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Shetland Islands Council

Shetland Islands Council

Planning report to the Audit Committee on the 2020/21 audit

Issued on 12 February 2021 for the meeting on 23 February 2021

Contents

Planning report

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 annual accounts.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

I have pleasure in presenting our planning report to the Audit Committee of Shetland Islands Council ('the Council') for the 2020/21 audit. I would like to draw your attention to the key messages of this paper:

Audit plan

We have updated our understanding of the Council, including discussion with management and review of relevant documents. This has included consideration of the impact the COVID-19 pandemic has had on 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 expectation 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 12.

Audit dimensions

The Code of Audit Practice sets out four audit dimensions which set a common framework for all public sector audits in Scotland.

In carrying out our annual risk assessment, we have considered the arrangements in place for each dimension, building on our findings and conclusions from previous years' audits as well as planning guidance published by Audit Scotland. Our significant risks are presented on pages 26 to 33.

As part of our work on the audit dimensions, we will consider the arrangements in place to secure Best Value (BV) as well as other wider scope requirements set out on pages 26 to 33.

Introduction (continued)

The key messages in this report (continued)

Regulatory change

The implementation of the new standard on leases, IFRS 16, has been deferred again for another year, with a revised implementation date of 2022/23 and will require adjustments to recognise on balance sheet arrangements currently treated as operating leases.

Our audit approach reflects changes to International Standards on Auditing (UK) on going concern (ISA (UK) 570) and management estimates (ISA (UK) 540), and Practice Note 10, effective for this year.

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.

As part of our planning discussions with management, we have shared our "*Key Lessons from 2019/2020 Audits*" to help prepare for the 2020/21 audit, ensuring a focus on quality.

Added 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.

We have also shared our recent research, informed perspectives and best practice from our work across the wider public sector on pages 35 to 43 of this paper.

Pat Kenny
Audit Director

Responsibilities of the Audit Committee

Helping you fulfil your responsibilities

Why do we interact with the Audit Committee?

- To communicate audit scope
- To provide timely and relevant observations
- To provide additional information to help you fulfil your broader responsibilities

As a result of regulatory change in recent years, the role of the Audit Committee has significantly expanded. We set out here a summary of the core areas of Audit Committee 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 Committee 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 the engagement of the external auditor to supply non-audit services.

Integrity of reporting

- Impact assessment of key judgements and level of management challenge.

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

- Assess the quality of the internal team, their incentives and the need for supplementary skillsets.

- 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.

Internal controls and risks

- Review the internal control and risk management systems (unless expressly addressed by separate risk committee).

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

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 raised by staff in connection with improprieties.

We use this symbol to highlight areas of our audit where the Audit Committee needs to focus attention.

Your control environment

What we consider when we plan the audit

We expect management and those charged with governance to recognise the importance of a strong control environment and take proactive steps to deal with deficiencies identified on a timely basis.

Responsibilities of management

Auditing standards require us to only accept or continue with an audit engagement when the preconditions for an audit are present. These preconditions include obtaining the agreement of management and those charged with governance that they acknowledge and understand their responsibilities for, amongst other things, internal control as is necessary to enable the preparation of annual accounts that are free from material misstatement, whether due to fraud or error.

Responsibilities of the Audit Committee

As explained further in the Responsibilities of the Audit Committee slide on the previous page, the Audit Committee is responsible for:

- Reviewing the internal control and risk management systems (unless expressly addressed by a separate risk committee).
- Explaining what actions have been, or are being taken to remedy any significant failings or weaknesses.

As stakeholders tell us that they to wish to understand how external audit challenges and responds to the quality of an entity's control environment, we are seeking to enhance how we plan and report on the results of the audit in response. We will be placing increased focus on how the control environment impacts the audit, from our initial risk assessment, to our testing approach and how we report on misstatements and control deficiencies.

Reliance on controls	We will seek to undertake design and implementation testing on controls in respect of our identified significant risk areas. In accordance with forthcoming revisions to ISAs, we will assess inherent risk and control risk associated with accounting estimates.
Performance materiality	We set performance materiality as a percentage of materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed materiality. We determine performance materiality, with reference to factors such as the quality of the control environment and the historical error rate. Where we are unable to rely on controls, we may use a lower level of performance materiality.

Our audit explained

We tailor our audit to your business and your strategy

Identify changes in your business and environment

The Council continues to face significant financial pressures, which has increased during 2020/21 due to the COVID-19 pandemic. This is considered further on pages 17 to 19.

Scoping

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

More detail is given on page 11.

In our final report

In our final report to you we will conclude on the significant risks identified in this paper, report to you our other findings, and detail those items we will be including in our audit report, including key audit matters if applicable.

Identify changes in your business and environment → Determine materiality → Scoping → Significant risk assessment → Conclude on significant risk areas → Other findings → Our audit report

Determine materiality

We will use a materiality level of £3.691m (2019/20: £3.219m) in planning our audit. This is based on forecast gross expenditure. We will report to you any misstatements above £184k (2019/20: £160k).

Further details on our materiality considerations are provided on page 10.

Significant risk assessment

We have identified significant audit risks in relation to the Council. More detail is given on pages 12 to 14. The revenue risk is different to previous years as we have reassessed the risk profile of the Council and identified an alternative risk in relation to COVID-19 related income.

Quality and Independence

We confirm all Deloitte network firms and engagement team members are independent of Shetland Islands 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

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

Planning	Interim	Year end fieldwork	Reporting
• Planning meetings • Discussion of the scope of the audit • Discussion of audit fees • Discussion of fraud risk assessment • Update our understanding of key business cycles	• Carry out detailed risk assessments • Review of Council and Audit Committee papers and minutes • Complete wider scope procedures • Issue separate report on wider scope conclusions	• Audit of annual accounts, including annual governance statement • Year-end audit field work • Year-end closing meetings • Complete datasets	• Reporting of control deficiencies • Final Audit Committee meeting • Issue final Council and the Controller of Audit • Submission of audited annual accounts to Audit Scotland • Issue audited Whole of Government Accounts (WGA) • Audit feedback meeting
2020/21 Audit Plan	Report on audit dimensions and best value	Final report to the Audit Committee	
November 2020 – January 2021	**February – June 2021**	**July – September 2021**	**September 2021**

Ongoing communication and feedback

Materiality

Our approach to materiality

Basis of our materiality benchmark

- The Audit Director has determined materiality for the Council as £3.691m (2019/20: £3.219m) and performance materiality as £2.583m (2019/20: £2.575m), based on professional judgement, the requirements of auditing standards and the financial measures most relevant to users of the annual accounts.
- We have used 1.8% of forecast gross expenditure as the benchmark for determining materiality and applied 70% as performance materiality. We have judged expenditure to be the most relevant measure for the users of the accounts.
- The approach is consistent with previous years. However, the percentages applied have been revisited to take into account our knowledge of the Council and our understanding of the control environment, including the increased fraud risks as a result of the pandemic.

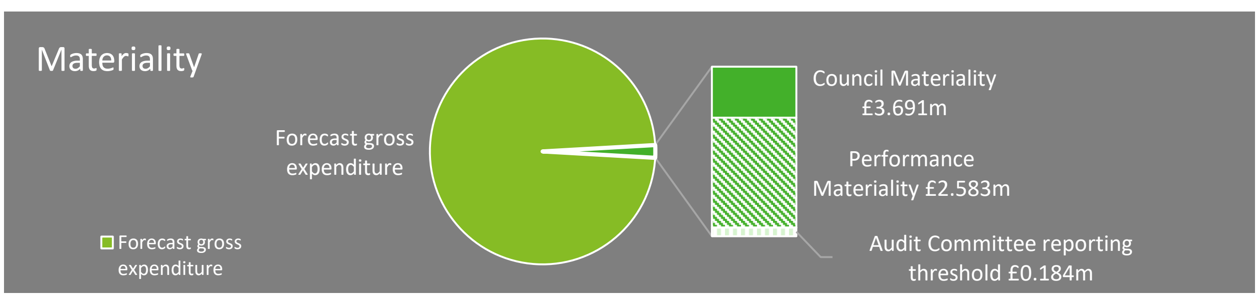
Reporting to those charged with governance

- We will report to you all misstatements found in excess of £184k (2019/20: £160k).
- We will report to you misstatements below this threshold if we consider them to be material by nature.
- 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 the Committee must not exceed £250k.

Our Annual Audit Report

We will:

- Report the materiality benchmark applied in the audit of the Council;
- Provide comparative data and explain any changes in materiality compared to prior year;
- Explain any normalised or adjusted benchmarks we use; and
- Explain the concept of performance materiality and state what percentage of materiality we used, with our rationale.



Although materiality is the judgement of the Audit Director, the Audit Committee 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
1. Auditing the annual accounts	Annual Audit Plan Independent auditor’s report	23 February 2021 30 September 2021
2. Audit dimensions, Best Value, Statutory Performance Information and Strategic Audit Priorities	Annual Audit Plan Report on audit dimensions and Best Value Annual Audit Report	31 March 2021 30 June 2021 30 September 2021
3. Contributing to performance audits	Dataset for overview report	March 2021 (submission deadline 8 May 2021)
4. Other wider scope audit work	Current issues returns Assurance Statement on WGA return Fraud Returns Certify grant claims	15 January, 26 March, 23 July and 22 October 2021 TBC Quarterly (30 November 2020, 28 February 2021, 31 May 2021 and 31 August 2021) As required

Significant risks

Significant risk dashboard

Risk	Fraud risk	Planned approach to controls	Level of management judgement	Page no
Management override of controls	✓	DI	⚠	13
Recognition of COVID-19 related income	✓	DI	⚠	14

Level of management judgement

⚠ High degree of management judgement

⚠ Some degree of management judgement

⚠ Limited management judgement

Controls approach adopted

DI Assess design and implementation

Significant risks (continued)

Management override of controls

Risk identified

Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent annual accounts by overriding controls that otherwise appear to be operating effectively.

Although management is responsible for safeguarding the assets of the entity, we planned our audit so that we had a reasonable expectation of detecting material misstatements to the annual accounts and accounting records.

Deloitte response and challenge

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

Test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the annual accounts. In designing and performing audit procedures for such tests, we plan to:

- test the design and implementation of controls over journal entry processing;
- make inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments;
- select journal entries and other adjustments made at the end of a reporting period; and
- consider the need to test journal entries and other adjustments throughout the period.

Review accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud. In performing this review, we plan to:

- evaluate whether the judgments and decisions made by management in making the accounting estimates included in the annual accounts, even if they are individually reasonable, indicate a possible bias on the part of the entity's management that may represent a risk of material misstatement due to fraud. If so, we will re-evaluate the accounting estimates taken as a whole; and
- perform a retrospective review of management judgements and assumptions related to significant accounting estimates reflected in the annual accounts of the prior year.

For significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual given our understanding of the entity and its environment and other information obtained during the audit, we shall evaluate whether the business rationale (or the lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets.

Significant risks (continued)

Recognition of COVID-19 related income

Risk identified and key judgements

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.

We have assessed the income streams of the Council, the complexity of the recognition principles and the extent of any estimates used, and concluded that, with the exception of the funding received in 2020/21 in response to the COVID-19 pandemic, there is no significant risk of fraud.

During 2020/21, the Council has received additional funding in relation to COVID-19 mobilisation costs, although all funding has not yet been confirmed. In addition, there are a number of business support schemes designed to help eligible businesses during the COVID-19 pandemic that are being administered by Councils on behalf of the Scottish Government.

We have pinpointed the significant risk to the completeness and occurrence of the funding for COVID-19 mobilisation costs and the completeness and accuracy of the agency arrangement disclosures.

The key judgements for management are assessing:

- any conditions associated with the mobilisation cost funding; and
- whether the Council is acting as a principal or agent in administering the business support schemes.

Deloitte response and challenge

We will perform the following:

- assess the design and implementation of the controls in relation to the accounting treatment of all COVID-19 related funding;
- test a sample of funding for COVID-19 mobilisation costs and confirm these have been recognised in accordance with any conditions applicable; and
- test the agency arrangement disclosures to confirm, where it is concluded that the Council is acting as an agent, that:
  - transactions have been excluded from the Comprehensive Income and Expenditure Statement;
  - the Balance Sheet reflects the debtor or creditor position at 31 March 2021 in respect of cash collected or expenditure incurred on behalf of the principal; and
  - the net cash position at 31 March 2021 is included in the financing activities in the Cash Flow Statement.

Other areas of focus

Expenditure recognition

Risk identified and key judgements

In accordance with Practice Note 10 (*Audit of annual accounts of public sector bodies in the United Kingdom*), in addition to the presumed risk of fraud in revenue recognition set out in ISA (UK) 240, as discussed further on page 13, auditors of public sector bodies should also consider the risk of fraud and error on expenditure. This is on the basis that most public bodies are net spending bodies, therefore the risk of material misstatement due to fraud related expenditure may be greater than the risk of material misstatement due to fraud related to revenue recognition.

We have considered this risk for the Council and concluded that we are satisfied that the control environment is strong and there is no history of errors or audit adjustments. This has therefore not been assessed as a significant risk area, but will continue to be an area of audit focus in line with Practice Note 10.

Deloitte response and challenge

We will perform the following procedures to address the risk:

- detailed analytical procedures on all invoices processed in the year to assess the risk of a material misstatement; and
- testing of creditors balances at the year-end to assess completeness of expenditure.

Other areas of focus (continued)

Pension liability

Risk identified and key judgements

The Council participates in two defined benefits schemes:

- Scottish Teachers' Superannuation Scheme, administered by the Scottish Government; and
- the Shetland Islands Council Pension Fund, administered locally by Shetland Islands Council.

The net pension liability has decreased from £209.9m in 2018/19 to £171.9m in 2019/20. The decrease is as a result in changes in assumptions, specifically driven by reduced inflation assumptions, resulting in a reduction in the value of pension liabilities, partly offset by a reduction in the return on Scheme assets, resulting in the change in the value of the pension assets. The liability also continues to be affected by the McCloud and Goodwin legal cases.

Hymans Robertson LLP are the Council's appointed actuary, who produce a detailed report outlining the estimated liability at the year-end along with the associated disclosure requirements.

The pension liability valuation is an area of audit focus due to the material value and significant assumptions used in the calculation of the liability. The valuations are prepared by a reputable actuary using standard methodologies which have been considered as appropriate in previous years and no significant changes in the membership of the scheme or accrued benefits are expected in the current year. As a result, we have not identified this as a significant risk.

Deloitte response and challenge

We will perform the following procedures to address the risk:

- assess the independence and expertise of the actuary supporting the basis of reliance upon their work;
- review and challenge the assumptions made by Hymans Robertson;
- obtain assurance from the auditor of the pension fund over the controls for providing accurate data to the actuary;
- consider the impact of the Triennial Review of the pension fund;
- assess the reasonableness of the Council's share of the total assets of the scheme with the Pension Fund annual accounts;
- review and challenge the calculation of the impact of the McCloud and Goodwin cases on pension liabilities; and
- review the disclosures within the accounts against the Code of Audit Practice.

Coronavirus (COVID-19) outbreak

Impact on our audit

Requirements	The COVID-19 pandemic had a significant impact on the 2019/20 audit process, despite impacting relatively late in the year. We would expect there to be guidance as we approach year-end on accounting and disclosure requirements for 2020/21, where the impact has been much more extensive on all organisations. A key element of this will be communicating risks and governance impacts in narrative reporting, consistent with the Financial Reporting Council's guidance to organisations on the importance of communicating the impact of COVID-19 and related uncertainties, including their impact on resilience and going concern assessments. Entity-specific explanations of the current and expected effects of COVID-19 and the Council's plans to mitigate those effects should be included in the narrative reporting (including where relevant the Annual Governance Statement), including in the discussion on Key Risks and Uncertainties impacting an organisation.
Actions	While there may be greater clarity as we approach year-end, we would expect as part of the Council's reporting within the 'Key Risks and Uncertainties' section of the annual accounts, that a thorough assessment of the current and potential future effects of the COVID-19 pandemic is performed, including: • Consideration of the impact across the Council's operations, including on its income streams, supply chains and cost base, and the consequent impacts on financial position; • The scenarios assumed in making forecasts and on the sensitivities arising should other potential scenarios materialise (including different funding scenarios); and • The effect of events after the reporting date, including the nature of non-adjusting events and an estimate of their financial effect, where possible.

Coronavirus (COVID-19) outbreak (continued)

Impact on our audit (continued)

Impact on the Council and management actions	Impact on annual accounts	Impact on our audit
We will consider the key impacts on the Council such as: • Interruptions to service provision • Supply chain disruptions • Unavailability of personnel • Reductions in service income	We have considered the impact of the outbreak on the annual report and annual accounts, discussed further on the next slide including: • Narrative reporting, including disclosures on financial sustainability • Principal risk disclosures • Impact on property, plant and equipment valuations • Impairment of non-current assets • Allowance for expected credit losses • Events after the reporting period and relevant disclosure	We will continue to assess the impact on the audit including: • Resource planning • Timetable of the audit • Impact on our risk assessment • Logistics including meetings with entity personnel

	Impact on annual accounts
Impact on Property, Plant and Equipment	The Royal Institute of Chartered Surveyors issued a practice alert, as a result of which valuers identified a material valuation uncertainty at 31 March 2020 for most types of property valuation. This practice alert was withdrawn in September 2020. Valuation reports at March 2020 typically identified a need to consider potential impairments in future periods, and this year's valuations may reflect more significant movements. The Council will need to consider the approach to its valuation (including any changes as a result of the pandemic and consequent service and organisational changes on the "modern equivalent asset" assumed in valuations). The Council will also need to consider whether there are any indications of impairment of assets requiring adjustment at 31 March 2021.

Coronavirus (COVID-19) outbreak (continued)

Impact on our audit (continued)

Impact on annual accounts	
Expected credit losses	While most debtors are with public sector entities (where significant changes in recoverability are not expected), for non-public sector debtors, the Council will need to consider the level of provision required for expected credit losses under IFRS 9.
Narrative and other reporting issues	The following areas will need to be considered by the Council: • Narrative reporting as well as the usual reporting requirements will need to cover the effects of the pandemic on services, operations, performance, strategic direction, resources and financial sustainability. • Reporting judgements and estimation uncertainty, the Council will need to report the impact on material transactions including decisions made on the measurements of assets and liabilities.
Going concern assessment	The annual accounts should include disclosure on the basis of the Council's going concern assessment, including related uncertainties. The Council also needs to report on the impact of financial pressures and its financial sustainability in the narrative report, as well as any relevant liquidity reporting requirements under IFRS 7 Financial Instruments: Disclosures.
Events after the reporting period and relevant disclosures	Events are likely to continue to move swiftly, and the Council will need to consider the events after the reporting period and whether these events will be adjusting or non-adjusting and make decisions on a transaction by transaction basis.

Reporting hot topics

Increased focus on quality reporting

Deloitte view

The expectations of corporate reporting, reflected in the Financial Reporting Council's ('the FRC') monitoring and enforcement priorities, are increasing. While the focus is primarily on corporate entities, we highlight these areas where improved disclosures would help meet stakeholder expectations.

The potential impacts of Brexit

Depending upon events, organisations may be preparing annual reports against the backdrop of continued uncertainty around the UK's future relationship with the EU. Even with a deal, the future basis of UK-EU trade will affect the longer-term viability period of 3-5 years and a longer consideration of prospects.

ACTION: Depending upon events through to the date of signing, we would expect to see annual reports reflecting at least:

- relevant risks and uncertainties, and actions taken to manage those risks; and
- consideration of whether there is any impact on critical accounting judgements and areas of estimation uncertainty.

We will discuss with the Council closer to the time areas where disclosures may be appropriate.

Climate-related risks

The report by the Intergovernmental Panel on Climate Change (IPCC) has made it clear that prompt and decisive action on climate change is required from governments, businesses and individuals alike.

The recommendations of the Taskforce on Climate-related Financial Disclosure (TCFD) are gaining momentum. The government has proposed mandatory TCFD disclosures by 2022, and the FRC is undertaking a major review of how organisations assess and report the impact of climate change. The FRC expects organisations to disclose how they have taken climate change into account in assessing the resilience of the business model, its risks, uncertainties and viability both in immediate and longer term.

Investors are challenging companies that are not factoring the effects of the Paris Climate Agreement into their critical accounting judgements and are not disclosing comprehensively these judgements, assumptions, sensitivities and uncertainties.

ACTION: Clearly articulate how your organisation is addressing climate change e.g.

- whether this is a principal risk and how it is being managed; and
- its impact on the business model, the viability statement and the key assumptions and projections in impairment reviews and valuations (including in assessing remaining asset lives).

Revisions to auditing standards coming into effect

ISA (UK) 570 – Going concern

The FRC issued a revised going concern standard in September 2019, that takes effect for periods commencing on or after 15 December 2019. For public sector bodies, this will be March 2021 year ends and later.

The revision was made in response to recent enforcement cases and well-publicised corporate failures where the auditor's report failed to highlight concerns about the prospects of entities which collapsed shortly after.

We have summarised below the key areas of change in the standard – however, the Public Audit Forum is also consulting on changes to Practice Note 10, with the intention of reflecting public sector considerations in the approach to going concern, and so the ultimate impact of ISA (UK) 570 changes will be affected by this.

The key changes affect:

- Risk assessment procedures and related activities, increasing consideration of the entity's business model, operations and financing;
- The auditor's evaluation of management's assessment of the going concern assumption (which therefore requires a clearly documented assessment to be prepared by management);
- Enhanced professional scepticism requirements, including around the evaluation of the sufficiency and appropriateness of audit evidence;
- Considering the appropriateness of disclosures; and
- Reporting in enhanced audit reports.

"The revised standard means UK auditors will follow significantly stronger requirements than those required by current international standards."

FRC's press release, 30 September 2019

Revisions to auditing standards coming into effect (continued)

ISA (UK) 540 – Auditing Accounting Estimates and Related Disclosures

Since 2015, the International Auditing and Assurance Standards Board (IAASB) has sought to identify audit issues relating to accounting estimates for financial institutions and other entities. Initially, this focused on the impact of IFRS 9 *Financial Instruments*, because it would fundamentally change the way that banks and other entities account for loan assets and other credit exposures.

However, the IAASB concluded that most, if not all, issues identified for expected credit losses would be equally relevant when auditing other complex accounting estimates. Accordingly, a holistic revision of ISA 540 was undertaken and the new standard takes effect for periods commencing on or after 1 January 2020. For public sector bodies, this will be March 2021 year ends and later.

We summarise on the next few slides how this will impact our audit.

"There is a clear need to update ISA 540 to support better quality audits of increasingly complex accounting estimates"

FRC letter to the IAASB, July 2017

Area of change	Impact on our audit	Impact on the Council
Assessment of oversight and governance relating to estimates	In connection with our planning work to understand the entity and its environment, including internal control, we will specifically enquire regarding management's processes, and the oversight and governance of those processes relating to accounting estimates.	You will need to consider the adequacy of your processes and controls over estimates, and documentation thereof.

Revisions to auditing standards coming into effect (continued)

ISA (UK) 540 – Auditing Accounting Estimates and Related Disclosures (continued)

Area of change	Impact on our audit	Impact on the Council
Identification of inherent risk factors; separate assessment of inherent risk and control risk	Recognising a spectrum of inherent risk, we will assess risks of material misstatement in estimates with reference not only to estimation uncertainty, but also complexity, subjectivity or other inherent risk factors, and the interrelationship among them.	You will need to provide clear documented rationale for (a) the selection and application of the method, assumptions and data in making the accounting estimate, including any changes in the current year, and controls relating to those aspects; and/or (b) the selection of a point estimate and related disclosures for inclusion in the annual accounts.
Objectives-based work effort requirements	We will specifically assess control risk relating to estimates, which may require us to evaluate the design and determine implementation of an increased number of internal controls. Our subsequent audit procedures will be responsive to this assessment, and designed to obtain evidence around the methods, significant assumptions, data and (where applicable) the selection of a point estimate and related disclosures about estimation uncertainty.	
Enhanced "stand back" requirement, to evaluate the audit evidence obtained	We will specifically design our procedures, to enhance our application of professional scepticism, so that they are not biased towards finding corroborative evidence; our overall evaluation of the evidence obtained will weigh both corroborative and contradictory evidence.	You should expect more challenge of the evidence provided in support of accounting estimates, use of external data sources and your consideration of contradictory evidence.

Revisions to auditing standards coming into effect (continued)

ISA (UK) 540 – Auditing Accounting Estimates and Related Disclosures (continued)

Area of change	Impact on our audit	Impact on the Council
Enhanced requirements about whether disclosures are “reasonable”	The extant ISA 540 required us to evaluate whether disclosures were “adequate”. The change to “reasonable” will involve greater consideration of the overall meaning conveyed through disclosures. For example, where estimation uncertainty associated with an estimate is multiple times materiality, we will consider whether the disclosures appropriately convey the high degree of estimation uncertainty and the range of possible outcomes.	You should expect more challenge on disclosures relating to estimates, particularly for where you have selected a point estimate from a range and those with high estimation uncertainty.
New requirements when communicating with those charged with governance	In accordance with ISA (UK) 260 and ISA (UK) 265, our communications from the audit have included significant qualitative aspects of your accounting practices and significant deficiencies in internal control. With the revised ISA (UK) 540, these communications will specifically include matters regarding accounting estimates and take into account whether the reasons for our risk assessment relate to estimation uncertainty, or the effects of complexity, subjectivity or other inherent risk factors.	You should expect increased reporting in relation to accounting estimates which may be mirrored in our Annual Audit Report.

Areas where we consider the impact to be greatest:

Key areas impacted will include valuation of property assets, provisions, pension liability (as discussed at page 16), investments and fishing quota.

- The property valuations are based on valuation reports provided by the internal valuer in line with instructions from management. We expect to receive reports setting out the basis for the valuations assumptions and we have already held discussion with the valuer around valuation methodologies.
- Investments are managed by external fund managers, with valuation of investments provided by them independently. We will consult with financial instrument specialists to review the assumptions and valuations performed by the fund managers.
- The fishing quota valuation is completed by an external expert. We will assess the objectivity and competence of management’s expert and will develop an independent estimate of the value based on information obtained from the active market in the year.

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 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 investments and pension specialists to support the audit team in our work investments and the pension fund liability.

In order to deliver a quality audit to you, each member of the core audit team has received tailored learning to develop their expertise in audit skills, delivered by Pat Kenny (Audit Director) 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.

Wider scope requirements

Overview

The Code of Audit Practice sets out four **audit dimensions** that frame the wider scope of the audit of the accounts. The audit dimensions provide a common framework for all the audit work conducted for the Auditor General and for the Accounts Commission.

In addition, the wider scope of audit in local government comprises the statutory duty of auditors to be satisfied that bodies have made proper arrangements to secure **Best Value (BV)** and to publish **statutory performance information**. The Commission also sets out five **Strategic Audit Priorities** that it expects auditors to consider in local government audits.

In carrying out our annual risk assessment, we have considered the arrangements in place, building on our findings and conclusions from previous years' audits as well as planning guidance published by Audit Scotland. The following pages summarise the significant risks identified and our planned audit response.

The risk profile of public bodies for the 2020/21 audits is significantly affected by the COVID-19 pandemic. The pandemic has highlighted the importance of many long-standing issues that auditors across the public sector have previously reported on, such as the need for good governance, openness and transparency and effective longer-term planning to deliver better outcomes. The risks and challenges associated with these issues have become greater due to the pandemic. Audit Scotland's COVID-19 Guide for Audit and Risk Committees https://www.audit-scotland.gov.uk/uploads/docs/report/2020/as_200825_covid19_guide_audit_risk_comm.pdf sets out the key short term risks and challenges facing public bodies. They are heightened further because of the uncertainty around the UK's exit from the European Union and increasing budget pressures.

In accordance with Audit Scotland planning guidance, in assessing risks in 2020/21, and in order to deliver a high quality audit, we have focussed on risks related to governance and transparency, financial sustainability, and counter-fraud arrangements.

Wider scope requirements (continued)

Audit dimensions

Audit dimension	Significant risks identified	Planned audit response
Financial sustainability	The Council continues to draw an unsustainable amount from reserves. While it has a healthy level of reserves, it remains in a financially unsustainable position, forecasting a cumulative funding gap of £103.6m by 2025/26. There is the risk that plans in place at the Council are not sufficiently robust to address the funding gap in the medium-term. The Council approved a Workforce Plan in December 2020. Following our conclusion in the 2019/20 audit, there is a risk that the Workforce Plan is not sufficiently detailed or supported by supplementary plans to ensure that the Council can address the funding gap, transformation requirements and workforce issues, particularly in light of additional pressures due to COVID-19 and EU withdrawal.	We will assess the robustness of the Council's transformation plans and the revised Medium-Term Financial Plan ('MTFP') published by the Council. In addition to this, we will assess and review the Workforce Plan to assess whether the plan is achievable and supported by effective delivery plans.

Wider scope requirements (continued)
Audit dimensions

Audit dimension	Significant risks identified	Planned audit response
Financial management	We have not identified any significant risks in relation to financial management during our planning. Since the start of the pandemic, the risk of fraud and error has increased as the control environment and internal control change. In accordance with Audit Scotland planning guidance, we will consider fraud as a particular focus area in 2020/21.	We will continue to review the financial management arrangements. Using Audit Scotland's publication "COVID-19 Emerging Fraud Risks", we will assess what action the Council has taken to minimise risk to its control environment and internal controls.

Wider scope requirements (continued)

Audit dimensions (continued)

Audit dimension	Significant risks identified	Planned audit response
Governance and transparency	In response to the pandemic, changes were made to the governance arrangements, including the use of teleconferencing for meetings. There is a risk that revised arrangements are not appropriate or operating effectively. While risk management processes continue to be in place, the likelihood and impact of existing risks and the emergence of new risks will need to be monitored carefully. There is a risk that officers and Committee members have not considered how sustainable any changes to the risk appetite will be in the longer term. There have been a number of resignations and referrals to the Standards Commission in the year from Council committees, with vacancies becoming increasingly difficult to fill. These issues create a risk that the Council committees do not have necessary resources to discharge their responsibilities and achieve their stated objectives. They also present a risk to the sustainability of the governance framework and highlight risks around the support and training provided to Members. The governance arrangements for health and social care integration is an area of particular interest to the Accounts Commission. There is a risk that the arrangements are not operating effectively (including services delivered by, or in partnership with, others). The Council is currently non-compliant with its responsibilities under the IJB's governing legislation and needs to address this as a priority.	We will review the work of the Council and its committees to assess whether the arrangements are operating effectively, including assessing whether there is effective scrutiny, challenge and informed decision making. We will also review progress made in addressing vacancies within committees. We will review the work undertaken in relation to risk management including updates to the policies in place as a result of COVID-19 and whether these are appropriate for the long-term, while also reviewing the work the Council is doing to address the risk of the ongoing operational changes due to the pandemic. We will review the progress made and work undertaken in the revision of the integration scheme.

Wider scope requirements (continued)

Audit dimensions (continued)

Audit dimension	Significant risks identified	Planned audit response
Value for money	The pandemic is expected to have had a substantial impact on performance measures, particularly for services which have been temporarily suspended, are being provided at a reduced level or have had to adapt to new ways of working. The pandemic has had a significant impact on the Council's operations. As at June 2020, the pandemic had resulted in £7.475m of Coronavirus Business Support Funds being awarded. In addition, £44k of newly self employed funding was awarded, an upsurge in social care delivered to meet the needs of adults with learning disabilities and autism, as well as the administration of childcare settings being provided to children within key worker families. There is a risk that performance reporting has not been timely, reliable, balanced, transparent and appropriate to users needs. This risk is heightened by the revisions made to the Performance Management Framework in 2019/20 and to the ongoing review and anticipated changes to the Business Transformation and Service Redesign programmes.	We will review the performance reports presented at the Council to assess the extent of openness and transparency during the year. We will review the progress made in relation to the ongoing changes to the Business Transformation and Service Redesign programmes. We will review progress made to assess and address any underlying concerns identified in relation to the pace of progress made.

Wider scope requirements (continued)

Best value and Strategic Audit Priorities

Considering Best Value arrangements

We have a duty to be satisfied that local government bodies have made proper arrangements for securing BV.

2020/21 is year five of the extended six-year approach to auditing BV in councils. BV audit work is integrated with the annual audit and we will work closely with Audit Scotland's Performance Audit and Best Value (PABV) team to plan, perform and report on the BV audit work.

A key feature of the approach to auditing BV is the Controller of Audit providing a Best Value Assurance Report (BVAR) to the Accounts Commission for each Council once over the audit appointment.

Shetland Islands Council is not scheduled to be reported on in 2020/21. Our BV audit work will be integrated into our audit approach, including our work on the audit dimensions discussed on pages 27 to 30.

Strategic Audit Priorities

In its 2019-24 strategy, the Accounts Commission sets out five Strategic Audit Priorities (SAPs):

- Having clear priorities with a focus on outcomes, supported by effective leadership and long-term planning;
- The strategic appraisal of options to re-shape services in line with priorities. This should consider good practice, innovation and collaborative working with partners;
- 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 deliver of local services and planning for their local area; and
- Reporting councils' performance in a way that enhances accountability to citizens and communities, helping them contribute better to the delivery of improved outcomes.

In recognition of the demands on auditors' time and the challenges of remote auditing, the Commission has agreed that auditors are not required to specifically consider and report on the SAPs as part of the 2020/21 audit. The SAPs continue to be important but the work on the audit dimensions will be used to inform progress.

Wider scope requirements (continued)

Statutory Performance Information

Statutory Performance Information

The Accounts Commission has a statutory responsibility to define the performance information that councils must publish. 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 Accounts Commission issued a revised **2018 Statutory Performance Information Direction** in December 2018 which requires a council to report on:

- Performance in improving local public services provided by the Council (on its own and with its partners and communities), and progress against agreed desired outcomes;
- Its own assessment and independent audit assessments of how it is performing against its duty of BV, and how it plans to improve these assessments; and
- How it (with its partners where appropriate) has engaged with and responded to its diverse communities.

As 2019/20 was the first year of the direction, we evaluated the effectiveness and appropriateness of the arrangements at the Council to fulfil the above requirements and concluded that "*the Council has robust and long-standing arrangements in place to comply with the new SPI Direction including its public performance reporting requirements*". As noted on pages 17 to 19 , the COVID-19 pandemic is expected to have had a substantial impact on performance reporting. We will therefore consider the effectiveness and appropriateness of the current arrangements as part of our audit dimensions work.

Wider scope requirements (continued)

Other requirements

Contributing to performance audits	Shared Risk Assessment and Joint Scrutiny Planning
As in previous years, the Accounts Commission will publish two overview reports (financial and performance) covering the local government sector. The reports use information from the audited accounts and Annual Audit Reports. However, we will also be requested to provide important supplementary information collected as a dataset. The local government dataset is expected to be available in March 2021, with a submission deadline of 8 May 2021.	We continue to play a key role in the Shared Risk Assessment (SRA) process which is the vehicle for scrutiny bodies to share intelligence and agree scrutiny risks at each council. As the local auditor, we lead the Local Area Network (LAN), which comprises representatives from the main local government scrutiny bodies. The COVID-19 pandemic has impacted on the work of all local government scrutiny during 2020 and will continue to affect plans going forward. As a result, a National Scrutiny Plan for 2020 has not been published. The Strategic Scrutiny Group is considering how scrutiny partners can best respond in a co-ordinated way to the challenges and changes brought about by COVID-19. We will provide management with any updates as this develops.

Current issues returns	Other areas
Timely communication by auditors of intelligence is important in helping Audit Scotland to maintain a good level of awareness across the public sector and to keep the Auditor General, the Controller of Audit and Accounts Commission informed. Current Issue Returns for local government represent an important source of intelligence for reporting to the Commission's Financial Audit and Assurance Committee.	We are required to also carry out the following areas of work: • Assurance on approved grant claims and other financial returns • Assurance on WGA returns • Preliminary enquiries on all correspondence received • Consider and report on any statutory objections received • Submission of fraud returns

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 annual accounts 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 annual accounts and the other procedures performed in fulfilling our audit plan.

Use of this report

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

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

Other relevant communications

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

P. Kenny

Pat Kenny

for and on behalf of Deloitte LLP

Glasgow | 12 February 2021

Technical update

What does climate change mean for business?

New website – learning, interviews and resources

Climate change is likely to drive some of the most profound changes to businesses in our lifetimes.

Impacts on products and services, supply chains, loss of asset values and market dislocation are already being caused by more frequent and severe climate-related events.

Discover how to think through the challenges and futureproof your business.

The time to act is now!

Visit: www.deloitte.co.uk/climatechange

Changes to the Code of Practice on Local Authority Accounting
2020/21

Background

The accounting code has been issued by the CIPFA/ LASAAC Local Authority Code Board and its financial reporting framework is based on International Financial Reporting Standards (IFRS) as adopted by the European Union, adapted for the local government context where necessary.

The 2020/21 accounting code has been prepared on the basis of accounting standards and other pronouncements in effect for accounting periods commencing on or before 1 January 2020 (except for IFRS 16 Leases discussed on page 43).

The changes in the 2020/21 accounting code are summarised in the Foreword. The most significant changes impacting the Council are:

- ***The total line in the Comprehensive Income and Expenditure Statement –*** the line description used now needs to provide clarity regarding the use of positive and negative signage. For example, where brackets are used to represent an overall surplus the description "Total comprehensive (income) and expenditure" may be used.

- ***Amendments to reflect changes to the definition of material in IAS 8*** – it now states that information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that users make on the basis of those annual accounts.

- ***The implementation of amendments to IAS 19 Employee Benefits*** – it creates an exception to the rule that financial assumptions are based on market expectations at 31 March. Where a pension scheme amendment, curtailment or settlement occurs during the year the amended assumptions, as used for the re-measurement of the net defined benefit liability, are to be applied in relation to the benefits for the remainder of the year.

Changes to the Code of Practice on Local Authority Accounting
2020/21 (continued)

Background (continued)

- ***Amendments relating to financial instruments*** – as summarised below*:*

    - Gains and losses on financial instruments classified as fair value through the profit or loss have been added to the items included in the financing and investment income and expenditure line of the Comprehensive Income and Expenditure Statement.
    - Clarification has been added regarding the extent of the exemption from recognising a loss allowance for expected credit losses on a financial asset where the counterparty is central government. It has been clarified that the exemption does not apply to credit impaired assets or NDPBs unless explicitly covered by a guarantee given by their sponsor division.
    - Clarification has been added in respect of the application of the interpretation of IFRS 9 that the options that characterise clauses within a LOBO contract should not be separately accounted for. It has been clarified that this interpretation only applies where the specific derivative elements are separable. It does not apply to a compound embedded derivative if separation of the exempted derivative is not permitted by IFRS 9.
    - Clarification has been added that the modification of financial liabilities follows the principles specified for the modification of financial assets, i.e. when the change in terms is not substantial, it is not accounted for as an extinguishment.
    - The wording of the definition for a soft loan has been amended to include loans where the interest rate specified at below zero (i.e. negative interest).

- ***Amendments to accounting and reporting by pension funds*** – the disclosure requirement for pooled investment vehicles in the net assets statement has been amended to require an analysis between equities, bonds, property, hedge funds, diversified growth funds, private equity funds, infrastructure funds and others. Also, the previous requirement for an analysis of investment assets between 'UK' and 'overseas' and between 'quoted' and 'unquoted' has been removed.

Next steps

We recommend that management review the changes to the accounting code at the earliest opportunity. We are happy to have early discussion on this to agree and apply the required changes.

The State of the State 2020-21

Government in the pandemic and beyond

Background and overview

Now in its ninth year, this report brings together Deloitte and Reform to reflect on new research into the issues facing government and public sector across the UK. This year, that research focuses on the impact of the coronavirus pandemic both on the public sector and the public it services. It comes as all nations of the UK faces new lockdown measures designed to reduce transmission, manage demand on health services and ultimately saving lives.

At the heart of the report is our exclusive citizen survey, which offers insight into perceptions of public services and public spending beyond COVID-19, as well as a public perspective on the government's 'levelling up' agenda.

That survey is complemented by our interviews with public sector leaders. This year, we spoke to 40 senior figures in government and public services, producing the most extensive qualitative research of its kind.

Next steps

A summary of the key conclusions are provided on the next page. The full report is available at https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/public-sector/deloitte-uk-state-of-the-state-2020.pdf

The State of the State 2020-21 (continued)

Government in the pandemic and beyond (continued)

The state according to the public

A survey of more than 5,000 members of the public shows how people feel about tax, spending and public service priorities amid the COVID-19 pandemic. We also explore attitudes towards data sharing with and across government, and unpick what the public across each nation and region wants to see levelled up

58% of the public believe opportunities for young people will be worse as a result of coronavirus.

42% of the public believe that community spirit will have improved after the pandemic

The state according to the people who run it

Over 40 senior public sector figures in England, Scotland, Wales and Northern Ireland talked with us about the issues that matter to them. We explore their views on the legacy of COVID-19, levelling up, EU Exit and creating a data-driven government.

Our interviews of **40** senior public sector figures found that many want to retain the agility of new ways of working however, many sense a gravitational pull back to normality.

Fast forward to the past

Is automation making organisations less diverse?

Background and overview

Robotics and intelligent automation are in the process of transforming the nature of work and the skills required to do it. Whilst there is a clear risk of reinforcing structural inequalities there is also an opportunity to address diversity issues within automation programmes to ensure public sector organisations can capitalise on the benefits that both automation and diversity bring to business outcomes.

For many public sector organisations implementing automation whist considering diversity is new and unchartered territory. We would like to encourage our public sector clients to consider and discuss this crucial issue.

Based on exclusive client interviews, insight from public sector projects and extensive desk research, our report explores the potential risks of not considering the implications of automation on workforce diversity and inequality. It also identifies the barriers to embedding diversity in automation programmes.

The report provides a practical four stage framework to integrate diverse groups to not only survive but thrive in a new automated and digital world.

Next steps

The full report is available at https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/public-sector/deloitte-uk-diversity-and-automation-brochure-landscape.pdf

The future unmasked

Predicting the future of healthcare and life science in 2025

Background and overview

What does the future hold for the life sciences and healthcare industry? Our latest predictions report looks ahead to the year 2025 to help you see what's coming and to keep your organisation moving forward.

Each prediction is brought to life through snapshots of how patients, healthcare and life science companies and their staff might behave and operate in this new world. We explore the major trends and the key constraints to be overcome; and identify the evidence today to predict how near that future might be.

This year, inevitably, our predictions have been informed by the unparalleled impact of the COVID-19 pandemic on society in general and more specifically on how people perceive health risks. We have seen a new public appreciation of the contribution that healthcare and life sciences companies are making to each countries response and how these companies are paving the way for a new era of collaboration to identify and implement solutions. A key stand out has been the huge acceleration in the pace and scale of technology-enabled transformation across the whole health ecosystem.

Next steps

Explore the individual predictions or download the full series below to learn more **https://www2.deloitte.com/uk/en/pages/life-sciences-and-healthcare/articles/life-sciences-and-health-care-predictions.html**

Changes to accounting standards

IFRS 16 - Leases

Background

The implementation of the new standard has been deferred again for another year, with a revised implementation date of 2022/23 and will require adjustments to recognise on balance sheet arrangements currently treated as operating leases.

For 2021/22, the Council will need to include disclosures on the expected impact of the standard, but not make any adjustments in the financial statements in respect of IFRS 16. However, many organisations have identified previously unidentified leases (or arrangements that contain a lease, such as service contracts) as part of their transition project, and so there may be some 2021/22 impact.

CIPFA/ LASAAC will shortly be issuing for consultation proposals on how housing secure tenancy agreements should be treated under IFRS 16. The proposals in this consultation are expected in the 2022/23 accounting code.

In the local government context relatively small effects from standards can have a significant impact against performance metrics and targets, and so it is important to clearly understand the impact of the standards.

While the deferral of implementation means there is no direct impact on the 2020/21 annual accounts, finance teams should use this additional time to continue their preparation for implementation.

Next steps

We recommend that the Audit Committee review the impact of IFRS 16, including calculating any adjustments that will be required as at 31 March 2022 for transition. We would suggest that the Audit Committee receive reporting from management on the implementation of the new standard, and we will report specifically on the findings from our audit work in this area.

Appendices

Prior year audit adjustments

Uncorrected misstatements

The following uncorrected misstatements were identified during the course of our prior year audit:

		Debit/ (credit) CIES £m	Debit/ (credit) MIRS £m	Debit/ (credit) in net assets £m	Debit/ (credit) reserves £m
Pension Liability – McCloud current service costs	(1)	0.303	(0.303)	(0.303)	0.303
Total		**0.303**	**(0.303)**	**(0.303)**	**0.303**

(1) Due to the McCloud judgement - which resulted in transitional pension arrangements due to government changes being ruled unlawful - and the subsequent consultation by the SPPA, the pension liability required to be adjusted to account for the judgement. The adjustment by the actuary did not include an adjustment for the current service cost impact.

We obtained written representations from the Council of confirming that after considering all these uncorrected items, both individually and in aggregate, in the context of the consolidated annual accounts taken as a whole, no adjustments were required.

Our other responsibilities explained

Fraud responsibilities

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 annual accounts as a whole are free from material misstatement, whether caused by fraud or error.
- As set out in the significant risks section of this document, we have identified risks of material misstatement due to fraud in relation to recognition of grant income, and management override of controls.
- We will explain in our audit report how we considered the audit capable of detecting irregularities, including fraud. In doing so, we will describe the procedures we performed in understanding the legal and regulatory framework and assessing compliance with relevant laws and regulations.

Whilst this requirement has been in place for a few years for public interest entities (as defined by the EU Audit Regulation), recent changes to ISAs (UK) mean it will apply to **all** entities for periods **commencing on or after 15 December 2019.**

Fraud Characteristics:

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

Our other responsibilities explained (continued)

Fraud responsibilities (continued)

We will make the following inquiries regarding fraud and non-compliance with laws and regulations:

Management:

- Management's assessment of the risk that the annual accounts may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Management's process for identifying and responding to risks of fraud.
- Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud.
- 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.
- We plan to involve management from outside the finance function in our inquiries, including Maggie Sandison (CEO) and Jan Riise (Executive Manager – Governance & Law).

Internal audit

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

Those charged with governance

- How those charged with governance exercise oversight of 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 Committee for the year ending 31 March 2021 in our final report to the Audit Committee.

Fees

The proposed audit fee for 2020/21, which is 5% below the expected fee range proposed by Audit Scotland, is £212,553 as analysed below:

	£
Auditor remuneration	140,373
Audit Scotland fixed charges:	
Pooled costs	14,010
Performance Audit and Best Value	50,070
Audit support costs	8,100
Total proposed audit fee	**212,553**

In addition, the total proposed audit fee for the charitable trust audit is £400.

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 company'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

Audit quality remains our number one priority and we have a relentless commitment to it. We continue to invest in and enhance our Audit Quality Monitoring and Measuring programme.

In July 2020 the Financial Reporting Council (“FRC”) issued individual reports on each of the seven largest firms, including Deloitte, on Audit Quality Inspections providing a summary of the findings of its Audit Quality Review (“AQR”) team for the 2019/20 cycle of reviews.

We greatly value the FRC reviews of our audit engagements and firm wide quality control systems, a key aspect of evaluating our audit quality.

We are pleased with our results for the inspections of FTSE 350 entities achieving 90% assessed as good or needing limited improvement, which included some of our highest risk audits. Our objective is for 100% of our audits to be assessed as good or needing limited improvement and we know we still have work to do in order to meet this standard. We are however, extremely disappointed one engagement received a rating of significant improvements required during the period. This is viewed very seriously within Deloitte and we have worked with the AQR to agree a comprehensive set of swift and significant firm wide actions.

We are also pleased to see the impact of our previous actions on prior year adjustments is reflected in the results of current year inspections with no findings in this areas. In addition the FRC identified good practice examples including in: risk assessment, group oversight, our comprehensive IFRS9 expected credit loss audit programme and our audit committee reporting.

Embedding a culture of challenge in our audit practice underpins the key pillars of our audit strategy. We invest continually in our firm wide processes and controls, which we seek to develop globally, to underpin consistency in delivering high quality audits whilst ensuring engagement teams exercise professional scepticism through robust challenge.

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

Our approach to quality (continued)

AQR team report and findings (continued)

The AQR's 2019/20 Audit Quality Inspection Report on Deloitte LLP

"We reviewed 17 individual audits this year and assessed 13 (76%) as requiring no more than limited improvements. Of the ten FTSE 350 audits we reviewed this year, we assessed nine (90%) as achieving this standard."

"We have highlighted in this report aspects of firm-wide procedures which should be improved, including strengthening the monitoring of the firm's audit quality initiatives."

"Our key findings related principally to the need to:

- Improve the extent of challenge over cash flow forecasts in relation to the impairment of goodwill and other assets.
- Enhance the effectiveness of substantive analytical review and other testing for revenue.
- Improve the assessment and extent of challenge regarding management's estimates, particularly for model testing."

"The firm has taken steps to address the key findings in our 2019 public reports, with actions that included focused training and standardising the firm's audit work programs. We have identified improvements, for example in the audit of potential prior year adjustments and related disclosures, a key finding last year. We also identified good practice in a number of areas of the audits we reviewed (including effective group oversight and robust risk assessment) and in the firm-wide procedures (including the firm's milestone program, with expected dates for the phasing of the audit monitored by the firm)."