External Audit Plan 2017/2018

Nottingham City Council

—

Updated in May 2018

Summary for Audit Committee

Financial statements

There are no significant changes to the Code of Practice on Local Authority Accounting ("the Code") in 2017/18, which provides stability in terms of the accounting standards the Authority need to comply with. Despite this, the deadline for the production and signing of the financial statements has been significantly advanced in comparison to year ended 31 March 2017. Whilst the Authority chose to advance its own accounts production timetable last year, further advances will be required this year in order to ensure that deadlines are met. As a result we have recognised a significant risk in relation to this matter.

In order to meet the revised deadlines it will be essential that the draft financial statements and all prepared by client documentation is available in line with agreed timetables. Where this is not achieved there is a significant likelihood that the audit report will not be issued by 31 July 2018.

Materiality

Materiality for planning purposes has been set at **£10.5 million**.

We are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' and this has been set at **£0.525 million**.

Significant risks

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error have been identified as:

- **Valuation of PPE** – Whilst the Authority operates a cyclical revaluation approach, the Code requires that all land and buildings be held at fair value. We will consider the way in which the Authority ensures that assets not subject to in-year revaluation are not materially misstated;
- **Pension Liabilities** – The valuation of the Authority's pension liability, as calculated by the Actuary, is dependent upon both the accuracy and completeness of the data provided and the assumptions adopted. We will review the processes in place to ensure accuracy of data provided to the Actuary and consider the assumptions used in determining the valuation; and
- **Faster Close** – As set out above, the timetable for the production of the financial statements has been significantly advanced with draft accounts having to be prepared by 31 May (2017: 30 June) and the final accounts signed by 31 July (2017: 30 September). There are a number of logistical challenges that will need to be managed, one of which is ensuring that any third parties (subsidiaries and subsidiary auditors) involved in the production of the accounts are aware of the revised deadlines. We will work with the Authority in advance of our audit to understand the steps being taken to meet these deadlines and the impact on our work.

(continued overleaf)

Summary for Audit Committee (cont.)

Financial Statements (cont.)

Other areas of audit focus

Those risks with less likelihood of giving rise to a material error but which are nevertheless worthy of additional audit focus have been identified as:

- Group Accounts including Robin Hood Energy Ltd;
- Implications of Tramlink's auditors' comments regarding its going concern;
- Broadmarsh development;
- Commercial property investment; and
- Proposed changes to Minimum Revenue Provision (MRP) policy.

See pages 3 to 12 for more details

Value for Money Arrangements work

Our risk assessment regarding your arrangements to secure value for money has identified the following VFM significant risk to date:

- **Delivery of Budgets** – As a result of reductions in central government funding, and other pressures increased such as demand for Adult Social Care Services, the Authority is having to make additional savings beyond those from prior years and subsequently is also pursuing income generation strategies to help deliver sustainable budgets going forward. We will consider the way in which the Authority identifies, approves, and monitors both savings plans and income generation projects and how budgets are monitored throughout the year. We will also consider the financial impact of the Authority's participation in the Nottingham Sustainability and Transformation Plan; and
- **Group governance** - The Authority has a relatively complex Group structure. In 2016/17 the Authority consolidated within its Group accounts six subsidiaries, two joint ventures and one trust fund. The Authority has recognised that as its Group structure evolves, then so must the overarching governance arrangements in place at the Authority to monitor and ensure that appropriate accountability of the respective subsidiaries and joint ventures are in place. We will consider the group governance arrangements the Authority has in place.

See pages 13 to 18 for more details

Logistics

Our team is:

- Tony Crawley– Director
- Thomas Tandy – Manager
- Arvinder Khela – Assistant manager

More details are in **Appendix 2**.

Our work will be completed in four phases from December to July and our key deliverables are this Audit Plan and a Report to Those Charged With Governance as outlined on **page 21**.

Our fee for the 2017/18 audit is £172,118 (£178,727 2016/2017) see **page 20**. These fees are in line with the scale fees published by PSAA.

Introduction

Background and Statutory responsibilities

This document supplements our Audit Fee Letter 2017/18 presented to you in April 2017, which also sets out details of our appointment by Public Sector Audit Appointments Ltd (PSAA).

Our statutory responsibilities and powers are set out in the Local Audit and Accountability Act 2014, the National Audit Office's Code of Audit Practice and the PSAA Statement of Responsibilities.

Our audit has two key objectives, requiring us to audit/review and report on your:

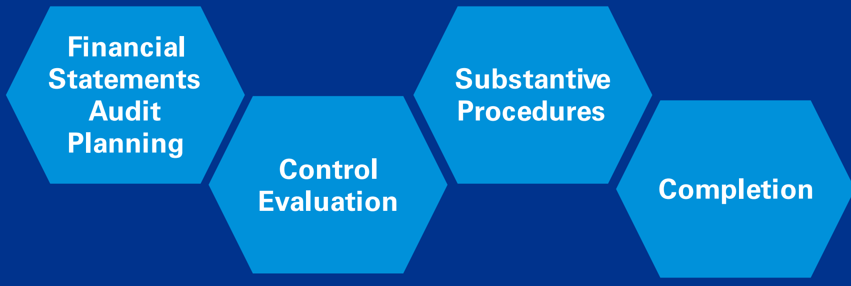
01 **Financial statements :**
Providing an opinion on your accounts. We also review the Annual Governance Statement and Narrative Report and report by exception on these; and

02 **Use of resources:**
Concluding on the arrangements in place for securing economy, efficiency and effectiveness in your use of resources (the value for money conclusion).

The audit planning process and risk assessment is an on-going process and the assessment and fees in this plan will be kept under review and updated if necessary. Any change to our identified risks will be reported to the Audit Committee.

Financial Statements Audit

Our financial statements audit work follows a four stage audit process which is identified below. Appendix 1 provides more detail on the activities that this includes. This report concentrates on the Financial Statements Audit Planning stage of the Financial Statements Audit.



Value for Money Arrangements Work

Our Value for Money (VFM) Arrangements Work follows a five stage process which is identified below. Page 13 provides more detail on the activities that this includes. This report concentrates on explaining the VFM approach for 2017/18 and the findings of our VFM risk assessment.

Financial statements audit planning

Financial Statements Audit Planning

Our planning work takes place during December 2017 to January 2018. This involves the following key aspects:

- Determining our materiality level;
- Risk assessment;
- Identification of significant risks;
- Consideration of potential fraud risks;
- Identification of key account balances in the financial statements and related assertions, estimates and disclosures;
- Consideration of management's use or experts; and
- Issuing this audit plan to communicate our audit strategy.

Risk assessment

Auditing standards require us to consider two standard risks for all organisations. We are not elaborating on these standard risks in this plan but consider them as a matter of course in our audit and will include any findings arising from our work in our ISA 260 Report.

01

Management override of controls

Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we carry out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.

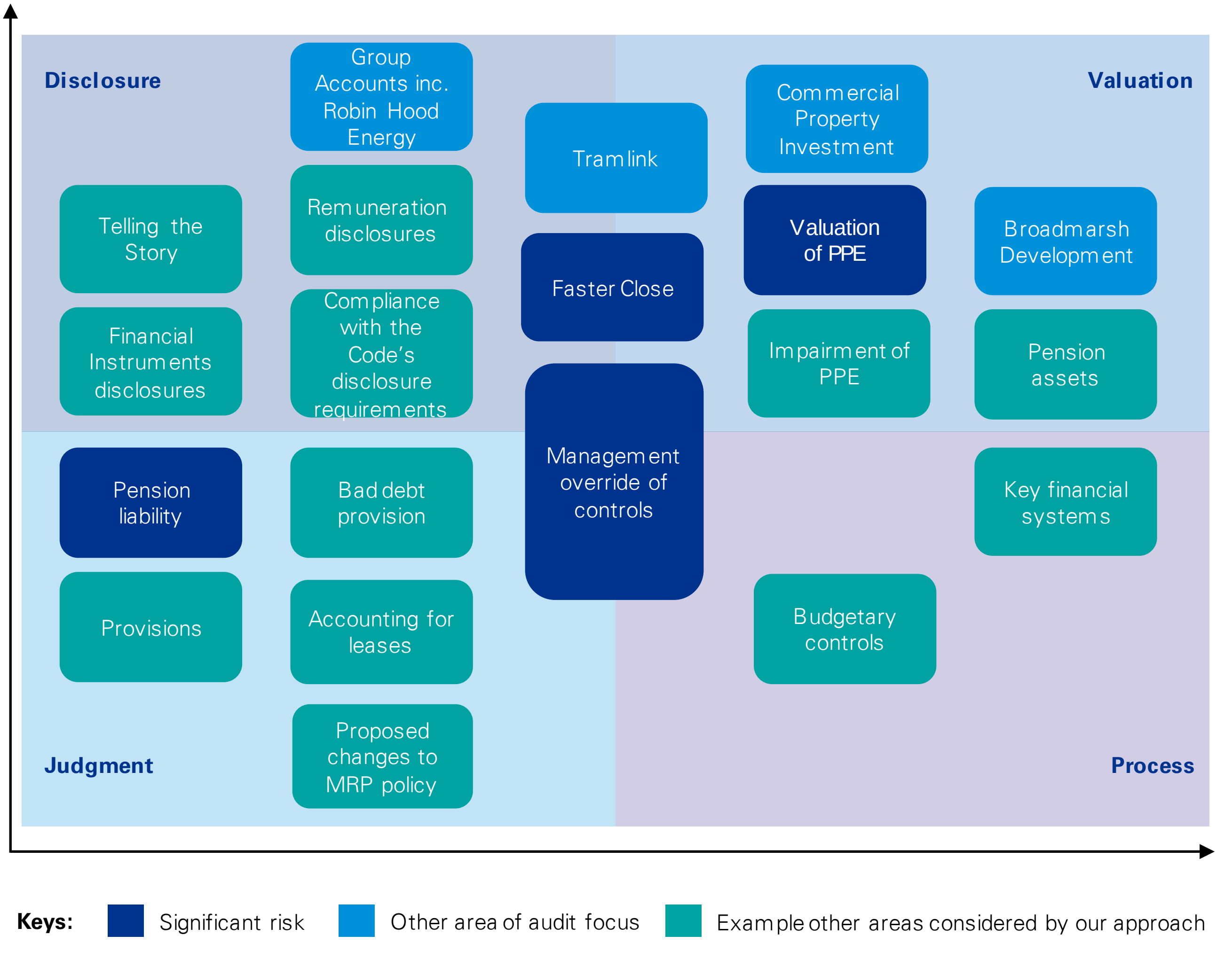
02

Fraudulent revenue recognition

We do not consider this to be a significant risk for local authorities as there are limited incentives and opportunities to manipulate the way income is recognised. We therefore rebut this risk and do not incorporate specific work into our audit plan in this area over and above our standard fraud procedures.

Financial statements audit planning (cont.)

The diagram below identifies significant risks and other areas of audit focus, which we expand on overleaf. The diagram also identifies a range of other areas considered by our audit approach.



Financial statements audit planning (cont.)

Significant Audit Risks

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error in relation to the Authority.

Risk:

Valuation of PPE

The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Authority has adopted a rolling revaluation model which sees all land and buildings revalued over a five year cycle. As a result of this, however, individual assets may not be revalued for four years.

This creates a risk that the carrying value of those assets not revalued in year differs materially from the year end fair value. In addition to this, for various assets, the valuation is undertaken as at 1 April, which presents a risk that the fair value is different at the year end.

Approach:

We will undertake the following work over the valuation of material fixed assets:

- upon application of any revaluation exercise, we will review the revaluation basis and consider its appropriateness. We will engage our valuation specialist to undertake an assessment of the revaluation:
- undertake an assessment of the expertise of the valuer commissioned to perform the revaluation exercise. We will obtain the instructions provided to the valuer and assess the independence and objectivity of the surveyors and the terms under which they were engaged by management;
- consider the source of the information provided to, and used by, the valuer, and undertake appropriate testing to ensure both its completeness and accuracy, including the existence of assets;
- review the approach that the Authority has adopted to assess the risk that assets not subject to valuation are materially misstated and consider the robustness of that approach.
- confirm the appropriateness of any amendments made by management to the information received from the valuer before being incorporated into the financial statements.
- undertake appropriate work to understand the basis upon which any impairments to land and buildings have been calculated. We will test the associated assumptions.

Financial statements audit planning (cont.)

Significant Audit Risks (cont.)

Risk:

Pension Liabilities

The net pension liability represents a material element of the Authority's balance sheet. The Authority is an admitted body of the Nottinghamshire Pension Fund, which had its last triennial valuation completed as at 31 March 2016. This forms an integral basis of the valuation as at 31 March 2018.

The valuation of the Local Government Pension Scheme relies on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which results in the Authority's overall valuation.

There are financial assumptions and demographic assumptions used in the calculation of the Authority's valuation, such as the discount rate, inflation rates, mortality rates etc. The assumptions should also reflect the profile of the Authority's employees, and should be based on appropriate data. The basis of the assumptions is derived on a consistent basis year to year, or updated to reflect any changes.

There is a risk that the assumptions and methodology used in the valuation of the Authority's pension obligation are not reasonable. This could have a material impact to net pension liability accounted for in the financial statements.

Approach:

We will undertake the following the work over the valuation of the pension liability:

- review the controls that the Authority has in place over the information sent directly to the Scheme Actuary;
- liaise with the auditors of the Pension Fund in order to gain an understanding of the effectiveness of those controls operated by the Pension Fund. This will include consideration of the process and controls with respect to the assumptions used in the valuation;
- evaluate the competency, objectivity and independence of Barnett Waddingham;
- review the appropriateness of the key assumptions included within the valuation, compare them to expected ranges, and consider the need to make use of a KPMG Actuary; and
- review the overall actuarial valuation and consider the disclosure implications in the financial statements.

Financial statements audit planning (cont.)

Significant Audit Risks (cont.)

Risk:

Faster Close

In prior years, the Authority has been required to prepare draft financial statements by 30 June and then final signed accounts by 30 September. For years ending on and after 31 March 2018 however, revised deadlines apply which require draft accounts by 31 May and final signed accounts by 31 July.

During 2016/17, the Authority started to prepare for these revised deadlines and advanced its own accounts production timetable so that draft accounts were ready by 12 June. Whilst this was an advancement on the timetable applied in preceding years, further work is still required in order to ensure that the statutory deadlines for 2017/18 are met.

In order to meet the revised deadlines, the Authority may need to make greater use of accounting estimates. In doing so, consideration will need to be given to ensuring that these estimates remain valid at the point of finalising the financial statements. In addition, there are a number of logistical challenges that will need to be managed. These include:

— Ensuring that any third parties involved in the production of the accounts (including valuers, actuaries, subsidiaries and subsidiary auditors are aware of the revised deadlines and have made arrangements to provide the output of their work in accordance with this;

— Revising the closedown and accounts production timetable in order to ensure that all working papers and other supporting documentation are available at the start of the audit process;

— Ensuring that the Audit Committee meeting schedules have been updated to permit signing in July; and

— Applying a shorter paper deadline to the July meeting of the Audit Committee meeting in order to accommodate the production of the final version of the accounts and our ISA 260 report.

In the event that the above areas are not effectively managed there is a significant risk that the audit will not be completed by the 31 July deadline.

There is also an increased likelihood that the Audit Certificate (which confirms that all audit work for the year has been completed) may be issued separately at a later date if work is still ongoing in relation to the Authority's Whole of Government Accounts return. This is not a matter of concern and is not seen as a breach of deadlines.

Approach:

We will liaise with officers in preparation for our audit in order to understand the steps that the Authority is taking in order to ensure it meets the revised deadlines. We will also look to advance audit work into the interim visit in order to streamline the year end audit work.

Where there is greater reliance upon accounting estimates we will consider the assumptions used and challenge the robustness of those estimates.

Financial statements audit planning (cont.)

Other areas of audit focus

Those risks with less likelihood of giving rise to a material error but which are nevertheless worthy of audit understanding.

Issue: **Group Accounts including Robin Hood Energy**

The Authority has a relatively complex Group structure and will therefore need to ensure its Group Accounts are complete and intra group transactions correctly identified and removed.

As we noted in our prior year ISA260 report, one of the Authority's subsidiaries, Robin Hood Energy Ltd (RHE), has seen significant increases in turnover and outturn position since 2015/16, this included posting a £7.5 million operating loss in 2016/17, although we note that this is expected to be improved in 2017/18. As per last year we have made RHE a significant component for our audit.

Approach: We will review the consolidation procedures in place at the Authority, and the Authority's assessment of all entities over which the Authority has control or significant influence and the Authority's subsequent consideration whether or not to consolidate each entity within the Group Accounts.

We will liaise formally with RHE's auditor's to enable us to make use of the outcome of their audit (including their opinion) for our audit opinion on the Authority's Group Accounts.

We will discuss the process to identify and eliminate intra-group transactions.

We will agree the final accounts consolidation back to audited financial statements for each subsidiary, joint venture and Trust fund consolidated within the Group Accounts.

Issue: **Implications of Tramlink's auditors' comments regarding going concern**

Tramlink Nottingham Ltd is one of the Authority's key external partners. The company is a PFI concession who built the tram lines for NET Phase 2, and now operates and maintains all tram lines in Nottingham.

In their 2016/17 financial statements, Tramlink's auditors' issued an Emphasis of Matter paragraph within their opinion in regards to going concern and financial uncertainties linked to breaching bank covenant ratios.

Approach: We will discuss with the Authority the latest position in regards to Tramlink Nottingham Ltd and any implications for the Authority's financial statements.

Financial statements audit planning (cont.)

Other areas of audit focus (cont.)

Issue: **Broadmarsh Development**

The Authority has began work on its Broadmarsh redevelopment with the demolition of the Broadmarsh car park. The Authority is due to submit plans to Executive Board for approval in regards to the next phase of the project in developing a new car park and shopping centre.

The work to date will have an impact upon the financial statements, through disposing of the existing car park, and capitalising costs incurred up to 31 March 2018.

Approach: We will consider the accounting treatment of the Broadmarsh development as at 31 March 2018, specifically the accounting treatment of the demolition of the car park and capitalisation of costs incurred to date.

We will discuss with officers the financial plans of the project including proposed financing and financial plan.

Issue: **Commercial Property Investment**

In 2016/17 the Authority invested £87.5 million in commercial properties. The Authority set out within its 2017/18 budget a planned £41.85m of further investment property acquisitions for 2017/18, and it is anticipated that valuation of the Authority's investment property portfolio will exceed £200m by the year-end.

The Authority will need to ensure that all commercial property investments are valued at fair value at 31 March 2018, that there are arrangements in place to ensure associated borrowing is sustainable, and that arrangements are in place to cope with events such as impairment of the assets.

Approach: We will review the valuation of commercial property investments, including new additions in year.

We will consider the arrangements to assess the sustainability of borrowings both individually and as a whole to the Authority's investment property portfolio, and the financial robustness of the Authority if the assets decrease in value.

Issue: **Proposed changes to Minimum Revenue Provisions**

The Authority has informed us that they are considering making changes to the way it calculates its Minimum Revenue Provision (MRP) which has the potential to have a significant financial impact.

Approach: We will review the proposed changes to the MRP policy.

We will consider how the Authority communicates to its Members the financial impact of any changes, including in the medium and long term.

Financial statements audit planning (cont.)

Materiality

We are required to plan our audit to determine with reasonable confidence whether or not the financial statements are free from material misstatement. An omission or misstatement is regarded as material if it would reasonably influence the user of financial statements. This therefore involves an assessment of the qualitative and quantitative nature of omissions and misstatements.

Generally, we would not consider differences in opinion in respect of areas of judgement to represent 'misstatements' unless the application of that judgement results in a financial amount falling outside of a range which we consider to be acceptable.

For the Authority, materiality for planning purposes has been set at £10.5 million for the Authority's standalone accounts and for the group accounts (PY £13 million).

We design our procedures to detect errors in specific accounts at a lower level of precision.

Materiality

£10.5m

(2016/17: £13m, 1.15%)

£525k Misstatements reported to the audit committee (2016/17: £650k)

£7.8m Procedures designed to detect individual errors (2016/17: £9.75m

£10.5m Materiality for the financial statements as a whole (2016/17: £13m)

Reporting to the Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any unadjusted misstatements of lesser amounts to the extent that these are identified by our audit work.

Under ISA 260(UK&I) 'Communication with those charged with governance', we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 (UK&I) defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £525k.

If management has corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit Committee to assist it in fulfilling its governance responsibilities.

We will report:

- Non-Trivial corrected audit misstatements
- Non-trivial uncorrected audit misstatements
- Errors and omissions in disclosure (Corrected and uncorrected)

Financial statements audit planning (cont.)

Group audit

In addition to the Authority, the group accounts for 2016/17 included six subsidiaries, two joint ventures and one trust fund. We have identified Robin Hood Energy Ltd as significant component in a financial context of the group audit.

We will reassess the significance of these subsidiaries throughout our audit and will report any changes in our assessment to the Audit Committee.

To support our audit work on the Authority's group accounts, we seek to place reliance on the work of BDO LLP who is the auditor to Robin Hood Energy Ltd. We will liaise with them in order to confirm that their programme of work is adequate for our purposes and they satisfy professional requirements.

We will report the following matters in our Report to those charged with Governance:

01

Any deficiencies in the system of internal controls or instances of fraud which the subsidiary auditors identify;

02

Any limitations on the group audit, for example, where the our access to information may have been restricted; and

03

Any instances where our evaluation of the work the subsidiary auditors gives rise to concern about the quality of that auditor's work.

Value for money arrangements work

VFM audit approach

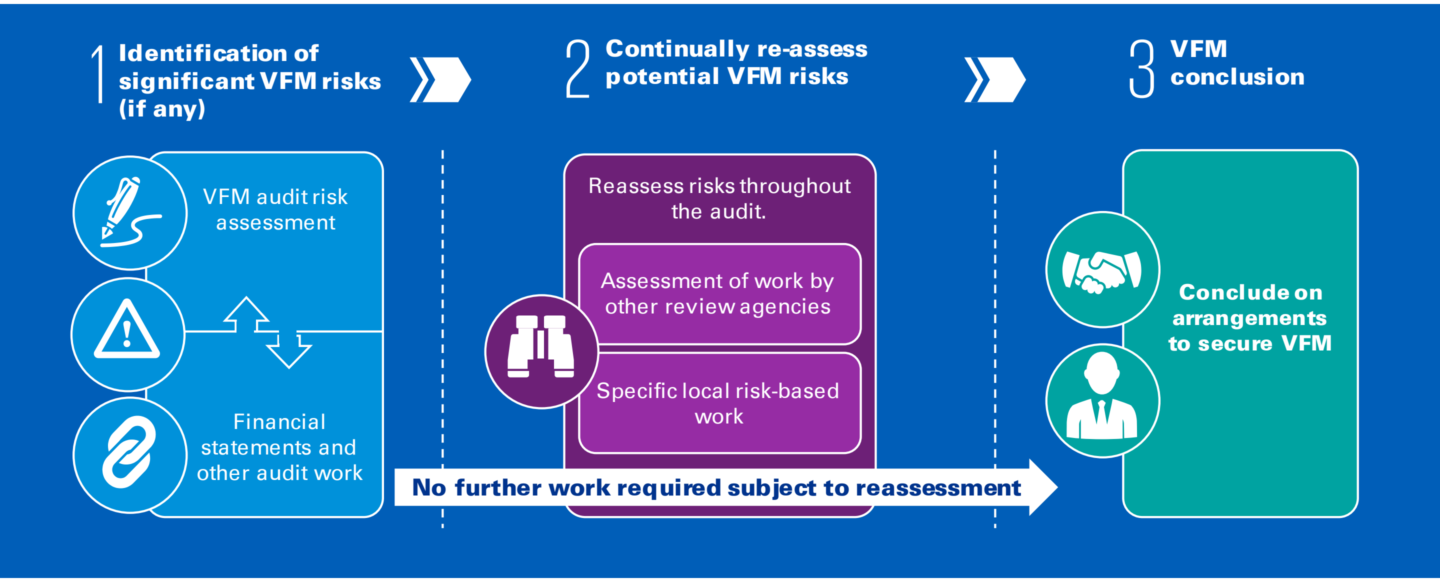
The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the authority ‘has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources’.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to ‘take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor’s judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body’s arrangements.’

Overall criterion

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

The VFM approach is fundamentally unchanged from that adopted in 2016/17 and the process is shown in the diagram below. The diagram overleaf shows the details of the sub-criteria for our VFM work.



Value for money arrangements work (cont.)

Value for Money sub-criterion

Informed decision making

Proper arrangements:

- Acting in the public interest, through demonstrating and applying the principles and values of sound governance.
- Understanding and using appropriate and reliable financial and performance information to support informed decision making and performance management.
- Reliable and timely financial reporting that supports the delivery of strategic priorities.
- Managing risks effectively and maintaining a sound system of internal control.

Sustainable resource deployment

Proper arrangements:

- Planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions.
- Managing and utilising assets to support the delivery of strategic priorities.
- Planning, organising and developing the workforce effectively to deliver strategic priorities.

Working with partners and third parties

Proper arrangements:

- Working with third parties effectively to deliver strategic priorities.
- Commissioning services effectively to support the delivery of strategic priorities.
- Procuring supplies and services effectively to support the delivery of strategic priorities.

Value for money arrangements work (cont.)

VFM audit stage

VFM audit risk assessment

Audit approach

We consider the relevance and significance of the potential business risks faced by all local authorities, and other risks that apply specifically to the Authority. These are the significant operational and financial risks in achieving statutory functions and objectives, which are relevant to auditors' responsibilities under the *Code of Audit Practice.*

In doing so we consider:

- The Authority's own assessment of the risks it faces, and its arrangements to manage and address its risks;
- Information from the Public Sector Auditor Appointments Limited VFM profile tool;
- Evidence gained from previous audit work, including the response to that work; and
- The work of other inspectorates and review agencies.

Linkages with financial statements and other audit work

Audit approach

There is a degree of overlap between the work we do as part of the VFM audit and our financial statements audit. For example, our financial statements audit includes an assessment and testing of the Authority's organisational control environment, including the Authority's financial management and governance arrangements, many aspects of which are relevant to our VFM audit responsibilities.

We have always sought to avoid duplication of audit effort by integrating our financial statements and VFM work, and this will continue. We will therefore draw upon relevant aspects of our financial statements audit work to inform the VFM audit.

Identification of significant risks

Audit approach

The Code identifies a matter as significant *'if, in the auditor's professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public. Significance has both qualitative and quantitative aspects.'*

If we identify significant VFM risks, then we will highlight the risk to the Authority and consider the most appropriate audit response in each case, including:

- Considering the results of work by the Authority, inspectorates and other review agencies; and
- Carrying out local risk-based work to form a view on the adequacy of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources.

Value for money arrangements work (cont.)

VFM audit stage

Assessment of work by other review agencies, and Delivery of local risk based work

Audit approach

Depending on the nature of the significant VFM risk identified, we may be able to draw on the work of other inspectorates, review agencies and other relevant bodies to provide us with the necessary evidence to reach our conclusion on the risk.

We will also consider the evidence obtained by way of our financial statements audit work and other work already undertaken.

If evidence from other inspectorates, agencies and bodies is not available and our other audit work is not sufficient, we will need to consider what additional work we will be required to undertake to satisfy ourselves that we have reasonable evidence to support the conclusion that we will draw. Such work may include:

– Additional meetings with senior managers across the Authority;

– Review of specific related minutes and internal reports;

– Examination of financial models for reasonableness, using our own experience and benchmarking data from within and without the sector.

Concluding on VFM arrangements

Audit approach

At the conclusion of the VFM audit we will consider the results of the work undertaken and assess the assurance obtained against each of the VFM themes regarding the adequacy of the Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources.

If any issues are identified that may be significant to this assessment, and in particular if there are issues that indicate we may need to consider qualifying our VFM conclusion, we will discuss these with management as soon as possible. Such issues will also be considered more widely as part of KPMG's quality control processes, to help ensure the consistency of auditors' decisions.

Reporting

Audit approach

We have completed our initial VFM risk assessment and have identified one significant VFM risk. On the following page, we report the results of our initial risk assessment.

We will report on the results of the VFM audit through our ISA 260 Report. This will summarise any specific matters arising, and the basis for our overall conclusion.

The key output from the work will be the VFM conclusion (i.e. our opinion on the Authority's arrangements for securing VFM), which forms part of our audit report.

Value for money arrangements work (cont.)

Significant VFM Risks

Those risks requiring specific audit attention and procedures to address the likelihood that proper arrangements are not in place to deliver value for money.

Risk:

Delivery of budgets

The Authority's net revenue budget of £238.54m 2017/18 was approved by full Council in March 2017. The forecast at Quarter 2, stated that the Authority will deliver an over spend which has been forecasted at: £2.65m (Best case), £2.70m (Medium Case) or £6.55m (Worst Case).

Proposed savings for 2017/18 have been planned at £24.45m from savings on both portfolios and health integration as per the 2017/18 budget. Further savings of £25.86m and £29.14m for 2018/19 and 2019/20 respectively will be required principally to address future reductions to local authority funding alongside service cost and demand pressures as set out within the Medium Term Financial Plan, notably within Adult Social Care. As a result, the need for savings along with income generation from commercial activity will continue to have a significant impact on the Authority's financial resilience, as it strives to put in place a sustainable budget

In addition, the Authority's overall level of borrowing as at 31 March 2017 was £796.26m. As reported to Audit Committee in January 2018 via the Treasury Management Half Yearly Update, external borrowing is expected to increase by £255m in 2017/18 based on the revised capital program and forecast cash flow requirements.

Therefore we consider this to be a significant risk.

Approach:

As part of our additional risk based work we will undertake the following procedures over this significant risk:

— review the Authority's Medium Term Financial Plan, and consider the proposed actions to mitigate factors such as funding reductions, salary and general inflation, demand pressures, restructuring costs and sensitivity analysis given the degree of variability in the above factors;

— review the reported actual delivery of the Authority's savings programme compared to planned savings;

— review the arrangements in place to ensure that overall borrowing levels are sustainable;

— review the budget and savings plan for 2018/19, including any contingencies.

VFM Sub-criterion:

This risk is related to the following Value For Money sub-criteria

— Informed decision making;

— Sustainable resource deployment; and

— Working with partners and third parties

Financial statements audit planning (cont.)

Significant VFM Risks (cont.)

Risk:

Group Governance Arrangements

The Authority has a relatively complex group structure. In 2016/17 the Authority consolidated within its group accounts, six subsidiaries, two joint ventures and one trust fund. Of these, most notably was the expansion of the Robin Hood Energy (RHE), which we classified as a significant component. For 2017/18, further growth of RHE is forecast, and we will therefore continue to classify RHE as a significant component.

The Authority has recognised that as its group structure evolves, then so must the overarching governance arrangements in place at the Authority to monitor and ensure that appropriate accountability of the respective subsidiaries and joint ventures are in place. The Authority is in the process of commencing a key review of the Authority's group governance arrangements.

In addition to this for years ending on and after 31 March 2018 revised deadlines apply which require draft accounts by 31 May and final signed accounts by 31 July. In order to meet the revised deadlines, there are a number of logistical challenges that will need to be managed, one of which is ensuring that any third parties (subsidiaries and subsidiary auditors) involved in the production of the accounts are aware of the revised deadlines and have made arrangements to provide the output of their work in accordance with the closedown and accounts production timetable.

Approach:

As part of our work we shall:

— review the current governance arrangements in place surrounding the current group structure:

— consider the findings from the Authority's own internal review of group governance arrangements. We referred to this review in our prior year ISA260 report, where the terms of reference for the internal review were presented to Audit Committee in September last year

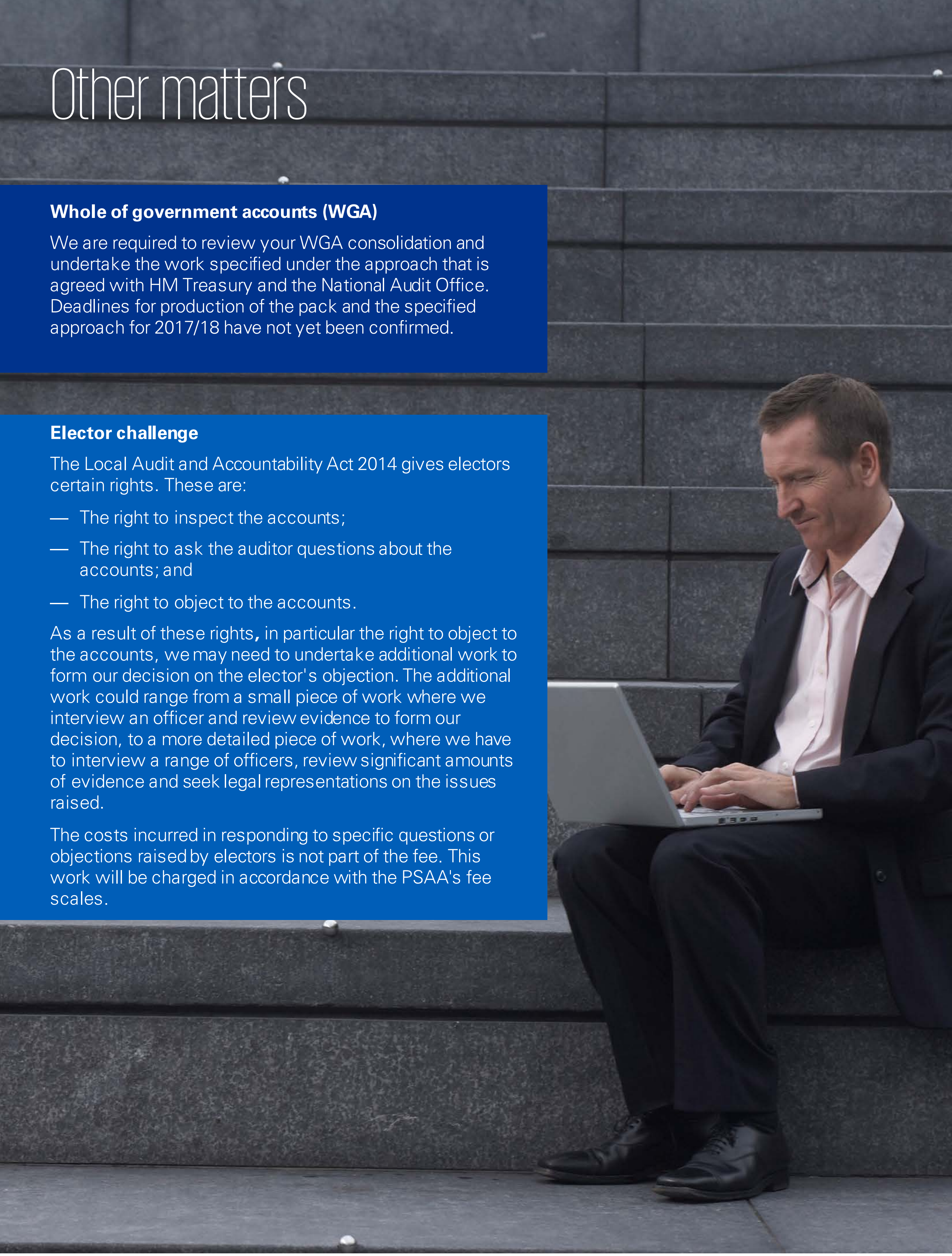
VFM Sub-criterion:

This risk is related to the following Value For Money sub-criteria

— Informed decision making;

— Sustainable resource deployment; and

— Working with partners and third parties



Other matters

Whole of government accounts (WGA)

We are required to review your WGA consolidation and undertake the work specified under the approach that is agreed with HM Treasury and the National Audit Office. Deadlines for production of the pack and the specified approach for 2017/18 have not yet been confirmed.

Elector challenge

The Local Audit and Accountability Act 2014 gives electors certain rights. These are:

- The right to inspect the accounts;
- The right to ask the auditor questions about the accounts; and
- The right to object to the accounts.

As a result of these rights, in particular the right to object to the accounts, we may need to undertake additional work to form our decision on the elector's objection. The additional work could range from a small piece of work where we interview an officer and review evidence to form our decision, to a more detailed piece of work, where we have to interview a range of officers, review significant amounts of evidence and seek legal representations on the issues raised.

The costs incurred in responding to specific questions or objections raised by electors is not part of the fee. This work will be charged in accordance with the PSAA's fee scales.

Other matters

Reporting and communication

Reporting is a key part of the audit process, not only in communicating the audit findings for the year, but also in ensuring the audit team are accountable to you in addressing the issues identified as part of the audit strategy. Throughout the year we will communicate with you through meetings with the finance team and the Audit Committee. Our communication outputs are included in Appendix 1.

Independence and Objectivity

Auditors are also required to be independent and objective. Appendix 3 provides more details of our confirmation of independence and objectivity.

Audit fee

Our Audit Fee Letter 2017/2018 presented to you in April 2017 first set out our fees for the 2017/2018 audit. This letter also set out our assumptions. We have not considered it necessary to seek approval for any changes to the agreed fees at this stage.

Should there be a need to charge additional audit fees then this will be agreed with the s.151 Officer and PSAA. If such a variation is agreed, we will report that to you in due course.

The planned audit fee for 2017/18 is £172,118, consistent with the scale fee for 2016/2017 of £172,118 (note that we have agreed a fee variation of £6,609 in regards to last year's external audit, with your officers and the PSAA. The fee variation relates to additional audit work required in order for us to sign our accounts opinion relating to:

- Estimated pensions data used by the Authority during its triennial revaluation (£2,102);
- Authority's Group Structure (£2,594); and
- NET 2 PFI Model and related disclosures (£1,913).

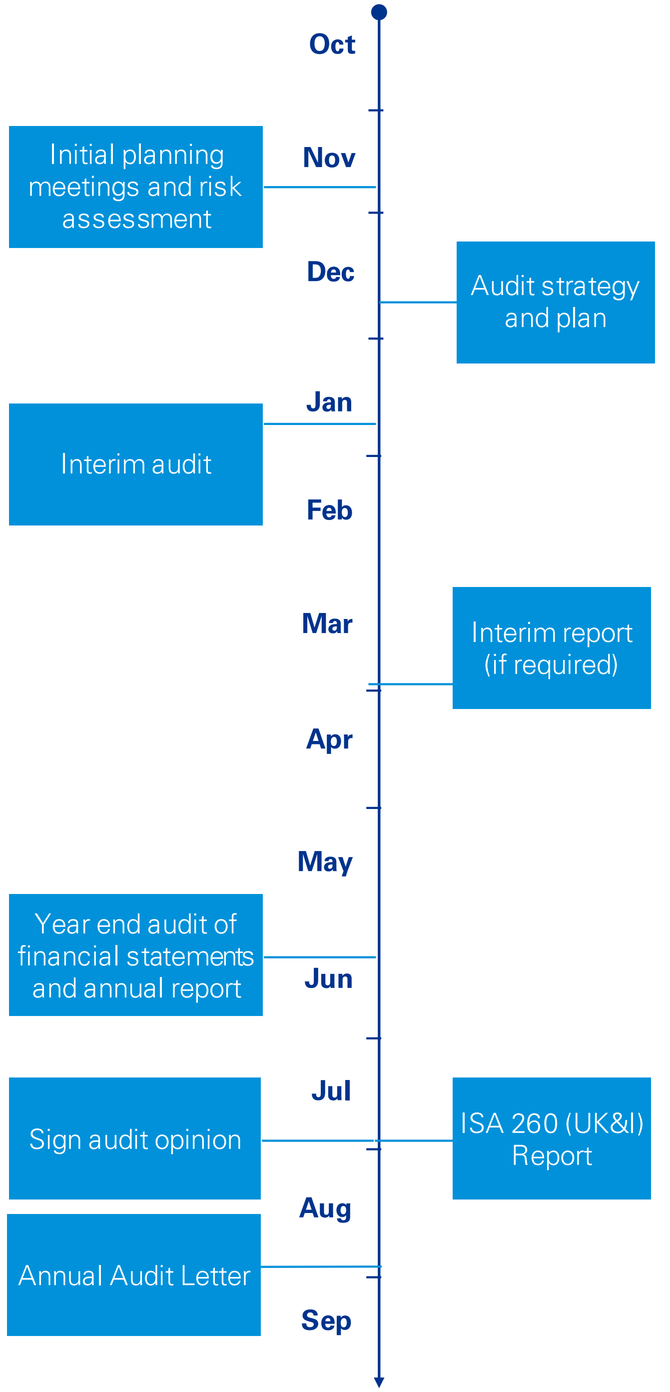
Our scale fee in regards to the Authority's Housing benefits audit for 2017/18 is £18,458. This fee is determined by PSAA.

Appendix 1:

Key elements of our financial statements audit approach

Communication

Continuous communication involving regular meetings between Audit Committee, Senior Management and audit team.



Appendix 1:

Key elements of our financial statements audit approach (cont.)

Audit workflow

Planning

- Determining our materiality level;
- Risk assessment;
- Identification of significant risks;
- Consideration of potential fraud risks;
- Identification of key account balances in the financial statements and related assertions, estimates and disclosures;
- Consideration of managements use or experts; and
- Issuing this audit plan to communicate our audit strategy.

Control evaluation

- Understand accounting and reporting activities
- Evaluate design and implementation of selected controls
- Test operating effectiveness of selected controls
- Assess control risk and risk of the accounts being misstated

Substantive testing

- Plan substantive procedures
- Perform substantive procedures
- Consider if audit evidence is sufficient and appropriate

Completion

- Perform completion procedures
- Perform overall evaluation
- Form an audit opinion
- Audit Committee reporting

Appendix 2:

Audit team

Your audit team has been drawn from our specialist public sector assurance department.

Tony Crawley
Director

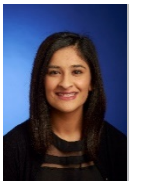
T: +44 (0) 11 6256 6067
E: tony.crawley@kpmg.co.uk

'My role is to lead our team and ensure the delivery of a high quality, valued added external audit opinion.
I will be the main point of contact for the Audit Committee and Chief Executive.'

Thomas Tandy
Manager

T: +44 (0) 11 5945 4480
E: tandy.thomas@kpmg.co.uk

'I provide quality assurance for the audit work and specifically any technical accounting and risk areas.
I will work closely with Tony to ensure we add value.
I will liaise with the Strategic Director of Finance'



Arvinder Khela
Assistant Manager

T: +44 (0) 12 1609 5880
E: arvinder.khela@kpmg.co.uk

'I will be responsible for the on-site delivery of our work and will supervise the work of our audit assistants.'

Appendix 3:

Independence and objectivity requirements

ASSESSMENT OF OUR OBJECTIVITY AND INDEPENDENCE AS AUDITOR OF NOTTINGHAM CITY COUNCIL

Professional ethical standards require us to provide to you at the planning stage of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code of Audit Practice, the provisions of Public Sector Audit Appointments Ltd's ('PSAA's') Terms of Appointment relating to independence and the requirements of the FRC Ethical Standard and General Guidance Supporting Local Audit (Auditor General Guidance 1 – AGN01) issued by the National Audit Office ('NAO').

This Appendix is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

- General procedures to safeguard independence and objectivity;
- Independence and objectivity considerations relating to the provision of non-audit services; and
- Independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners, Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Communications
- Internal accountability
- Risk management
- Independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

Independence and objectivity considerations relating to the provision of non-audit services

Summary of fees

We have considered the fees charged by us to the authority and its affiliates for professional services provided by us during the reporting period.

Facts and matters related to the provision of non-audit services and the safeguards put in place that bear upon our independence and objectivity, are set out in the following table

Analysis of Non-audit services for the year ended 31 March 2018

See table overleaf.

Independence and objectivity requirements

Independence and objectivity considerations relating to the provision of non-audit services (cont.)

Analysis of Non-audit services for the year ended 31 March 2018

<table>
<tr><th>Description of scope of services</th><th>Value of Services Delivered in the year ended 31 March 2018
£000</th><th>Principal threats to independence and Safeguards Applied.</th></tr>
<tr><td>Additional certification work in regards to Pooling of Capital Receipts Return</td><td>£4,000</td><td rowspan="4">Self-interest: These engagements are entirely separate from the audit through a separate contract. In addition, the audit fee scale rates were set independently to KPMG by the PSAA (previously Audit Commission). Therefore, the proposed engagement will have no perceived or actual impact on the audit team and the audit team resources that will be deployed to perform a robust and thorough audit.

Self review: The nature of this other ‘assurance’ work has no impact on the 2017/18 audit as it relates to 2016/17 financial year. Therefore, it does not impact on our opinion and we do not consider it to be a threat to our role as external auditors. We do not audit the Nottingham City Transport (NCT) in regards to our pensions work.

Management threat: This work involved the certification of these returns only –all decisions were made by the Authority. In regards to the pensions work, we are not the auditors for NCT

Familiarity: This threat is limited given the scale, nature and timing of the work.

Advocacy: We will not act as advocates for the Authority in any aspect of this work. We have drawn on our experience in such roles to certify the returns but the scope of this work falls well short of any advocacy role

Intimidation: Not applicable.</td></tr>
<tr><td>Additional certification work in regards to Teachers Pension Return</td><td>£2,500</td></tr>
<tr><td>Additional certification work in regards to SFA subcontracting</td><td>£4,000</td></tr>
<tr><td>Pensions Advisory Services for Nottingham City Transport</td><td>£14,750</td></tr>
</table>

Appropriate approvals have been obtained from PSAA for all non-audit services above the relevant thresholds provided by us during the reporting period. In addition, we monitor our fees to ensure that we comply with the 70% non-audit fee cap set by the NAO. Non-audit services currently **total £25,250**, which is **15%** of the audit fee. We have agreed with the PSAA that our £31,000 fee for strategic advisory services work for Midlands Engine, procured on its behalf by the Authority, does not count towards the fee threshold as it is not for the Authority. For clarity, your audit team is not involved in the Midlands Engine work.

Independence and objectivity considerations relating to other matters

There are no other matters that, in our professional judgment, bear on our independence which need to be disclosed to the Audit Committee.

Confirmation of audit independence

We confirm that as of the date of this report, in our professional judgment, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This report is intended solely for the information of the Audit Committee of the authority and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

kpmg.com/uk

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Tony Crawley, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers, by email to Andrew.Sayers@kpmg.co.uk. After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

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