value Assurance Report (BVAR) to the Commission for each Council at least once in a five year period. The national five year BVAR programme is updated each year reflecting changes to risk assessments identified from the SRA process or annual audits. South Ayrshire Council has not been identified for a BVAR report in 2018/19.

Our BV audit work in 2018/19 will be integrated into our audit approach, including our work on the audit dimensions discussed on pages 20 to 23, and will be reported in our annual audit report.

Strategic audit priorities

In its Strategy, which is updated annually, the Accounts Commission sets out an overall aim of holding councils to account for their pace, depth and continuity of improvement facilitated by effective governance. Within this, the Commission also sets out five Strategic Audit Priorities that will be built into audit expectations, which are set out below:

- Having clear priorities with a focus on outcomes, supported by effective long term planning.
- Demonstrating the effective appraisal of options for changing how services are delivered in line with their priorities.
- Ensuring that members and officers have the right knowledge, skills and support to design, develop and deliver effective services in the future.
- Empowering local communities and involving them in the design and delivery of local services and planning for their local area.
- Reporting the council's performance in a way that enhances accountability to citizens and communities, helping them contribute better to the delivery of improved outcomes.

We will consider each of these areas as part of our audit dimensions work and report within our annual audit report.

Wider scope requirements (continued)

Other responsibilities (continued)

Shared Risk Assessment and Joint Scrutiny Planning

The Accounts Commission, supported by Audit Scotland, chairs the Strategic Scrutiny Group (SSG). The SSG is made up of scrutiny bodies from across the public sector to make their work on local government more co-ordinated, better targeted and more proportionate to identified risks.

The arrangements for coordinating scrutiny at a local level include a Local Area Network (LAN) for each Council. LANs are led by each Council's appointed auditor. LANs bring together relevant scrutiny bodies, typically Audit Scotland, Care Inspectorate, Education Scotland and the Scottish Housing Regulator, to share information and intelligence on an ongoing basis and to carry out a Shared Risk Assessment (SRA). The purpose of the SRA is to inform discussions between the LAN and its Council and to inform the National Scrutiny Plan (NSP) for local government.

A number of changes have been made to the process for 2018/19, the most notable being there is no requirement for LANs to produce local scrutiny plans. LANs can produce local outputs if they determine, in consultation with the Council, that this would be useful. The new approach looks to embed a discussion about risks and responses between scrutiny bodies across the year, rather than a specific one-off approach.

Councils' Statutory Performance Indicators

The Accounts Commission has a statutory responsibility to define the performance information that Councils must publish to allow citizens to gauge their performance comparatively. This responsibility links with the Commission's BV audit responsibilities. In turn, Councils have their own responsibilities, under their BV duty, to report performance to the public. The 2015 Statutory Performance Information Direction published by the Commission requires Councils to report a range of information in accordance with, but not confined to, the requirements of the LGBF. The Commission has committed to reviewing its 2015 Direction after three years, this will be updating its Direction at the end of 2018.

We will assess the suitability of the arrangements for preparing and publishing the information, closely linked to our work on the Strategic Audit Priority "Reporting the council's performance in a way that enhances accountability to citizens and communities, helping them contribute better to the delivery of improved outcomes" discussed on page 28.

Wider scope requirements (continued)

Other responsibilities (continued)

Performance Audits

In accordance with Audit Scotland planning guidance, we will be requested to provide information to support performance audits that Audit Scotland intends to publish during 2018/19 and 2019/20, as summarised below:

Title and planned publication date	**Local auditor input**
Innovative Financing: City Deals – Autumn 2019	Evidence gathered through the routine local audit work in relation to City Deal arrangements as applicable to the audited body. Note that the three Ayrshire Councils are currently in negotiations with the UK and Scottish Governments relating to the Ayrshire Growth Deal.
Digital progress in local government – Spring 2020	We will be asked to inform the performance audit team of any significant ICT and digital developments within their audited body.
Education outcomes – Winter 2019	Scoping work for the audit will take place in early 2019 and will inform any specific input required from auditors. This is likely to be providing an update on governance arrangements and operation of the Regional Improvement Collaboratives.
Value for money of non-profit distributing models of capital financing – Summer 2019	Scoping work for this audit is under way and it is not anticipated that a formal data return will be required from auditors. The performance audit team will consider national data and liaise with local auditors around potential case studies as appropriate.
Waste management	Guidance will be provided to auditors, but would typically seek information in relation to local, regional and national waste management arrangements, including cost, investment, volume and Landfill Tax data.

Impact reports

We will also be requested to provide information to support assessing the impact of previously published performance audit reports as follows:

- Supporting Scotland's economic growth (Winter 2018)
- Equal pay in Scottish Councils (Spring 2019)
- Self-directed support: 2017 progress report (Spring 2019)
- Early learning and child care (Summer 2019)
- Transport Scotland's ferry services (Summer 2019)

Wider scope requirements (continued)

Other responsibilities (continued)

Anti-money laundering

The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 came into force on 26 June 2017 and replaced the Money Laundering Regulations 2007. The regulations impose an obligation of the Auditor General to inform the National Crime Agency if she knows or suspects that any person has engaged in money laundering or terrorist financing. As part of our audit work, we will ensure we are informed of any instances of money laundering at the Council so that we can advise the Auditor General.

National Fraud Initiative (NFI)

All Council's are participating in the NFI 2018/19. All data was required to be submitted in October 2018 and Councils will receive matches for investigation in January 2019. Audit Scotland expects bodies to investigate all recommended matches based on findings and the risk of error or fraud. Match investigation work should be largely completed by 30 September 2019 and the results recorded on the NFI system.

We will monitor the Council's participation and progress during 2018/19 and into 2019/20 and, where appropriate, include references to the NFI in our annual audit reports for both years. We will also complete an NFI audit questionnaire and submit to Audit Scotland by 30 June 2019.

Audit Quality
Our commitment to audit quality

Our objective is to deliver a distinctive, quality audit to you. Every member of the engagement team will contribute, to achieve the highest standard of professional excellence.

In particular, for your audit, we consider that the following steps will contribute to the overall quality:

- We will apply professional scepticism on material issues and significant judgements identified, by using our expertise in the local government sector and elsewhere to provide robust challenge to management.
- We have obtained a deep understanding of your business, its environment and of your processes in income and expenditure recognition, payroll expenditure and capital expenditure, enabling us to develop a risk-focused approach tailored to the Council.
- Our engagement team is selected to ensure that we have the right subject matter expertise and industry knowledge. We will involve specialists to support the audit team in our work.

In order to deliver a quality audit to you, each member of the core audit team will receive tailored learning to develop their expertise in audit skills, delivered by Pat Kenny and other sector experts. This includes sector-specific matters, and audit methodology updates.

Engagement Quality Control Review

We have developed a tailored Engagement Quality Control approach. Our dedicated Professional Standards Review (PSR) function will provide a 'hot' review before any audit or other opinion is signed. PSR is operationally independent of the audit team, and supports our high standards of professional scepticism and audit quality by providing a rigorous independent challenge.

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our report is designed to establish our respective responsibilities in relation to the financial statements audit, to agree our audit plan and to take the opportunity to ask you questions at the planning stage of our audit. Our report includes:

- Our audit plan, including key audit judgements and the planned scope; and
- Key regulatory and corporate governance updates, relevant to you.

What we don't report

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

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

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

Other relevant communications

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

This report has been prepared for the Audit and Governance Panel, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

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

Pat Kenny, CPFA

for and on behalf of Deloitte LLP

Glasgow

12 March 2019

Appendices

Prior year audit adjustments
Uncorrected and disclosure misstatements

Uncorrected misstatements

There were no uncorrected misstatements above our clearly trivial threshold and no uncorrected material disclosure deficiencies.

Fraud responsibilities and representations

Responsibilities explained

Your responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Our responsibilities:

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

Fraud characteristics:

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

We will request the following to be stated in the representation letter signed on behalf of the Council:

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

Fraud responsibilities and representations (continued)

Inquiries

We will make the following inquiries regarding fraud:

Management

- Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Management's process for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to employees regarding its views on business practices and ethical behaviour.
- Whether management has knowledge of any actual, suspected or alleged fraud affecting the entity.

Internal audit and local counter fraud specialist

- Whether internal audit and the Council's local counter fraud specialist has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain their views about the risks of fraud.

Those charged with governance

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

Independence and fees

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

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Council and will reconfirm our independence and objectivity to the Audit and Governance Panel for the year ending 31 March 2019 in our final report to the Audit and Governance Panel.
Fees	The audit fee for 2018/19, in line with the fee range provided by Audit Scotland, is £273,570 as analysed below:

	£
Auditor remuneration	167,310
Audit Scotland fixed charges:	
Pooled costs	16,220
Performance Audit and Best Value	77,740
Audit support costs	10,500
Total proposed fee	**271,770**

In addition, the audit fee for the charitable trusts audit is £1,800.

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

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

Our approach to quality

AQR team report and findings

We maintain a relentless focus on quality and our quality control procedures and continue to invest in and enhance our overall firm Audit Quality Monitoring and Measuring programme.

In June 2018 the Financial Reporting Council ("FRC") issued individual reports on each of the eight largest firms, including Deloitte, on Audit Quality Inspections which provides a summary of the findings of its Audit Quality Review ("AQR") team for the 2017/18 cycle of reviews.

We take the findings of the AQR seriously and we listen carefully to the views of the AQR and other external audit inspectors. We remediate every finding regardless of its significance and seek to take immediate and effective actions, not just on the individual audits selected but across our entire audit portfolio. We are committed to continuously improving all aspects of audit quality in order to provide consistently high quality audits that underpin the stability of our capital markets.

We have improved the speed by which we communicate potential audit findings, arising from the AQR inspections and our own internal reviews to a wider population, however, we need to do more to ensure these actions are embedded. In order to achieve this we have launched a more detailed risk identification process and our InFlight review programme. This programme is aimed at having a greater impact on the quality of the audit before the audit report is signed. Consistent achievement of quality improvements is our aim as we move towards the AQR's 90% benchmark.

All the AQR public reports are available on its website. https://www.frc.org.uk/auditors/audit-quality-review/audit-firm-specific-reports

The AQR's 2017/18 Audit Quality Inspection Report on Deloitte LLP

"The overall results of our reviews of the firm's audits show that 76% were assessed as requiring no more than limited improvements, compared with 78% in 2016/17. Of the FTSE 350 audits we reviewed this year, we assessed 79% as achieving this standard compared with 82% in 2016/17. We are concerned at the lack of improvement in inspection results. The FRC's target is that at least 90% of these audits should meet this standard by 2018/19."

"Where we identified concerns in our inspections, they related principally to aspects of group audit work, audit work on estimates and financial models, and audit work on provisions and contingencies. During the year, the firm has continued to develop the use of "centres of excellence", increasing the involvement of the firm's specialists in key areas of the audit. We have no significant issues to report this year in most of the areas we reported on last year."

"The firm has revised its policies and procedures in response to the revised Ethical and Auditing Standards. We have identified some examples of good practice, as well as certain areas for improvement."

The firm has enhanced its policies and procedures in the following areas:

- Increased use of centres of excellence ("CoE") involving the firm's specialists, including new CoEs focusing on goodwill impairment (established in response to previous inspection findings) and corporate reporting, to address increasing complexity of financial reporting.
- Further methodology updates and additional guidance issued to the audit practice including the audit approach to pension balances, internal controls, data analytics, group audits and taxation.
- A new staff performance and development system was implemented with additional focus on regular timely feedback on performance, including audit quality.
- Further improvements to the depth and timeliness of root cause analysis on internal and external inspection findings.

Our key findings in the current year requiring action by the firm:

- Improve the group audit team's oversight and challenge of component auditors.
- Improve the extent of challenge of management's forecasts and the testing of the integrity of financial models supporting key valuations and estimates.
- Strengthen the firm's audit of provisions and contingencies.

Review of firm-wide procedures. The firm should:

- Enhance certain aspects of its independence systems and procedures.