

# Audit Progress Report and Sector Update

Plymouth City Council Year ending 31 March 2020

March 2021



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# Introduction

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This paper provides the Audit and Governance Committee with a report on progress in delivering our responsibilities as your external auditors.

The paper also includes a summary of emerging national issues and developments that may be relevant to you as a local authority.

Members of the Audit and Governance Committee can find further useful material on our website, where we have a section dedicated to our work in the public sector. Here you can download copies of our publications [www.grantthornton.co.uk](http://www.grantthornton.co.uk).

If you would like further information on any items in this briefing, or would like to register with Grant Thornton to receive regular email updates on issues that are of interest to you, please contact either Paul or Geraldine.

# Progress at March 2021 - Financial Statements Audit

## Financial Statements Audit

We began our planning for the 2019/20 audit in January 2020. Our interim work was largely undertaken across March and April.

Our interim fieldwork included:

- updated review of the Council's control environment;
- updated understanding of financial systems;
- review of Internal Audit reports on core financial systems;
- early work on emerging accounting issues,
- early substantive testing.
- discussions on emerging technical matters.

We issued a detailed audit plan, following the conclusion of planning and interim work in early April and presented this to the 11<sup>th</sup> May 2020 Audit and Governance Committee.

As a result of the Covid-19 pandemic, the deadline for the submission of the draft financial statements was put back to the 31<sup>st</sup> August 2020. We received the draft financial statements on 31<sup>st</sup> August 2020. We commenced our substantive audit work on 7<sup>th</sup> September 2020.

Since then our work has been ongoing. The target deadline, as set by MHCLG, for the audit opinion was 30<sup>th</sup> November 2020. During the course of our audit work and testing we have had to undertake additional audit procedures and testing. These are primarily in the areas of PPE valuations, government grants and grants received in advance, financial instruments and fair values, journals, debtors and creditors. The audit has been protracted as a result of working remotely as a result of the pandemic. It has also been protracted as a result of regulatory pressures to increase substantive testing across all significant areas as detailed above. The council has also had to work remotely throughout the course of this audit, whilst having to respond to additional duties and obligations as set by central government as, for example, the administration of a number of Covid – 19 related grants. It has proved difficult at times, to obtain core documentation for areas such as debtors, creditors, journals, income and expenditure and financial instruments testing.

We will also have to undertake further audit testing on post year end receipts of debtors, post year end payments for creditors, financial instruments fair value assessments, the Council's calculation of its Minimum Revenue Provision (MRP), the Council's calculation of its Capital Financing Reserve (CFR); the Council's going concern assessment and related cashflows. Our work is ongoing and further details of progress against the significant risks identified in the audit plan are provided in slides 6 -12.

Our original audit plan, as presented to the 11<sup>th</sup> May 2020 Audit and Governance Committee, reported the following areas of focus :

Valuation of property, plant and equipment (Inc Investment Properties)

Valuation of the Pension Liability

Reduction of the net Pension Liability through the use of Miel Ltd.

Accounting treatment for Government Grants

Management over-ride of controls through journals testing

Financial Instruments.

## Audit Plan – Revision February 2021

## Governance Review

Over the course of the 2018/19 financial statements audit we made a series of recommendations to both management and the Audit and Governance Committee regarding the Miel transaction. These recommendations were made - 22 July 2019; 23<sup>rd</sup> September 2019; 9 December 2019; and 2 April 2020. Whilst one of these recommendations was related to the need to obtain accounting advice for the transaction, the remaining items were of a governance nature. We recommended that the Council:

- obtain independent actuarial advice regarding the estimated pension liability amount
- obtain independent financial advice from financial advisers regarding the available options to the Council and consideration of all business case options including value for money

# Progress at March 2021 – 2019/20 Audit

## Audit Plan – Revision February 2021

### Governance Review Contd.

- obtain independent legal advice as to the legality of the transaction including borrowing from PWLB to transact the payment of the pension fund liability
- obtain independent due diligence on any companies or company structures that may be used to transact the payment – paying particular attention to any complexities and risks associated with the Financial Conduct Authority regulations
- obtain advice regarding the use of any company in the transaction;
- update the business plan and re present to Members
- obtain independent accounting advice and
- ensure that detailed due diligence, business cases, financial information and decision.

Our review of the progress made against these recommendations has concluded that we have not yet gathered sufficient evidence to support that these have been enacted.

In April 2020, the Council entered into an interest rate swap transaction. Our initial enquiries have determined that the governance and due diligence arrangements in place for both of these transactions now requires further scrutiny by us as auditors.

We have therefore updated our original plan as issued in May 2020, to include a specific review of the governance and due diligence arrangements regarding these transactions.

Our review has commenced and we aim to report the conclusions of this review at the next scheduled Audit and Governance Committee.

## Value for Money Audit

At the Audit and Governance Committee on 21 September 2020 we reported our initial findings of our value for money review for 2019/20. We continue to update our review and will incorporate our findings of the governance review, as detailed above, in our Audit Findings Report for 2019/20.

### Other areas

#### Certification of claims and returns

*Housing Benefit Subsidy claim* - in accordance with procedures agreed with the Department for Work and Pensions (DWP). The Council have completed the initial testing and we have reviewed a sample of cases to verify accuracy. Additional testing is currently being undertaken by the Council following the identification of errors from the initial testing.

The DWP has moved the reporting deadline back to 31 January 2021 with extensions being granted to April 2021. The Council have requested an extension for April 2021. The DWP have granted this extension and our testing continues. We are currently reperforming testing undertaken by the Council relating to the errors identified in the Housing Benefits claim for 2018/19.

We will report our findings at the next scheduled Audit and Governance Committee.

*Teachers Pension's claim* – We have completed our audit of the Teachers Pension's claim.

#### Meetings

We meet with Finance Officers on a weekly basis and regularly discuss the progress of the audit and emerging findings and issues.

# Significant Risks - Progress at March 2021

Significant risk	Planned approach	Progress
<p><b>Covid- 19</b></p> <p>The global outbreak of the Covid-19 virus pandemic has led to unprecedented uncertainty for all organisations, requiring urgent business continuity arrangements to be implemented.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>work with management to understand the implications the response to the Covid-19 pandemic has on the organisation's ability to prepare the financial statements and update financial forecasts and assess the implications on our audit approach;</li> <li>liaise with other audit suppliers, regulators and government departments to co-ordinate practical cross sector responses to issues as and when they arise;</li> <li>evaluate the adequacy of the disclosures in the financial statements in light of the Covid-19 pandemic;</li> <li>evaluate whether sufficient audit evidence using alternative approaches can be obtained for the purposes of our audit whilst working remotely;</li> <li>evaluate whether sufficient audit evidence can be obtained to corroborate significant management estimates such as asset valuations</li> <li>evaluate management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment; and</li> <li>discuss with management any potential implications for our audit report if we have been unable to obtain sufficient audit evidence.</li> </ul>	<p>We have:</p> <ul style="list-style-type: none"> <li>worked with management to understand the implications the response to the Covid-19 pandemic had on the Council's ability to prepare the financial statements and update financial forecasts and assessed the implications for our materiality calculations. No changes have been made to materiality levels previously reported.</li> <li>liaised with other audit suppliers, regulators and government departments to co-ordinate practical cross-sector responses to issues as and when they arose. Examples include the material uncertainty disclosed by the Council's property valuation expert;</li> <li>evaluated the adequacy of the disclosures in the financial statements that arose in light of the Covid-19 pandemic; and</li> <li>engaged the use of auditor experts for all asset valuations, including the Tamar Bridge</li> </ul> <p>We are:</p> <ul style="list-style-type: none"> <li>ensuring to obtain sufficient audit evidence through remote technology;</li> <li>evaluating whether sufficient audit evidence can be obtained to corroborate significant management estimates such as assets;</li> <li>evaluating management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment.</li> <li>testing the recoverability of debts and the impact of the pandemic on bad debts in general</li> </ul>

# Significant Risks - Progress at March 2021

Significant risk	Planned approach	Progress
<p><b>Fraud in revenue and expenditure recognition</b></p> <p>Under ISA (UK) 240, there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue.</p> <p>This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.</p>	<p>Having considered the risk factors set out in ISA (UK) 240, and the nature of the revenue streams at the Authority, we have determined that the risk of fraud arising from revenue recognition can be rebutted in all areas.</p> <p>The exception to this is in relation to the accounting treatment in government grants due to issues arising in 2018/19 and 2017/18. This was not a significant risk in these years.</p>	<p>We have not identified any changes to our assessment reported in the audit plan.</p> <p>We have:</p> <ul style="list-style-type: none"><li>• evaluated the design effectiveness of management controls over grant recognition;</li><li>• analysed the detailed transaction listings for grants received in advance and government grants</li><li>• tested, on a sample basis, grants received in advance, including capital grants and government grant transactions</li><li>• been able to obtain supporting documentation relating to grants including, where relevant, conditions relating to the use of the grant. We are currently awaiting evidence for some capital grants selected</li><li>• tested, where evidence has been provided, receipt of the grant.</li></ul> <p>We are currently awaiting evidence to support the release of grants applied in year to ensure that conditions have been satisfactorily met.</p>

# Significant Risks - Progress at March 2021

Significant risk	Planned approach	Progress
<p><b>Management override of controls</b></p> <p>Under ISA (UK) 240, there is a non-rebuttable presumed risk that the risk of management override of controls is present in all entities. The Authority faces external scrutiny of its spending and this could potentially place management under undue pressure in terms of how they report performance.</p> <p>We therefore identified management override of control, in particular journals, management estimates, and transactions outside the course of business as a significant risk for the authority which was one of the most significant assessed risks of material misstatement.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>• evaluate the design effectiveness of management controls over journals;</li> <li>• analyse the journals listing and determine the criteria for selecting high risk and unusual journals;</li> <li>• test unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration;</li> <li>• gain an understanding of the accounting estimates and critical judgements applied made by management and consider their reasonableness with regard to corroborative evidence; and</li> <li>• evaluate the rationale for any changes in accounting policies, estimates or significant unusual transactions.</li> </ul>	<p>We have:</p> <ul style="list-style-type: none"> <li>• evaluated the design effectiveness of management controls over journals; and</li> <li>• analysed the journals listing and determine the criteria for selecting high risk and unusual journals.</li> <li>• analysing and selecting those journals that will require further testing.</li> <li>• tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration;</li> <li>• Identified that in some instances, journals have been processed and authorised by the same officer. Although there is a retrospective process in place to ensure that an independent officer reviews the processing of the journal, in some instances, we have found that this has not always been applied. As a result we have had to undertake further, detailed testing on journals transactions.</li> <li>• Identified that in some instances, journals have been both processed and authorised by senior officers of the Council's finance team. As a result, we have had to undertake further, detailed testing on these journals</li> <li>• gained an understanding of the accounting estimates and critical judgements applied made by management and consider their reasonableness with regard to corroborative evidence; and</li> <li>• evaluating the rationale for any changes in accounting policies, estimates or significant unusual transactions.</li> </ul> <p>We are currently undertaking additional testing on journals processed and authorised by the same officer.</p> <p>We are currently undertaking additional testing on those journals processed and authorised by senior officers of the finance team.</p>



# Significant Risks - Progress at March 2021

Significant risk	Planned approach	Progress
<p><b>Valuation of land and buildings Including investment properties</b></p> <p>The Council re-values its land and buildings on a five-yearly rolling basis to ensure that carrying value is not materially different from fair value. This represents a significant estimate by management in the financial statements due to the size of the numbers involved, and the sensitivity of the estimate to changes in key assumptions.</p> <p>Additionally, management will need to ensure the carrying value of assets not revalued as at 31 March 2020 in the Authority's financial statements is not materially different from the current value at the financial statements date, where a rolling programme is used.</p> <p>We identified the valuation of land and buildings and investment properties, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement, and a key audit matter.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>• evaluate management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work;</li> <li>• evaluate the competence, capabilities and objectivity of the valuation expert;</li> <li>• discuss with or write to the relevant valuer to confirm the basis on which the valuation was carried out;</li> <li>• engage our own valuer expert, Wilks Head and Eve, to provide commentary on: <ul style="list-style-type: none"> <li>• the instruction process in comparison to requirements from CIPFA/ IFRS / RICS; and</li> <li>• the valuation methodology and approach, resulting assumptions adopted and any other relevant points;</li> </ul> </li> <li>• challenge the information and assumptions used by the valuer to assess completeness and consistency with our understanding;</li> <li>• test revaluations made during the year to see if they had been input correctly into the Authority's asset register; and</li> <li>• evaluate the assumptions made by the management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value at year end.</li> </ul>	<p>We have :</p> <ul style="list-style-type: none"> <li>• evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work;</li> <li>• evaluated the competence, capabilities and objectivity of the valuation expert;</li> <li>• written to the relevant valuers to confirm the basis on which the valuation was carried out; and</li> <li>• engaged our own valuer expert, Wilks Head and Eve, and our own internal valuer for the Tamar Bridge valuation, to provide commentary on: <ul style="list-style-type: none"> <li>• the instruction process in comparison to requirements from CIPFA/ IFRS / RICS; and</li> <li>• the valuation methodology and approach, resulting assumptions adopted and any other relevant points.</li> </ul> </li> <li>• challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding;</li> <li>• evaluated the assumptions made by management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value at year end.</li> <li>• tested revaluations made during the year to see if they had been input correctly into the Council's asset register.</li> <li>• challenged the assumptions of the valuer for those assets not valued in year. Those assets either not valued in year or valued as at 31 December 2020 fall into two categories – those valued on a depreciated replacement cost (DRC) and those valued on an existing use basis (EUV). For these assets we have obtained relevant industry assumptions and indices from the valuer.</li> </ul> <p>We are currently in the process of reviewing the assumptions for assets not valued in year and will liaise with our own valuation expert.</p>

# Significant Risks - Progress at March 2021

Significant risk	Planned approach	Progress
<p><b>Valuation of pension fund net liability</b></p> <p>The pension fund net liability, as reflected in the Authority's balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements.</p> <p>The pension fund net liability is considered a significant estimate due to the size of the numbers involved and the sensitivity of the estimate to changes in key assumptions.</p> <p>We therefore identified valuation of the Authority's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement, and a key audit.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>• update our understanding of the processes and controls put in place by management to ensure that the Council's pension fund net liability is not materially misstated and evaluate the design of the associated controls;</li> <li>• evaluate the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work;</li> <li>• assess the competence, capabilities and objectivity of the actuary who carried out the Council's pension fund valuation;</li> <li>• assess the accuracy and completeness of the information provided by the Council to the actuary to estimate the liability;</li> <li>• test the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary; and</li> <li>• undertake procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report.</li> </ul>	<p>We have:</p> <ul style="list-style-type: none"> <li>• updated our understanding of the processes and controls put in place by management to ensure that the Council's pension fund net liability is not materially misstated and evaluate the design of the associated controls;</li> <li>• evaluated the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work; and</li> <li>• assessed the competence, capabilities and objectivity of the actuary who carried out the Council's pension fund valuation.</li> <li>• assessed the accuracy and completeness of the information provided by the Council to the actuary to estimate the liability;</li> <li>• tested the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary; and</li> <li>• undertaken procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report.</li> </ul> <p>We are in the process of testing the experienced items within the pension fund liability and the adjustments made by the actuary for the updated Mc Cloud liability and pension guarantees.</p>

# Significant Risks - Progress at March 2021

Significant risk	Planned approach	Progress
<p><b>Reduction of the net pension fund liability through the use of Miel Ltd</b></p> <p>As noted on the previous page, the Authority's pension fund net liability represents a significant estimate in the financial statements.</p> <p>The Authority has used a separate vehicle (Miel Ltd) to pay a £73m off of its Pension Fund liability amount. This transaction took place in early October 2019.</p> <p>This type of transaction is both material and unusual and has therefore been assessed as a Financial Statements significant risk.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>review the Council's response to the series of recommendations that we have made in our Audit Findings Reports throughout 2018/19, in particular to -</li> <li>assess the due diligence undertaken by the Authority</li> <li>review the action taken by the Authority to ensure the transaction's legality, supplementing this with our own independent legal advice where appropriate</li> <li>assess the arrangements the Authority has in place to assess whether it considers the transaction to reduce the pension fund net liability to be financially sound.</li> <li>review the Authority's proposed accounting treatment to ensure it is compliant with CIPFA's Code and the relevant accounting standards.</li> </ul>	<p>We have reviewed the responses to our series of recommendations made in our 2018/19 Audit Findings Report including due diligence undertaken, legality reviews and advice and the arrangements put in place to establish the financial viability of the Transaction.</p> <p>As a result of our review we are now undertaking a specific review of the governance and due diligence arrangements regarding both this transaction and the Interest rate swap transaction in April 2020.</p> <p>We have reviewed the proposed accounting treatment for the Miel Pension Liability transaction. As a result of this review, the Council have commissioned a review of the appropriate accounting treatment and we currently await the outcome of this and the associated adjustments to the draft financial statements.</p> <p>As a result of our detailed technical review of the accounting treatment we are also undertaking detailed testing on the calculation of the Council's MRP provision and the calculation of the Council's capital financing requirement.</p> <p>Should amendments to the draft financial statements be required, there will be a number of entries that will require adjustment throughout the statements and these will require time to both process and review</p>

# Significant Risks - Progress at March 2021

Significant risk	Planned approach	Progress
<p><b>Financial Instrument Disclosure notes</b></p> <p>Accounting standards and the CIPFA Code require detailed disclosure notes to be published in the accounts regarding financial instruments held by the Council. These financial instruments can be in the form of loans and borrowings as well as assets and investments. Arriving at the fair value of financial instruments is usually complex and requires specialist support as part of the valuation process for these items.</p> <p>In 2018/19 the Council's draft financial statements did not include the required detail or disclosures relating to all financial instruments held by the Council. Further detailed work had to be performed by the Council and its advisers to ensure that the financial instrument notes were in accordance with regulation and guidance. As this is a complex area and requires specialist support and advice, it is susceptible to possible error.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>• review the Council's processes implemented to establish the correct valuations of all material financial instruments held.</li> <li>• Test disclosures for financial instruments back to the figures within the main financial statements</li> <li>• Test the disclosures in accordance with the CIPFA Code and accounting and auditing guidance</li> <li>• Review the work of the Council's experts in this area.</li> </ul>	<p>We have :</p> <ul style="list-style-type: none"> <li>- undertaken a detailed technical review of the Financial Instruments disclosures. This has highlighted a number of changes that are required and will be processed by the Council</li> <li>- obtained detailed evidence and accounting treatment support for the CCLA investment vehicle. This has highlighted a number of errors within the disclosures and accounts and the Council will be amending for these.</li> <li>-tested material disclosures and material fair values for investments and loans. We are currently awaiting further evidence to support the fair value assumptions disclosed, the underlying assumptions regarding how investment and liability categories are determined, supporting data and information supplied to the Council's fair value experts and further details of the assumptions made by the Council's experts.</li> </ul>

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## Other risks identified

### Other audit areas

In addition to our work on the significant risks, work is also in progress in the following areas, some of these are subject to Grant Thornton UK LLP review:

- PPE additions – Completed
- Cash – year end balancing items and controls account require further testing
- Expenditure (including welfare expenditure) - completed
- Employee benefits – completed.
- Debtors and bad debt provision – further testing to be undertaken
- Creditors – completed.
- Leases – completed.
- Reserves – further review to be undertaken as a result of amendments to the accounts
- Financial instruments, investments and borrowings – currently ongoing
- PFI liabilities – completed.
- Provisions - ongoing
- Financial statements disclosures – testing ongoing
- Pooled budgets – completed.
- Related parties – ongoing.
- Going concern – a revised going concern statement will be requested from the Council. Further, detailed cashflow forecasts 12 months from the audit opinion date will be required prior to the audit opinion being issued.
- Annual Governance Statement – a further review of the annual governance will be undertaken following our governance review.

# Audit deliverables

2019/20 Deliverables	Planned Date	Status
<b>Fee Letter</b> <ul style="list-style-type: none"><li>• Confirming PSAA audit fee for 2019/20.</li><li>• Advise of additional fee for 2019/20</li><li>• Final Audit Fee</li></ul>	April 2020 April 2020 May 2021	Complete Complete To be agreed
<b>Accounts Audit Plan</b> <p>We are required to issue a detailed accounts audit plan to the Audit and Governance Committee setting out our proposed approach in order to give an opinion on the Council's 2019-20 financial statements.</p>	April 2020	Complete
<b>Interim Audit Findings</b> <p>We will report to you the findings from our interim audit and our initial value for money risk assessment within our Progress Report.</p>	May 2020	Complete
<b>Audit Findings Report</b> <p>The Audit Findings Report will be reported to the November Audit and Governance Committee.</p>	November 2020	To be agreed.
<b>Auditors Report</b> <p>This is the opinion on your financial statement, annual governance statement and value for money conclusion.</p>	November 2020	To be agreed
<b>Annual Audit Letter</b> <p>This letter communicates the key issues arising from our work.</p>	January 2021	To be agreed

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# Sector update

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Councils continue to try to achieve greater efficiency in the delivery of public services, whilst facing the challenges to address rising demand, ongoing budget pressures and social inequality.

Our sector update provides you with an up to date summary of emerging national issues and developments to support you. We cover areas which may have an impact on your organisation, the wider local government sector and the public sector as a whole. Links are provided to the detailed report/briefing to allow you to delve further and find out more.

Our public sector team at Grant Thornton also undertake research on service and technical issues. We will bring you the latest research publications in this update. We also include areas of potential interest to start conversations within the organisation and with Audit and Governance Committee members, as well as any accounting and regulatory updates.

- [Grant Thornton Publications](#)
- [Insights from local government sector specialists](#)
- [Reports of interest](#)
- [Accounting and regulatory updates](#)

More information can be found on our dedicated public sector and local government sections on the Grant Thornton website by clicking on the logos below:



Public Sector



Local  
government

# New NAO Code of Audit Practice for 2020-21

The NAO issued a new Code of Audit Practice which came into force on 1 April 2020 and applies to audits of 2020-21. The key change is an extension to the framework for VfM work. The NAO has prepared Auditor Guidance Note (AGN 03), which sets out detailed guidance on what VfM work needs to be performed. Public consultation on this ended 2 September.

The new approach to VfM re-focuses the work of local auditors to:

- promote more timely reporting of significant issues to local bodies;
- provide more meaningful and more accessible annual reporting on VfM arrangements issues in key areas;
- provide a sharper focus on reporting in the key areas of financial sustainability, governance, and improving economy, efficiency and effectiveness; and
- provide clearer recommendations to help local bodies improve their arrangements.

Under the previous Code, auditors had only to undertake work on VfM where there was a potential significant risk and reporting was by exception. Whereas against the new Code, auditors are required to undertake work to provide a commentary against three criteria set by the NAO – governance; financial sustainability and improving economy, efficiency and effectiveness.

A new Auditor's Annual Report presented at the same time as the audit opinion is the forum for reporting the outcome of the auditor's work on Value for Money. It is required to contain:



The '**Commentary on arrangements**' will include a summary under each of the three specified reporting criteria and compared to how the results of VfM work were reported in previous years, the commentary will allow auditors to better reflect local context and also to draw attention to emerging or developing issues which may not represent significant weaknesses, but which may nevertheless require attention from the body itself. The commentary will not simply be a description of the arrangements in place, but an evaluation of those arrangements.

**Recommendations:** Where an auditor concludes there is a significant weakness in a body's arrangements, they report this to the body and support it with a recommendation for improvement.

**Progress in implementing recommendations:** Where an auditor has reported significant weaknesses in arrangements in the previous year, the auditor should follow up recommendations issued previously and include their view as to whether the recommendations have been implemented satisfactorily

**Use of additional powers:** Where an auditor uses additional powers, such as making statutory recommendations or issuing a public interest report, this needs to be reported in the auditor's annual report.

**Opinion on the financial statements:** The auditor's annual report also needs to summarise the results of the auditor's work on the financial statements. This is not a replacement for the AFR, or a verbatim repeat of it – it is simply a summary of what the opinion audit found

The new approach is more complex, more involved and will subsequently increase the cost of audit. We will be discussing this with the Chief Operating Officer shortly.

To review the new Code and AGN03 click [here](#)

NAO

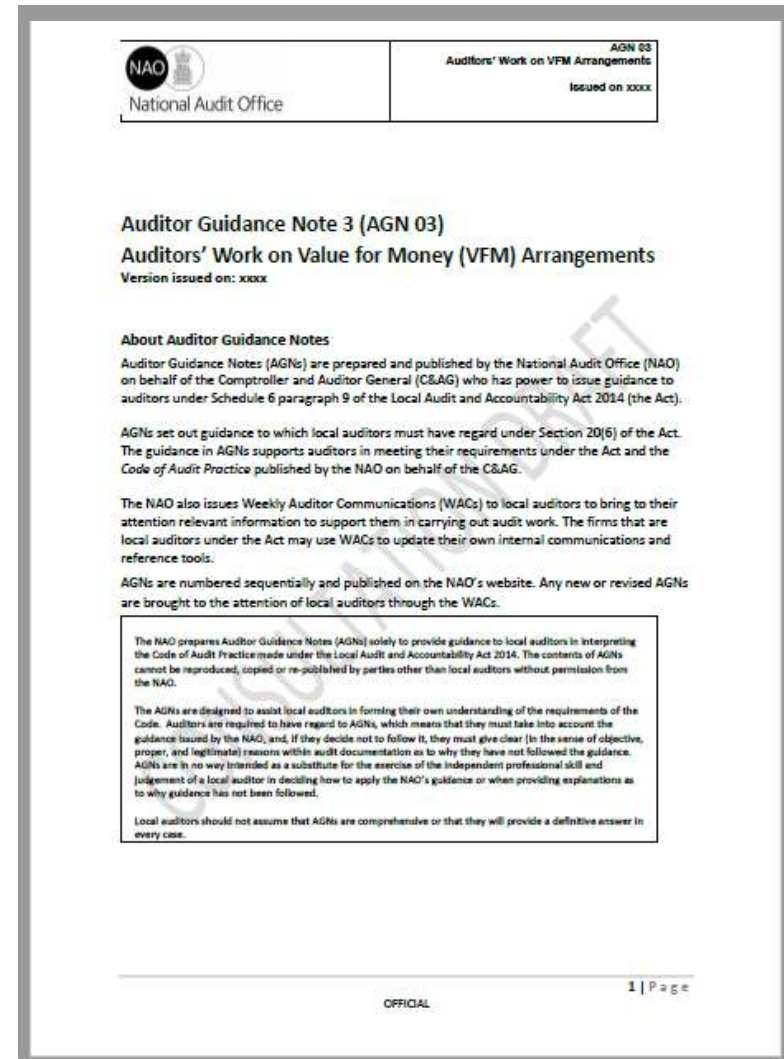
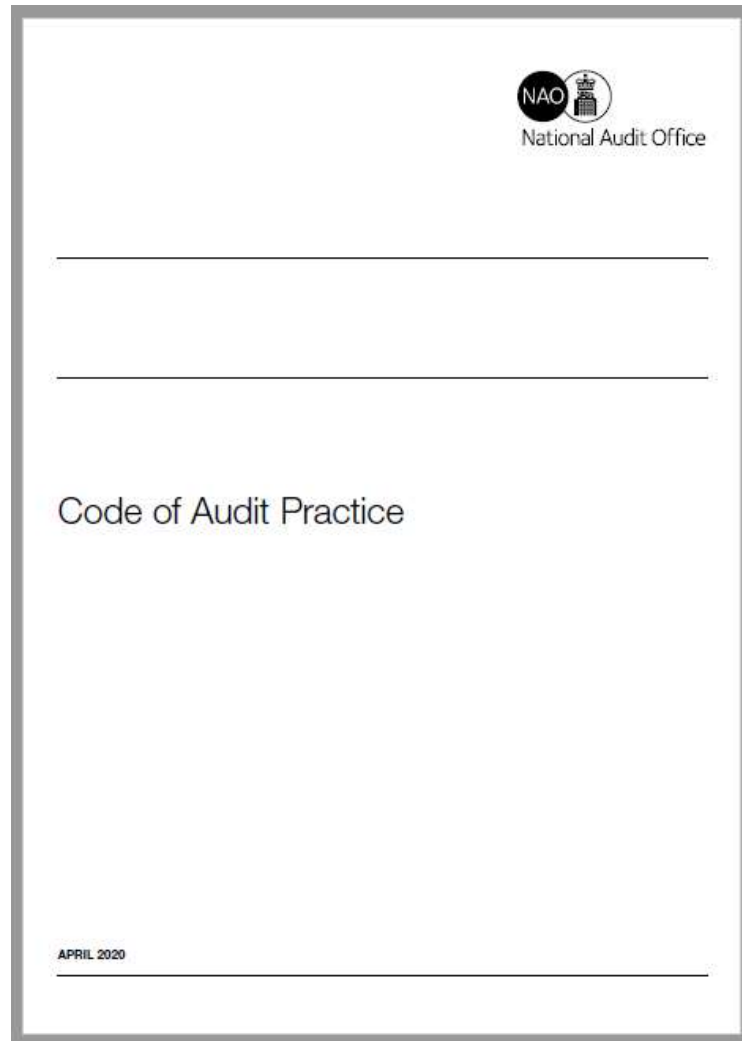




# Value for Money update for Audit & Governance Committee on new arrangements 2020-21



# How have the NAO changed value for money work ?

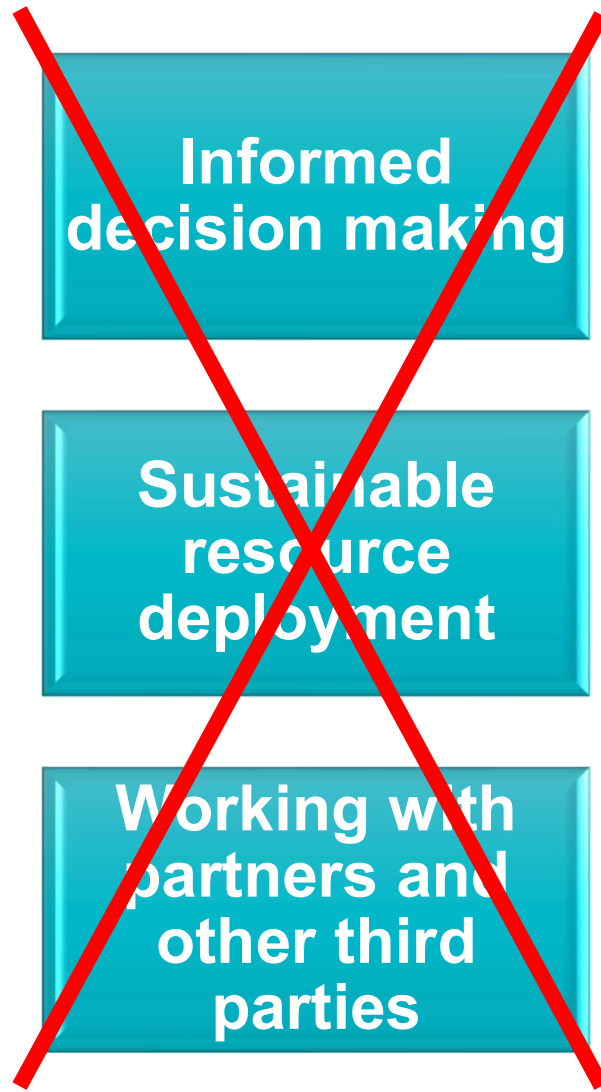


# How is value for money work changing ?



**VFM arrangements commentary and recommendations**

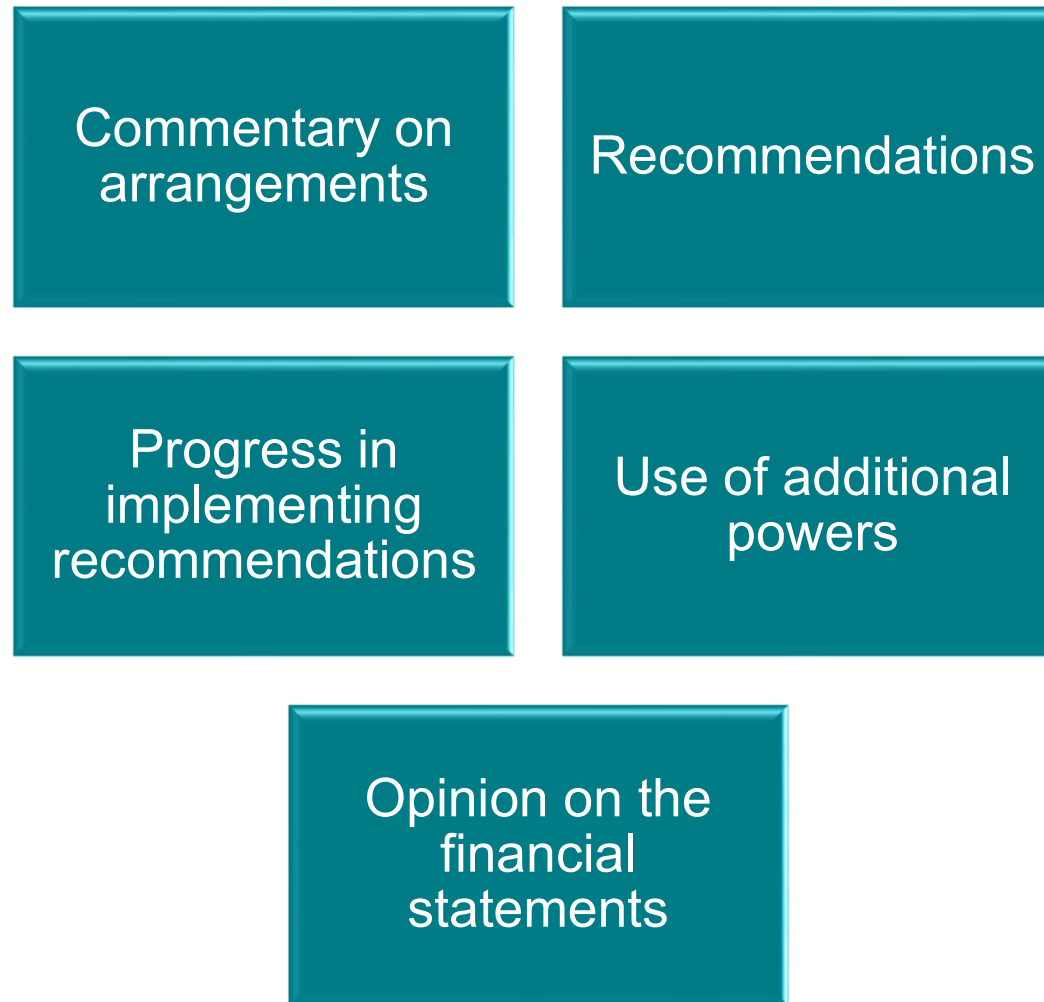
# The three criteria have changed...



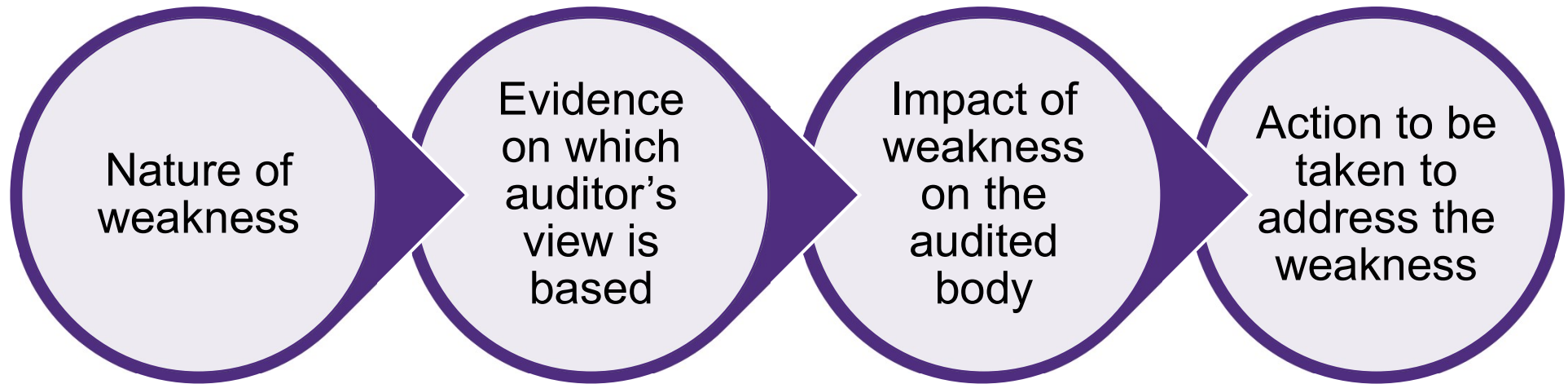
# A key change in reporting...



# So what is in an Auditor's Annual Report ?



# Recommendations



# Practical implications

The new approach is more complex, more involved and will lead to better quality working achieving more impact. Before beginning work, we will discuss with you:

- Timing
- Resourcing



# Revised auditing standard: Auditing Accounting Estimates and Related Disclosures

In the period December 2018 to January 2020 the Financial Reporting Council issued a number of updated International Auditing Standards (ISAs (UK)) which are effective for audits of financial statements for periods beginning on or after 15 December 2019. ISA (UK) 540 (revised): *Auditing Accounting Estimates and Related Disclosures* includes significant enhancements in respect of the audit risk assessment process for accounting estimates.

## Introduction

Under ISA (UK) 540 (Revised December 2018) auditors are required to understand and assess an entity's internal controls over accounting estimates, including:

- The nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates;
- How management identifies the need for and applies specialised skills or knowledge related to accounting estimates;
- How the entity's risk management process identifies and addresses risks relating to accounting estimates;
- The entity's information system as it relates to accounting estimates;
- The entity's control activities in relation to accounting estimates; and
- How management reviews the outcomes of previous accounting estimates.

As part of this process auditors also need to obtain an understanding of the role of those charged with governance, which is particularly important where the estimates have high estimation uncertainty, or require significant judgement.

Specifically do Audit and Governance Committee members:

- Understand the characteristics of the methods and models used to make the accounting estimates and the risks related to them;
- Oversee management's process for making accounting estimates, including the use of models, and the monitoring activities undertaken by management; and
- Evaluate how management made the accounting estimates?

## Additional information that will be required for our March 2021 audits

To ensure our compliance with this revised auditing standard, we will be requesting further information from management and those charged with governance during our audit for the year ended 31 March 2021 in all areas summarised above for all material accounting estimates that are included in the financial statements.

Based on our knowledge of the Council we have identified the following material accounting estimates for which this is likely to apply:

- Valuations of land and buildings, council dwellings, Tamar Bridge, inventory and group inventory and group land and buildings
- Depreciation
- Year end provisions and accruals
- Credit loss and impairment allowances
- Valuation of defined benefit net pension fund liabilities
- Fair value estimates
- Valuation of level 2 and level 3 investments

## The Council's Information systems

In respect of the Council's information systems we are required to consider how management identifies the methods, assumptions and source data used for each material accounting estimate and the need for any changes to these. This includes how management selects, or designs, the methods, assumptions and data to be used and applies the methods used in the valuations.

When the models used include increased complexity or subjectivity, as is the case for many valuation models, auditors need to understand and assess the controls in place over the models and the data included therein. Where adequate controls are not in place we may need to report this as a significant control deficiency and this could affect the amount of detailed substantive testing required during the audit.

If management has changed the method for making an accounting estimate we will need to fully understand management's rationale for this change. Any unexpected changes are likely to raise the audit risk profile of this accounting estimate and may result in the need for additional audit procedures.

We are aware that the Council uses management experts in deriving some of its more complex estimates, e.g. investments and asset valuations. However, it is important to note that the use of management experts does not diminish the responsibilities of management and those charged with governance to ensure that:

- All accounting estimates and related disclosures included in the financial statements have been prepared in accordance with the requirements of the financial reporting framework, and are materially accurate;
- There are adequate controls in place at the Council (and where applicable its management expert) over the models, assumptions and source data used in the preparation of accounting estimates.

### Estimation uncertainty

Under ISA (UK) 540 (Revised December 2018) we are required to consider the following:

- How management understands the degree of estimation uncertainty related to each accounting estimate; and
- How management address this estimation uncertainty when selecting their point estimate.

For example, how management identified and considered alternative, methods, assumptions or source data that would be equally valid under the financial reporting framework, and why these alternatives were rejected in favour of the point estimate used.

The revised standard includes increased emphasis on the importance of the financial statement disclosures. Under ISA (UK) 540 (Revised December 2018), auditors are required to assess whether both the accounting estimates themselves and the related disclosures are reasonable.

Where there is a material uncertainty, that is where there is a significant risk of a material change to the estimated carrying value of an asset or liability within the next year, there needs to be additional disclosures. Note that not all material estimates will have a material uncertainty and it is also possible that an estimate that is not material could have a risk of material uncertainty.

- Where there is material estimation uncertainty, we would expect the financial statement disclosures to disclose:
- What the assumptions and uncertainties are;
- How sensitive the assets and liabilities are to those assumptions, and why;

- The expected resolution of the uncertainty and the range of reasonably possible outcomes for the next financial year; and
- An explanation of any changes made to past assumptions if the uncertainty is unresolved.

### How can you help

As part of our planning risk assessment procedures we routinely make a number of enquiries of management and those charged with governance, which include general enquiries, fraud risk assessment questions, going concern considerations etc. Responses to these enquires are completed by management and confirmed by those charged with governance at an Audit and Governance Committee meeting. For our 2020/21 audit we will be making additional enquires on your accounting estimates in a similar way (which will cover the areas highlighted above).

### Further information

Further details on the requirements of ISA (UK) 540 (Revised December 2018) can be found in the auditing standard on the Financial Reporting Council's website:

[https://www.frc.org.uk/getattachment/0fa69c03-49ec-49ae-a8c9-cc7a2b65382a/ISA-\(UK\)-540\\_Revised-December-2018\\_final.pdf](https://www.frc.org.uk/getattachment/0fa69c03-49ec-49ae-a8c9-cc7a2b65382a/ISA-(UK)-540_Revised-December-2018_final.pdf)