

# Tendring District Council

## DRAFT - Report to the Audit Committee

External Audit Plan & Strategy for the year ending  
31 March 2025

March 2025

# Introduction

To the Audit Committee  
of Tendring District Council

We are pleased to have the opportunity to meet with you to discuss our audit of the financial statements of Tendring District Council for the year ending 31<sup>st</sup> March 2025.

We have been appointed as your auditors by Public Sector Audit Appointments Ltd. The audit is governed by the provisions of the Local Audit and Accountability Act 2014 and in compliance with the NAO Code of Audit Practice.

This report outlines our risk assessment and planned audit approach. Our planning activities are still ongoing and we will communicate any significant changes to the planned audit approach. We provide this report to you in advance of the meeting to allow you sufficient time to consider the key matters and formulate your questions.

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## The engagement team

Emma Larcombe is the engagement director on the audit. She has over 15 years of industry experience.

Other key members of the engagement team include Jodie Preston (Lead Manager).

Yours sincerely,

Emma Larcombe  
**Director - KPMG LLP**  
27<sup>th</sup> March 2025

## How we deliver audit quality

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion. We consider risks to the quality of our audit in our engagement risk assessment and planning discussions.

We define 'audit quality' as being the outcome when audits are:

- Executed consistently, in line with the requirements and intent of applicable professional standards within a strong system of quality controls and
- All of our related activities are undertaken in an environment of the utmost level of objectivity, independence, ethics and integrity.

We depend on well planned timing of our audit work to avoid compromising the quality of the audit. This is also heavily dependent on receiving information from management and those charged with governance in a timely manner. The audit undertaken in the current year is dependent on the finalisation of the previous auditor's work over historical financial statements. We aim to complete all audit work no later than 2 days before audit signing

# Overview of planned scope including materiality

## Our materiality levels

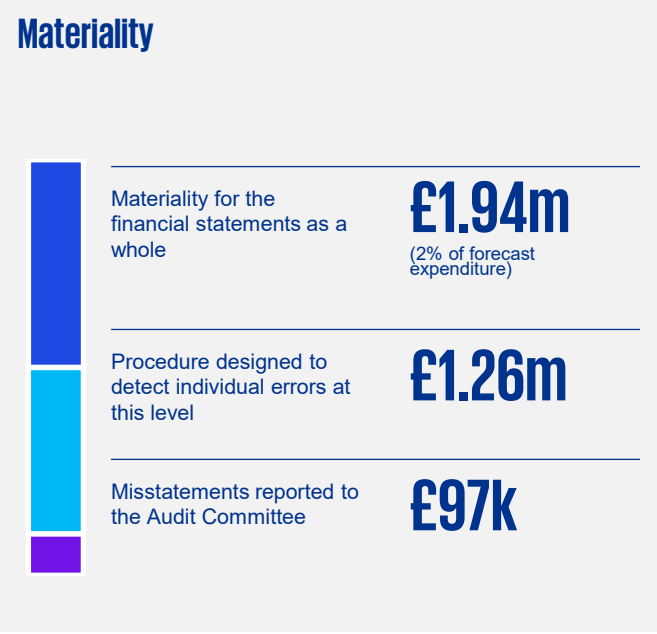
We determined materiality for the financial statements at a level which could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. We used a benchmark of expenditure which we consider to be appropriate given the sector in which the entity operates, its ownership and financing structure, and the focus of users.

We considered qualitative factors such as stability of legislation, lack of shareholders and debt arrangements when determining materiality for the financial statements as a whole.

To respond to aggregation risk from individually immaterial misstatements, we design our procedures to detect misstatements at a lower level of materiality £1.26m / 65% of materiality driven by our expectations of increased level of undetected or uncorrected misstatements in the period resulting from uncertainties in the prior year unaudited figures.

## We will report misstatements to the audit committee including:

- Corrected and uncorrected audit misstatements above £97K.
- Errors and omissions in disclosure (Corrected and uncorrected) and the effect that they, individually in aggregate, may have on our opinion.
- Other misstatements we include due to the nature of the item.



**Materiality**  
**£1.94m**  
 2% of expenditure £97m

# Overview of planned scope including materiality (cont.)

## Timing of our audit and communications

- We will maintain communication led by the engagement partner and manager throughout the audit. We set out below the form, timing and general content of our planned communications:
- Kick-off meeting with management in February 2025 where we discuss our approach to the Planning and Interim phases of our audit;
- Audit Committee meeting in March 2025 where we present our final draft plan;
- Regular status meetings with management on where we communicate progress on the audit plan, any misstatements, control deficiencies and significant issues;
- Closing meeting with management in December 2025 where we discuss the auditor’s report and any outstanding deliverables;
- Final Audit Committee meeting here we communicate audit misstatements and significant control deficiencies; and
- Biannual private meetings can also be arranged with the Committee chair if there is interest.

## Using the work of others and areas requiring specialised skill

We outline below where, in our planned audit response to audit risks, we expect to use the work of others such as Internal Audit or require specialised skill/knowledge to perform planned audit procedures and evaluate results.

Others	Extent of planned involvement or use of work
<b>Internal Audit</b>	We will perform inquiries with the internal audit team and review the minutes of internal audit meetings to understand if there are any specific risks identified as part of the routine internal audit process. However, we do not intend to use the work of internal auditors, therefore we will not perform any detailed risk assessment procedures.
<b>KPMG Pensions Centre of Excellence</b>	KPMG’s internal actuarial specialists will perform an assessment of the year end Pensions valuation
<b>KPMG Revaluation Centre of Excellence</b>	KPMG’s internal revaluation specialists will perform an assessment of the year-end property, plant and equipment valuation.

# Significant risks and Other audit risks

Our risk assessment draws upon our understanding of the applicable financial reporting framework, knowledge of the business, the sector and the wider economic environment in which Tendring District Council operates.

We also use our regular meetings with senior management to update our understanding and take input from sector and internal audit reports.

Due to the current levels of uncertainty there is an increased likelihood of changes to this risks throughout the audit cycle. Where such changes are identified we will amend our audit approach accordingly and communicate this to the Audit Committee.

## Value for money

We are required to provide commentary on the arrangements in place for ensuring Value for Money is achieved at the Council and report on this via our Auditor's Annual Report. This will be published on the Council's website and include a commentary on our view of the appropriateness of the Council's arrangements against each of the three specified domains of Value for Money: financial sustainability; governance; and improving economy, efficiency and effectiveness.

Our risk assessment work in this area is still ongoing.

### Significant risks

1. Valuation of fixed assets

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2. Valuation of post retirement benefit obligations

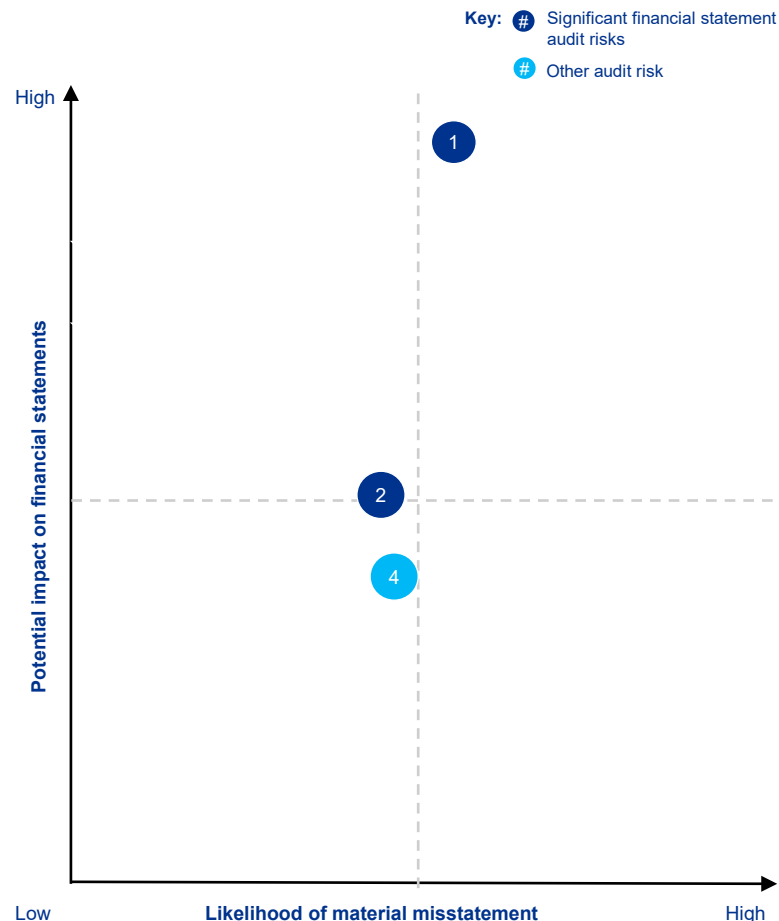
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3. Management override of controls\*

\* pervasive

### Other audit risks

4. IFRS16



# Audit risks and our audit approach (cont.)

## 1 Valuation of land and buildings

The carrying amount of revalued Land & Buildings differs materially from the fair value



### Significant audit risk

The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate current value at that date.

Land and buildings are valued either at existing use value (EUV) or for specialised assets at Depreciated Replacement cost (DRC) which includes assumptions made by the Valuer for relevant build costs, obsolescence and professional fees costs.

There is therefore the risk for those assets that are revalued in the year, which involves significant judgement and estimation on behalf of the engaged valuer.

We were unable to perform our planned procedures in the prior year due to identified issues including:

- The valuer used the gross external area (GEA) to perform the valuation, rather than gross internal area (GIA) for specialised buildings within other land and buildings and an accurate value of this difference could not be determined
- The Council do not hold sufficient data such as up to date floor plans for the asset portfolio revalued under other land and buildings.

We raised high priority recommendations in relation to this.



### Planned response

We will perform the following procedures designed to specifically address the significant risk associated with the valuation:

- We will critically assess the independence, objectivity and expertise of the valuers used in developing the valuation of the Council's properties at 31 March 2025;
- We will inspect the instructions issued to the valuers for the valuation of land and buildings to verify they are appropriate to produce a valuation consistent with the requirements of the CIPFA Code.
- We will compare the accuracy of the data provided to the valuers for the development of the valuation to underlying information;
- We will evaluate the design and implementation of controls in place for management to review the valuation and the appropriateness of assumptions used;
- We will challenge the appropriateness of the valuation of land and buildings; including any material movements from the previous revaluations. We will challenge key assumptions within the valuation as part of our judgement;
- We will agree the calculations performed of the movements in value of land and buildings and verify that these have been accurately accounted for in line with the requirements of the CIPFA Code;
- We will utilise our own valuation specialists to review the valuation report prepared by the Council's valuers to confirm the appropriateness of the methodology utilised; and
- Disclosures: We will consider the adequacy of the disclosures concerning the key judgements and degree of estimation involved in arriving at the valuation.

# Audit risks and our audit approach (cont.)

## 2 Valuation of post retirement benefit obligations

An inappropriate amount is estimated and recorded for the defined benefit obligation



### Significant audit risk

The valuation of the post retirement benefit obligations involves the selection of appropriate actuarial assumptions, most notably the discount rate applied to the scheme liabilities, inflation rates and mortality rates. The selection of these assumptions is inherently subjective and small changes in the assumptions and estimates used to value the Council's pension liability could have a significant effect on the financial position of the Council

The effect of these matters is that, as part of our risk assessment, we determined that post retirement benefits obligation has a high degree of estimation uncertainty. The financial statements disclose the assumptions used by the Council in completing the year end valuation of the pension deficit and the year on year movements.

We have identified this in relation to the following pension scheme memberships: Essex Local Government Pension Scheme



### Planned response

We will perform the following procedures:

- Understand the processes the Council have in place to set the assumptions used in the valuation;
- Evaluate the competency, objectivity of the actuaries to confirm their qualifications and the basis for their calculations;
- Perform inquiries of the accounting actuaries to assess the methodology and key assumptions made, including actual figures where estimates have been used by the actuaries, such as the rate of return on pension fund assets;
- Agree the data provided by the audited entity to the Scheme Administrator for use within the calculation of the scheme valuation;
- Evaluate the design and implementation of controls in place for the Council to determine the appropriateness of the assumptions used by the actuaries in valuing the liability;
- Test, with the support of our own actuarial specialists, the key assumptions applied, being the discount rate, inflation rate and mortality/life expectancy against externally derived data;
- Confirm that the accounting treatment and entries applied by the Group are in line with IFRS and the CIPFA Code of Practice;
- Consider the adequacy of the Council's disclosures in respect of the sensitivity of the deficit or surplus to these assumptions;
- Assess the impact of a new triennial valuation model and/or any special events, where applicable.

# Audit risks and our audit approach (cont.)

## 3 Management override of controls(a)

Fraud risk related to unpredictable way management override of controls may occur



- Professional standards require us to communicate the fraud risk from management override of controls as significant.
- Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.
- We have not identified any specific additional risks of management override relating to this audit.

*Note: (a) Significant risk that professional standards require us to assess in all cases.*



Our audit methodology incorporates the risk of management override as a default significant risk.

- Assess accounting estimates for biases by evaluating whether judgements and decisions in making accounting estimates, even if individually reasonable, indicate a possible bias.
- Evaluate the selection and application of accounting policies.
- In line with our methodology, evaluate the design and implementation of controls over journal entries and post closing adjustments.
- Assess the appropriateness of changes compared to the prior year to the methods and underlying assumptions used to prepare accounting estimates.
- Assess the business rationale and the appropriateness of the accounting for significant transactions that are outside the component's normal course of business, or are otherwise unusual.
- We will analyse all journals through the year using data and analytics and focus our testing on those with a higher risk.



# Audit risks and our audit approach (cont.)

## 4 IFRS16 Leases

Lease terms and lease payments may be inappropriately determined.



### Other audit risk

IFRS 16 Leases will be fully adopted for the first time within the 2024/25 accounts. Impact disclosures were required and reviewed as part of the 2023/24 audit.

The main source of this risk is that lease terms and lease payments are inappropriately determined. This is a particular risk for arrangements which are not subject to a formal contract. Other risks include that the discount rate used to measure the lease liability is inappropriately determined or that a lease liability is not appropriately remeasured when reassessment is required.

Linked to the above there is a potential risk that lease payments are not completely and accurately recorded, are not recorded in the correct accounting period or have not occurred.



### Planned response

We will perform the following procedures:

- We will evaluate the Council’s process for reviewing current arrangements and contracts to ascertain whether there is a lease falling within the remit of the standard;
- We will critically assess the key decisions made about material contracts such as property leases;
- We will review the discount rate used in the calculation of the lease liability and confirm that the rate used the rate implicit within the lease payments for that specific arrangement;
- We will reperform the calculation of the lease liability and right of use asset for a sample of leases; and
- We will critically assess the disclosure proposed for compliance with the requirements.

# Audit risks and our audit approach

## Revenue – Rebuttal of Significant Risk

Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. Due to the nature of the revenue within the sector we have rebutted this significant risk. We have set out the rationale for the rebuttal of key types of income in the table below.

Description of Income	Nature of Income	Rationale for Rebuttal
<b>Council tax</b>	This is the income received from local residents paid in accordance with an annual bill based on the banding of the property concerned.	The income is highly predictable and is broadly known at the beginning of the year, due to the number of properties in the area and the fixed price that is approved annually based on a band D property: it is highly unlikely for there to be a material error in the population.
<b>Business rates</b>	Revenue received from local businesses paid in accordance with an annual demand based on the rateable value of the business concerned.	The income is highly predictable and is broadly known at the beginning of the year, due to the number of businesses in the area and the fixed amount that is approved annually: it is highly unlikely for there to be a material error in the population.
<b>Fees and charges</b>	Revenue recognised from receipt of fixed fee services, in line with the fees and charges schedules agreed and approved annually.	The income stream represents high volume, low value sales, with simple recognition. Fees and charges values are agreed annually. We do not deem there to be any incentive or opportunity to manipulate the income.
<b>HRA Income</b>	The vast majority of this income relates to dwelling rents where revenue is recognised on a month by month basis in line with the rental agreement.	The income is highly predictable and is broadly known at the beginning of the year based on the number of properties rented out for a known amount. As a result: it is highly unlikely for there to be a material error in the population.
<b>Grant income</b>	Predictable income receipted primarily from central government, including for housing benefits.	Grant income at a local authority typically involves a small number of high value items and an immaterial residual population. These high value items frequently have simple recognition criteria and can be traced easily to third party documentation, most often from central government source data. There is limited incentive or opportunity to manipulate these figures.

# Mandatory communications - additional reporting


## Going concern

Under NAO guidance, including Practice Note 10 - A local authority's financial statements shall be prepared on a going concern basis; this is, the accounts should be prepared on the assumption that the functions of the authority will continue in operational existence for the foreseeable future. Transfers of services under combinations of public sector bodies (such as local government reorganization) do not negate the presumption of going concern.






However, financial sustainability is a core area of focus for our Value for Money opinion.

## Additional reporting

Your audit is undertaken to comply with the Local Audit and Accountability Act 2014 which gives the NAO the responsibility to prepare an Audit Code (the Code), which places responsibilities in addition to those derived from audit standards on us. We also have responsibilities which come specifically from acting as a component auditor to the NAO. In considering these matters at the planning stage we indicate whether:

Work is completed throughout our audit and we can confirm the matters are progressing satisfactorily 	We have identified issues that we may need to report 	Work is completed at a later stage of our audit so we have nothing to report 
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We have summarised the status of all these various requirements at the time of planning our audit below and will update you as our work progresses:

Type	Status	Response
Our declaration of independence		No matters to report. The engagement team and others in the firm, as appropriate, have complied with relevant ethical requirements regarding independence.
Issue a report in the public interest		We are required to consider if we should issue a public interest report on any matters which come to our attention during the audit. We have not identified any such matters to date.
Provide a statement to the NAO on your consolidation schedule		This "Whole of Government Accounts" requirement is fulfilled when we complete any work required of us by the NAO to assist their audit of the consolidated accounts of DLUHC.
Provide a summary of risks of significant weakness in arrangements to provide value for money		We are required to report significant weaknesses in arrangements. Work to be completed at a later stage.
Certify the audit as complete		We are required to certify the audit as complete when we have fulfilled all of our responsibilities relating to the accounts and use of resources as well as those other matters highlighted above.

# Mandatory communications

Type	Statements
<b>Management’s responsibilities (and, where appropriate, those charged with governance)</b>	<p>Prepare financial statements in accordance with the applicable financial reporting framework that are free from material misstatement, whether due to fraud or error.</p> <p>Provide the auditor with access to all information relevant to the preparation of the financial statements, additional information requested and unrestricted access to persons within the entity.</p>
<b>Auditor’s responsibilities</b>	<p>Our responsibilities set out through the NAO Code (communicated to you by the PSAA) and can be also found on their website, which include our responsibilities to form and express an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.</p>
<b>Auditor’s responsibilities – Fraud</b>	<p>This report communicates how we plan to identify, assess and obtain sufficient appropriate evidence regarding the risks of material misstatement of the financial statements due to fraud and to implement appropriate responses to fraud or suspected fraud identified during the audit.</p>
<b>Auditor’s responsibilities – Other information</b>	<p>Our responsibilities are communicated to you by the PSAA and can be also found on their website, which communicates our responsibilities with respect to other information in documents containing audited financial statements. We will report to you on material inconsistencies and misstatements in other information.</p>
<b>Independence</b>	<p>Our independence confirmation at page 25 discloses matters relating to our independence and objectivity including any relationships that may bear on the firm’s independence and the integrity and objectivity of the audit engagement partner and audit staff.</p>

# Tendring District Council

## DRAFT - Value for money risk assessment

### Our approach

Year ended 31 March 2025

March 2025

# Value for money

**For 2024/25 our value for money reporting requirements have been designed to follow the guidance in the Audit Code of Practice.**

Our responsibility to conclude on significant weaknesses in value for money arrangements is unchanged.

The main output remains a narrative on each of the three domains, summarising the work performed, any significant weaknesses and any recommendations for improvement.

We have set out the key methodology and reporting requirements on this slide and provided an overview of the process and reporting on the following page.

## Risk assessment processes

Our responsibility remains to assess whether there are any significant weaknesses in the Council's arrangements to secure value for money. Our risk assessment will continue to consider whether there are any significant risks that the Council does not have appropriate arrangements in place.

In undertaking our risk assessment we will be required to obtain an understanding of the key processes the Council has in place to ensure this, including financial management, risk management and partnership working arrangements. We will complete this through review of the Council's documentation in these areas and performing inquiries of management as well as reviewing reports, such as internal audit assessments.

## Reporting

As with the prior year our approach to value for money reporting aligns to the NAO guidance and includes:

- A summary of our commentary on the arrangements in place against each of the three value for money criteria, setting out our view of the arrangements in place compared to industry standards;
- A summary of any further work undertaken against identified significant risks and the findings from this work; and
- Recommendations raised as a result of any significant weaknesses identified and follow up of previous recommendations.

The Council will be required to publish the commentary on its website at the same time as publishing its annual report online.

**Financial sustainability**

*How the body manages its resources to ensure it can continue to deliver its services.*

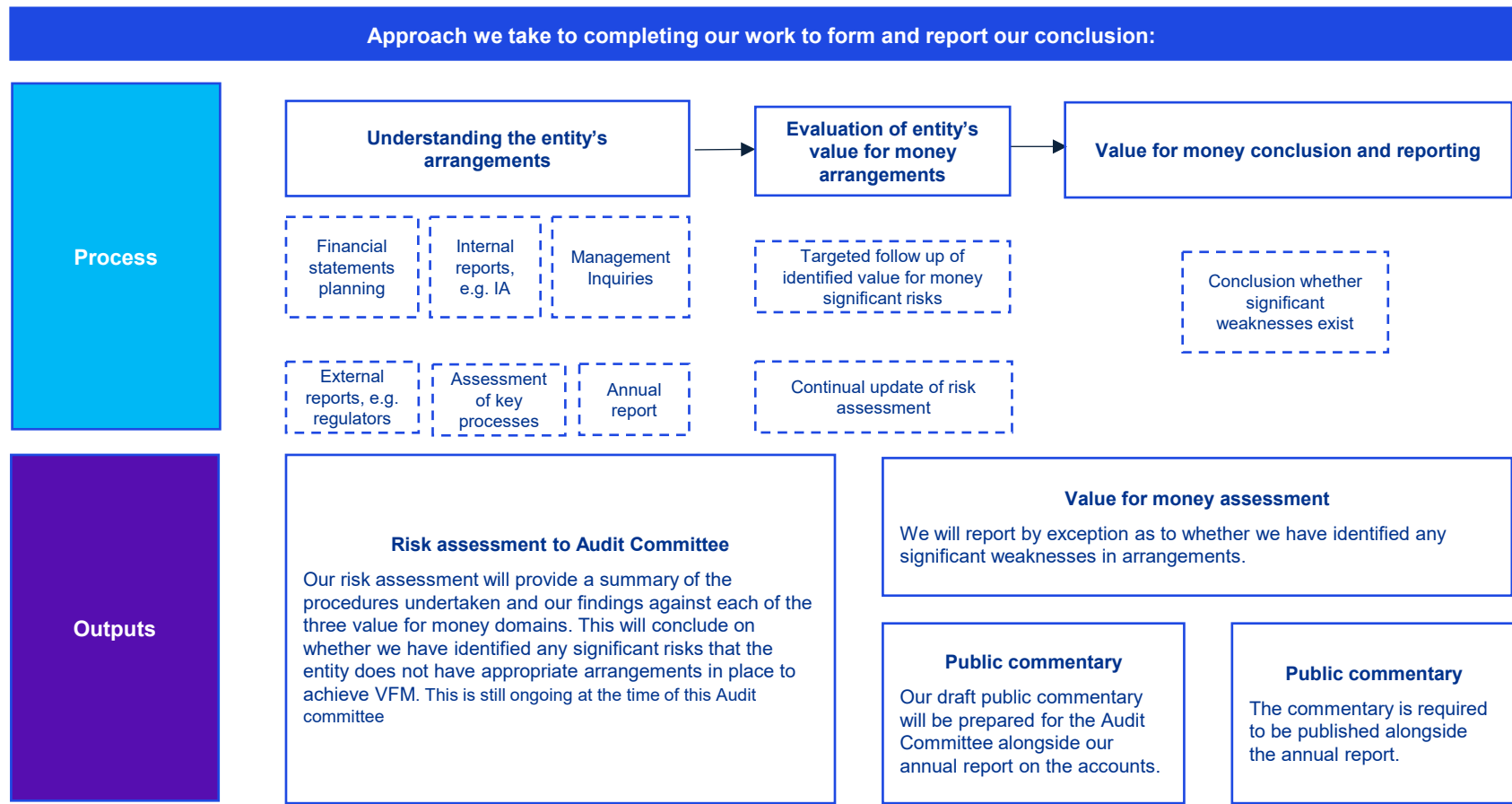
**Governance**

*How the body ensures that it makes informed decisions and properly manages its risks.*

**Improving economy, efficiency and effectiveness**

*How the body uses information about its costs and performance to improve the way it manages and delivers its services.*

# Value for money



# Value for money

## Summary of work to date

We have not completed our risk assessment for value for money at the date of reporting and we will provide our full risk assessment at the next Audit Committee.



# Appendix

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# Audit team and rotation

Your audit team has been drawn from our specialist local government audit department and is led by key members of staff who will be supported by auditors and specialists as necessary to complete our work. We also ensure that we consider rotation of your audit partner and firm.

	<p>Emma is the director responsible for our audit. They will lead our audit work, attend the Audit Committee and be responsible for the opinions that we issue.</p>		<p>Jodie is the manager responsible for our audit. They will co-ordinate our audit work, attend the Audit Committee and ensure we are co-ordinated across our accounts and VFM work.</p>
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To comply with professional standard we need to ensure that you appropriately rotate your external audit partner. There are no other members of your team which we will need to consider this requirement for:



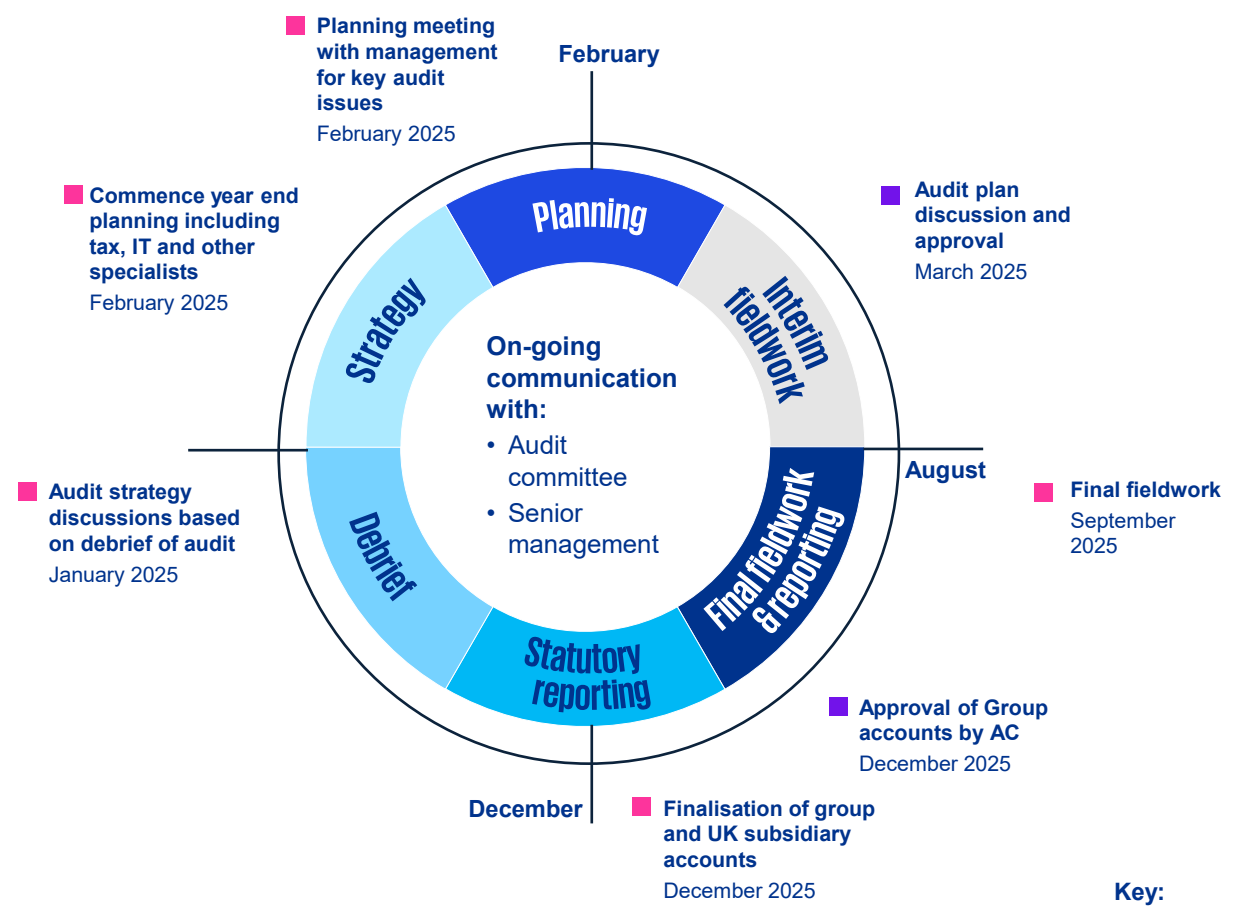
This will be director's second year as your engagement lead. They are required to rotate every five years, extendable to seven with PSAA approval.

# Audit cycle & timetable

## Our schedule 01 2025 – 12 2025

We have worked with management to generate our understanding of the processes and controls in place at the Council in its preparation of the Statement of Accounts.

We have agreed with management an audit cycle and timetable that reflects our aim to sign our audit report by December 2025.



**Key:**

- Timing of AC communications
- Key events

# Fees

## Audit fee

Our fees for the year ending 31 March 2025 are set out in the PSAA Scale Fees communication and are shown below.

Entity	2023/24 (£'000)	2024/25 (£'000)
Statutory audit	162	177
ISA315r	9	-
Fee variations	18	TBC
<b>TOTAL</b>	<b>189</b>	<b>177</b>

As per PSAA’s Scale Fees Consultation, the fees assume no significant risks are identified as part of the Value for Money risk assessment. Additional fees in relation to these areas will be subject to the fees variation process as outlined by the PSAA.

## Billing arrangements

Fees will be billed in accordance with the milestone completion phasing that has been communicated by the PSAA.

## Basis of fee information

Our fees are subject to the following assumptions:

- The entity’s audit evidence files are completed to an appropriate standard (we will liaise with you separately on this);
- Draft statutory accounts are presented to us for audit subject to audit and tax adjustments;
- Supporting schedules to figures in the accounts are supplied;
- The entity’s audit evidence files are completed to an appropriate standard (we will liaise with management separately on this);
- A trial balance together with reconciled control accounts are presented to us;
- All deadlines agreed with us are met;
- We find no weaknesses in controls that cause us to significantly extend procedures beyond those planned;
- Management will be available to us as necessary throughout the audit process; and
- There will be no changes in deadlines or reporting requirements.

We will provide a list of schedules to be prepared by management stating the due dates together with pro-formas as necessary.

Our ability to deliver the services outlined to the agreed timetable and fee will depend on these schedules being available on the due dates in the agreed form and content.

Any variations to the above plan will be subject to the PSAA fee variation process.

# Confirmation of Independence

We confirm that, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and that the objectivity of the Partner and audit staff is not impaired.

## To the Audit and Risk Committee members

### Assessment of our objectivity and independence as auditor of Tendring District 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.

This letter 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/directors and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. 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 except for those detailed below where additional safeguards are in place.

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

#### Summary of non-audit services

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 on the table on the next page

Description of scope of services	Principal Threats to independence	Safeguards applied	Basis of fee	Value of services delivered in the year ended 31/3/24
Council's Pooling of Housing Capital Receipts Return for 23/24.	Assumption of management responsibilities  Self interest	Standard language on non-assumption of management responsibilities is included in our engagement letter.  The level of fees is not considered to cause a significant self interest threat	Fixed	23/24: £5k



# Confirmation of Independence (cont.)

## Summary of fees

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

### Fee ratio

The ratio of non-audit fees to audit fees for the year is anticipated to be 0.03:1. We do not consider that the total non-audit fees create a self-interest threat since the absolute level of fees is not significant to our firm as a whole.

	2024/25
	£'000
Statutory audit	177
Other Assurance Services	5
<b>Total Fees</b>	<b>182</b>

## Application of the FRC Ethical Standard 2019

We communicated to you previously the effect of the application of the FRC Ethical Standard 2019. That standard became effective for the first period commencing on or after 15 March 2020, except for the restrictions on non-audit and additional services that became effective immediately at that date, subject to grandfathering provisions.

AGN 01 states that when the auditor provides non-audit services, the total fees for such services to the audited entity and its controlled entities in any one year should not exceed 70% of the total fee for all audit work carried out in respect of the audited entity and its controlled entities for that year.

We confirm that as at 15 March 2020 we were not providing any non-audit or additional services that required to be grandfathered.

## 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 and Risk Committee.

## Confirmation of audit independence

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

This report is intended solely for the information of the Audit and Risk Committee of the Group 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.

Yours faithfully

Emma Larcombe

**KPMG LLP**

# KPMG's Audit quality framework

**Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion.**

To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework.

Responsibility for quality starts at the top through our governance structures as the UK Board is supported by the Audit Oversight Committee, and accountability is reinforced through the complete chain of command in all our teams.

**■ Commitment to continuous improvement**

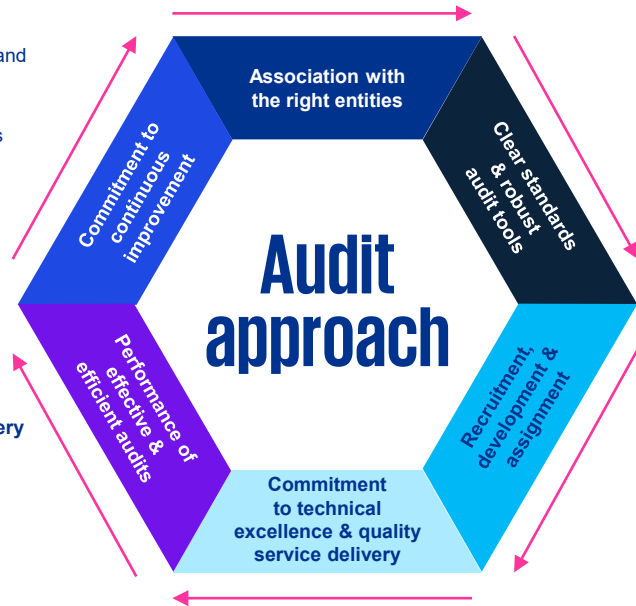
- Comprehensive effective monitoring processes
- Significant investment in technology to achieve consistency and enhance audits
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

**■ Performance of effective & efficient audits**

- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching, including the second line of defence model
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Insightful, open and honest two way communications

**■ Commitment to technical excellence & quality service delivery**

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights



**■ Association with the right entities**

- Select entities within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management

**■ Clear standards & robust audit tools**

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- KPMG Clara incorporating monitoring capabilities at engagement level
- Independence policies

**■ Recruitment, development & assignment of appropriately qualified personnel**

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members and specialists



# Understanding of IT



## Summary

**The release of ISA 315 (UK) revised brought an increased focus on Understanding of IT in the audit, and it continues to be an area of focus.**

Stakeholders now expect auditors to not only understand IT in detail, but also to consider the impact of the findings from their risk assessment procedures on their planned audit approach.

**Why is Understanding of IT so important?**

Businesses continue to embrace increasingly complex and sophisticated IT systems and place more and more reliance on automated IT processing not simply for a competitive advantage, but also for "business as usual" operations.

This increased reliance means that to effectively audit accounts, balances and transactions, auditors are required to understand and challenge more around how those IT system and process work.

Therefore, Understanding of IT is a crucial building block of our audit strategy and influences our planned audit approach at every stage.

This is true regardless of whether controls reliance is planned or the audit is expected to be fully substantive in nature.

**What kind of things might we identify?**

As part of our risk assessment procedures, we perform:

- An assessment of the formality, or otherwise, of certain financially relevant IT processes
- An evaluation of the design and implementation of related general IT controls
- An evaluation of the design and implementation of automated process level controls

As a result of these procedures, we may identify IT control deficiencies or IT process informalities that may have an impact on our planned audit approach.

Additionally, we may identify findings related to the wider control environment or threats to the accuracy or completeness of the information used by both entity management and auditors alike.

**What does this mean for our audits?**

Auditors are being asked to consider the findings from their risk assessment procedures over IT in relation to the planned audit approach.

The findings may impact any area of the audit, however there are three main areas of focus where we anticipate that most impact as a result of identifying IT deficiencies or IT process informality;

- Increased risk to data integrity
- Additional fraud risk factors
- Additional high-risk criteria to be used in journals analysis

It is important to understand that these findings may have an impact regardless of planned reliance on automated controls and general IT controls.



# Newly effective accounting standards and relevant IFRIC items

Standards	Expected impact				Effective for years beginning on or after		Early adoption permitted
	High	Moderate	Low	None	01 Jan 2024	1 Jan 2025	
Lease Liability in a Sale and Leaseback (Amendments to IFRS 16)		●			✓		✓
Classification of liabilities as Current or Non-Current and Non-current Liabilities with Covenants (Amendments to IAS 1 Presentation of Financial Statements)			●		✓		✓
Supplier Finance Arrangements (Amendments to IAS 7 and IFRS 7)			●		✓		✓
Lack of exchangeability (Amendments to IAS 21)			●			✓	✓
Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures) *				○			✓
UK legislation on international tax system reform (BEPS)			●		✓		✓
IFRS S1** General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2** Climate-related Disclosures			●		✓		✓

\* The effective date for these amendments was deferred indefinitely. Early adoption continues to be permitted.

\*\* The implementation and the effective dates of IFRS® Sustainability Disclosure Standards are subject to local regulation

# FRC's areas of focus

The FRC released their [Annual Review of Corporate Reporting 2022/23](#) in October 2023. In addition, they have released three thematic reviews during the year should be considered when preparing reporting for the current financial period.

The reports identify where the FRC believes companies should be improving their reporting. Below is a high level summary of the key topics. We encourage management and those charged with governance to read further on those areas which are significant to the [entity]/[group].



## Reporting on the effects of inflation and other uncertainties

This year's Annual Review of Corporate Reporting identifies that companies continue to face significant economic and geopolitical uncertainty and annual report and accounts should therefore tell a coherent story about the impacts on the business and the assumptions the company has made in preparing the financial statements.

The FRC notes that interest rate rises in response to persistent inflation, the related impact on consumer behaviour, and limited growth present a particularly challenging environment for companies. Financial reporting needs to set out the impact of these issues on their business, and the assumptions which underpin the values of assets and liabilities in financial statements. Significant changes in discount rates and future cash flows are expected as a result and they should be highlighted.

The impacts of uncertainty on companies' narrative reporting and financial statements are numerous, but the FRC sets out its clear disclosure expectations for 2023/2024:

- Disclosures about uncertainty should be sufficient to meet relevant requirements *and* for users to understand the positions taken in the financial statements.
- The strategic report should give a clear description of the risks facing the business, the impact of these risks on strategy, business model, going concern and viability, and disclosures should be cross-referenced to relevant detail in the report and accounts.
- Transparent disclosure should be provided of the nature and extent of material risks arising from financial instruments.

Preparers should take a step back to consider whether the annual report, as a whole, is clear, concise and understandable and whether additional information, beyond the requirements of the standards, is necessary to understand particular transactions, events or circumstances.



## Climate-related reporting

Companies in scope for either UK Climate-related Financial Reporting (through the Companies Act requirements last year) or Taskforce on Climate-Related Disclosures (TCFD) (through listing rules or other regulatory requirements) have now reported for the first time. Companies should be reconsidering these disclosures and reflecting any changes in the business or strategy that have happened since last years reporting, to ensure the disclosure remain relevant and reflects the impact of climate-related risk on the Company.

Climate-related risks remains an area of ongoing focus for the FRC as they embed the review of these disclosures into their routine annual reviews. The FRC has highlighted that it expects companies to provide improved disclosure explaining the linkage between narrative reporting on uncertainties such as climate change, and the assumptions made in the financial statements.

In respect of TCFD disclosures, the FRC notes that sustainability reporting requirements continue to evolve and companies are still at very different stages in their reporting in this area. The FRC expect in scope entities to provide a clear statement of consistency with TCFD which explains, unambiguously, whether management considers they have given sufficient information to comply with the framework in the current year. Companies must, in any case, comply with the new mandatory requirements for disclosure of certain TCFD-aligned information.

In relation to the specific thematic on metrics and targets they highlighted five areas of improvement:

- the definition and reporting of company-specific metrics and targets, beyond headline 'net zero' statements;
- better linkage between companies' climate-related metrics and targets and the risks and opportunities to which they relate;
- the explanation of year-on-year movements in metrics and performance against targets;
- transparency about internal carbon prices, where used by companies to incentivise emission reduction; and
- better linkage between climate-related targets reported in TCFD disclosures and ESG targets disclosed in the Directors' Remuneration Report.

# FRC's areas of focus (cont.)

## Impairment of assets

Heightened economic uncertainty, high inflation and higher interest rates have resulted in more instances of impairment or reductions in headroom, prompting the need for more detailed disclosures under IAS 36. The FRC notes that many of the queries it has raised with companies in the past year would have been avoided by clearer, more complete disclosures.

Disclosures should provide key inputs and assumptions applied, along with relevant values and sensitivity information where impairments could arise from reasonably possible changes in assumptions.

Assumptions and sensitivities should be consistent with information provided elsewhere in the annual report, including those related to climate and other commitments, and with the wider economic environment; where there are inconsistencies, these should be explained.

Discount rates should be consistent with the assumptions in the cash flow projections, particularly in respect of risk and the effects of inflation.

## Judgements and estimates

Providing quality disclosures in this area remains particularly important in the light of ongoing economic and political uncertainty. The FRC has noted that often disclosures did not contain sufficient information about the key assumptions or appeared inconsistent with disclosures given elsewhere in the annual report.

Disclosures should explain the significant judgements made and provide quantified sensitivities where there is a significant source of estimation uncertainty. This includes judgements and estimates relating to the going concern assessment and accounting for inflationary features, including the use of discount rates. Significant estimates should be reassessed each year and changes to assumptions explained.

The FRC highlights the need for disclosures to clearly distinguish between estimates with a significant risk of a material adjustment to carrying amounts within the next year, and other sources of estimation uncertainty.

## Cash flow statements

Cash flow statements have again been an area where the FRC have raised many queries and it remains one of the most common causes of prior year adjustments. Most queries raised by the FRC relate to unusual or complex transactions which have not been appropriately reflected in the cash flow statement.

Companies should ensure that descriptions of cash flows are consistent with those reported elsewhere in the report and accounts, with non-cash investing and financing transactions being excluded, but disclosed elsewhere if material.

In addition, companies should ensure that cash flows are appropriately classified between operating, financing and investing, and cash flows should not be inappropriately netted. Cash and cash equivalents should comply with the relevant definitions and criteria in the standard.

## Strategic report and other Companies Act 2006 matters

Strategic reports should focus not only on financial performance but should also explain significant movements in the balance sheet and cash flow statement. They should articulate the effect of principal risks and uncertainties facing the business, including economic and other risks such as inflation, rising interest rates, supply chain issues, climate-related risks and labour relations.

In addition, the FRC reminds companies that they should comply with the legal requirements for making distributions and repurchasing shares including, where relevant, the requirement to file interim accounts to support the transaction.

## Financial instruments

Companies should ensure that the nature and extent of material risks arising from financial instruments (including inflation and rising interest rates), and related risk management, are adequately disclosed.

This includes disclosures being sufficient to explain the approach and significant assumptions applied in the measurement of expected credit losses, including concentrations of risk, and assessments should be reviewed and adjusted for forecast future economic conditions.

The effect of refinancing and changes to covenant arrangements should be explained, with information about covenants being provided unless the likelihood of a breach is remote.

Lastly, the FRC reminds companies that cash and overdraft balances should be offset only when the qualifying criteria have been met.

# FRC's areas of focus (cont.)

## Income taxes

Following their thematic review last year, the FRC reminds companies that the nature of evidence supporting the recognition of deferred tax assets should be disclosed, and should factor in any difficult economic environment.

Additionally, companies should ensure tax-related disclosures are consistent throughout the annual report, uncertain tax positions are adequately disclosed, and material reconciling items in the tax rate reconciliation are presented separately and appropriately described.

## Provisions and contingencies

Clear descriptions of the nature and uncertainties for material provisions or contingent liabilities, the expected timeframe and the basis for estimating the probable or possible outflow should be provided.

Inputs used in measuring provisions should be consistent in the approach to incorporating inflation, and details of related assumptions should be provided.

## Revenue

Where variable consideration exists, companies should provide sufficient disclosure to explain how it is estimate and constrained.

Accounting policies and relevant judgement disclosures should be provided for all significant performance obligations. Those disclosures should address in sufficient detail the timing of revenue recognition, the basis for recognising revenue over time and the methodology applied.

Lastly, the FRC reminds companies that inflationary features in contracts with customers, and the accounting for such clauses, should be adequately disclosed and clearly explained.

## Presentation of financial statements and related disclosures

The FRC expects companies to disclose company-specific information to meet the overall disclosure objectives of relevant accounting standards, and not just the narrow specific disclosure requirements of individual standards. They set out a clear expectation that additional information (beyond the minimum requirements of the standards) should be included where needed.

## Fair value measurement

Fair value measurement has returned this year as one of the FRC's top ten issues raised in their correspondence with companies, and this has been the topic of a [thematic review](#). Common queries raised include the omission of sensitivity disclosures and the quantification of unobservable inputs into fair value measurements.

The FRC reminds companies that they should use market participants' assumptions, rather than their own, in measuring fair value.

## Thematic reviews

Over the past year FRC has issued Thematic reviews on the following topics:

- Climate-related metrics and targets
- IFRS 13 Fair value measurement
- IFRS 17 Insurance contracts – Interim disclosures in the first year of application
- Reporting by the UK's largest private companies

## 2023/24 review priorities

The FRC has indicated that its 2023/24 reviews will focus on the following sectors which are considered by the FRC to be higher risk by virtue of economic or other pressures:

-  Travel, hospitality and leisure
-  Retail and personal goods
-  Construction materials
-  Gas, water and multi-utilities



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