

# Plymouth City Council Audit Progress Report

**Year ending 31 March 2021**

November 2021



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The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit planning process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect the Authority or all weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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# Introduction

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This paper provides the auditors.

Audit and Governance Committee with a report on progress in delivering our responsibilities as your external

The paper also includes:

- a summary of emerging national issues and developments that may be relevant to you as a local authority; and
- includes a number of challenge questions in respect of these emerging issues which the Committee may wish to consider (these are a tool to use, if helpful, rather than formal questions requiring responses for audit purposes)

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 your Engagement Lead or Engagement Manager.

# Introduction & headlines

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

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.

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 your Engagement Lead or Engagement Manager team.

We continue to bring specialists to our update conversations where appropriate to share any learning from our position as a leading audit supplier across the Local Government sector.

You will also have access to our annual Chief Accountant Workshops and any other networking opportunities we create for the various stakeholders.

More information can be found on our dedicated public sector on the Grant Thornton website by clicking on the logos.



# The auditor's statutory responsibilities

## Opinion on the Council's financial statements

Our work enables us to give an opinion as to whether the financial statements:

- give a true and fair view of the financial position of the audited body and its expenditure and income; and
- have been prepared properly in accordance with the relevant accounting and reporting framework as set out in legislation, applicable accounting standards and other directions.

Our planning will document our understanding of your key risks, your control environment and inform our testing strategy. This will continue until we begin our final accounts testing for the 2020/21 financial statements.

Since we last reported we have:

- continued to have regular discussions with management discussing the Miel Pension Liability transaction and we have updated our 1920 progress item within this report to provide details of this.
- continued to review the material assumptions within the 2019/20 financial statements including further work with regards to the valuation of investment properties.
- reviewed Council and Committee papers and minutes and the latest financial and operational performance reports ensuring we understand your current challenges.

### 2019/20 Audit

The progress and key areas of commentary regarding our audit of the 2019/20 financial statements are included for Members information in slides XX to XX.

### 2020/21 Audit

Our Audit plan for 2020/21 is included as a separate item to this agenda.

## Work on value-for-money arrangements 2020/21

Under the 2020 Audit Code of Practice, we are required to undertake sufficient work to satisfy ourselves that the Council “has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.”

Our initial risk assessment has been built on our understanding of your arrangements, and will continue to be updated as we finalise our 2019/20 audit work. Our key areas of focus will be reported under the following criteria:

- Financial sustainability: how the Council plans and manages its resources to ensure it can continue to deliver its services;
- Governance: how the Council ensures that it makes informed decisions and properly manages its risks; and
- Improving economy, efficiency and effectiveness: how the Council uses information about its costs and performance to improve the way it manages and delivers its services.

We will keep our risk assessment under continuous review. Where appropriate, we will update our risk assessment to reflect emerging risks or findings and report this to you. Our final commentary in the Auditors' Annual Report will include:

- a summary of our findings on any risks identified during our work;
- our judgements on the adequacy of the Council's arrangements for each of the three reporting criteria, as set out above;
- any recommendations made to management as a result of our work; and
- a follow up of progress against any recommendations raised in previous audits.

# 19/20 Progress as at November 2021

## Financial Statements Audit 2019/20

As we previously communicated to the Audit and Governance Committee in July 2021 and September 2021, we began our planning for the 2019/20 audit in January 2020. Our interim work was undertaken across March and April 2020.

Our interim fieldwork included:

- updating review of the Council's control environment;
- updating 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 2020 and presented this to the 11<sup>th</sup> May 2020 Audit and Governance Committee.

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.

As a result of our detailed technical review of the accounting treatment we have undertaken testing on the calculation of the Council's MRP provision and the calculation of the Council's capital financing requirement.

During the course of our audit work and testing we have had to undertake additional audit procedures and testing. These have been in relation to the valuations for property plant and equipment, including obsolescence factors applied. We have requested additional support from our own valuation expert – Wilks Head and Eve, on the valuation of property, plant and equipment and investment properties.

We have had to undertake further work in relation to the valuation assumptions made regarding investment properties. Further information has been supplied by the Council's internal valuer and the Finance team.

We have had to perform additional audit procedures and testing on the balances for government grants and grants received in advance, financial instruments and fair values and journals.

We have also had to perform additional audit procedures and testing on the Council's MRP estimate and the Capital Finance Requirement.

We have continued to liaise with and perform additional audit procedures with regards to the Miel pension liability payment.

Our detailed audit testing is complete bar the items detailed below. There remain a number of areas that will need to be concluded prior to the issuing of our audit opinion for 2019/20. These are as follows:

- Resolution of points discussed and raised regarding the Miel Ltd transaction;
- Completion of the GT work on investment property valuations and obsolescence factors assigned as part of the valuation process for those buildings valued in year;
- Satisfactory conclusion of the GT technical review of the draft financial statements
- Quality review of the audit file and resolution of any queries raised
- Review of the Council's going concern statement and cashflow forecasts for 12 months from the opinion date
- Obtaining and reviewing the final version of the financial statements; and
- Obtaining the letter of representation from the Council.

Findings against the significant areas of audit focus are included in slides 7-12.



# Significant Risks - Progress at November 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</p> <ul style="list-style-type: none"> <li>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.</li> <li>As a result of our review we have undertaken a specific review of the governance and due diligence arrangements regarding both this transaction and the Interest rate swap transaction in April 2020.</li> <li>We have reviewed the proposed accounting treatment for the Miel Pension Liability transaction. As a result of this review, the Council commissioned a review of the appropriate accounting treatment and we have been in regular discussion with the Council throughout the year regarding both the accounting and legality of the transaction.</li> <li>This work is still ongoing and continues to require further specialist accounting and legal advice.</li> </ul>

# Significant Risks - Progress at November 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</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> <li>extended our sample testing to evidence appropriate accounting for section 106 income and grants applied in year.</li> </ul>



# Significant Risks - Progress at November 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>• analysed 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>• evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions.</li> </ul>

# Significant Risks - Progress at November 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. 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:</li> <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> <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:</li> <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> <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> <li>• challenged the assumptions made by the valuer for the calculations of obsolescence factors and engaged our own valuer expert to review key assumptions</li> <li>• tested a sample of investment property valuations and engaged our own valuer expert to review key assumptions. We have also been provided with details of income generation for investment properties for 2020/21 to aide this testing.</li> </ul>

# Significant Risks - Progress at November 2021

Significant risk	Planned approach	Progress
Valuation of pension fund net liability	We will:	We have:
<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 matter significant assessed risks of material misstatement.</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>	<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> <li>• obtained the IAS19 assurance letter from the Devon Pension Fund auditor.</li> </ul>

# Significant Risks - Progress at November 2021

Significant risk	Planned approach	Progress
<b>Financial Instrument Disclosure notes</b>  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. 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.	We will: <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>	We have : <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.</li> <li>• tested the fair value assumptions of associated financial instruments and data and evidence to support the categories of both investment and liability levels</li> <li>• discussed the fair value assessment and assumptions of the financial instruments directly with the Council's expert advisers</li> <li>• Identified a number of adjustments for the accounting of fair value investments which the Council have amended in the revised financial statements.</li> </ul>

# 2020/21 Deliverables

## 2020/21 Deliverables

## Completed date

### Audit Plan 2020/21

November 2021

The draft audit plan for 2020/21 is attached as a separate item to this agenda.

### Audit of the Financial Statements 2020/21

TBA

### Audit Findings Report

TBA

### Auditor's Annual Report

TBA

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# 2020/21 Deliverables

## Other areas

### Certification of claims and returns 2020/21

We certify the Council's annual Housing Benefit Subsidy claim in accordance with procedures agreed with the Department for Work and Pensions (DWP). The certification work for the 2020/21 claim began in October 2021. The Council have asked for and DWP have granted the Council an extension to the deadline of 31 January 2022 for this work. .

We certify the Authority's annual Teachers' Pensions return in accordance with procedures agreed with Teachers' Pensions. The certification work for the 2020/21 began in October.

### Meetings

We meet with your Finance Officers every week. We continue to be in discussions with finance staff regarding emerging developments and to ensure the audit process is smooth and effective. We also meet with your Chief Executive on a quarterly basis to discuss Council's strategic visions and plans.

# Grant Thornton Transparency Report 2020

## Key issues

The Grant Thornton Transparency Report 2020 (the Local audit section is on pages 44-46 see link [Transparency report 2020 \(grantthornton.co.uk\)](https://www.grantthornton.co.uk/transparency-report-2020) reflects the financial year ended 31/12/2020 and is a requirement for all major firms. It outlines financial performance and other business issues but is also required to include regulatory findings and other matters of concern. The 2020 report reflects

- Results of Financial Reporting Council reviews in respect of 2019 audits including public sector audits
- Results of reviews carried out by the Quality Assurance Division of the ICAEW
- Results of any FRC enforcement actions – including fines etc.

The main issues impact the wider firm (pages 35-43) firm and audit quality are related

- The audit of revenue where income streams are complex and subject to management judgements
- Whether we have demonstrated on our files sufficient professional scepticism and challenge to management

In local audit the FRC reviewed six 18/19 audits (only one of which related to the NHS) and found that more work needed to be done to challenge management's assumptions in respect of asset valuation.

### Enforcement action

Page 43 reflects a number of FRC investigations some of which have reported in 2021 such as Patisserie Valerie and Manchester Building Society which resulted in fines and enforcement action. The report also reflects on ethical breaches in respect of the audit of Conviviality Plc.

It's worth noting that enforcement action all relates to audits carried in periods between 2007 and 2017.

## Grant Thornton Response

Grant Thornton has launched a number of initiatives to drive improvement in audit quality. The key highlights are

The development of strong new quality arrangements with an Audit Quality Board chaired by an independent non-executive

The development of an audit investment plan with significant investments in resources and technology – the national public sector team increased the number of auditors in the team from 280 to 340 between April 2020 and March 2021

Significant investment in training and a strong focus on developing a culture of challenge and professional scepticism





# Grant Thornton Transparency Report 2020

## Our Latest Local Audit Report

*The Financial Reporting Council (FRC) has published (29 October 2021) the findings of its annual audit quality inspection of public sector (local) audit. The Annual Quality Review (AQR) monitors the quality of UK Public Interest Entity and local audits to promote continuous improvement in audit quality.*

We are one of seven firms which currently delivers local audit work. Of our 330 local government and NHS audits, 87 are currently defined as ‘major audits’ which fall within the scope of the AQR. This year, the FRC looked at nine of our audits.

### Our file review results

The FRC reviewed nine of our audits this year. It graded six files (67%) as ‘Good’ and requiring no more than limited improvements. No files were graded as requiring significant improvement, representing a very impressive year-on-year improvement. The FRC described the improvement in our audit quality as an ‘encouraging response by the firm to the quality findings reported in the prior year.’ Our Value for Money work continues to be delivered to a high standard, with all of the files reviewed requiring no more than limited improvement.

The FRC also identified a number of good practices including effective challenge of management’s valuer, use of an auditor’s expert to assist with the audit of a highly specialised property valuation, and the extent and timing of involvement by the audit partner on the VFM conclusion.

## Implications for the Council

The regulatory environment and challenges to improvement audit quality across the audit profession have a number of implications for all audited bodies . In particular;

- Increased requirements from new accounting and auditing standards meaning longer time spent on addressing these requirements
- the increased focus on demonstrating professional scepticism meaning more challenge of management’s assumptions and more time spent doing that
- The increasing workload and increased regulatory focus together with wider professional trends mean the demand for audit services and the capacity of auditors are currently match putting upwards pressures on prices ( between 20-50% ) and reducing competition
- The number of Local Government opinion deadlines being achieved reducing each year. In 2021, this mean that less than 10% of audit opinion were issued by the 30<sup>th</sup> September 2021 deadline.
- **Specific issues for the Plymouth City Council Audit**
- Increased fees for the 2020/21 and 2021/22 audits
- Heavy focus on demonstrating professional scepticism and challenge on balances and large estimates – for Plymouth City Council this includes the valuation of property, plant and equipment, the valuation of investment properties, the minimum revenue provision (MRP), accruals for both income and expenditure recognition, provision for doubtful debts, where material and provisions.
- Increased focus on grant income
- Increased focus on accounting for and disclosure of financial instruments.

As a Firm we continue to be heavily committed to the quality of audit and financial reporting. Both the Firm and the FRC’s expectations are that auditors are required to obtain sufficient and appropriate audit evidence prior to an opinion being issued. This will continue to put pressure on the on achievements of deadline across the sectors.



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