

Audit Progress Report and Sector Update

North Somerset Council Year ending 31 March 2021

January 2021



Contents

Section	Page
Introduction	3
2019/20 - Progress and completion	4
Audit deliverables	5
Sector update	6

Introduction



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This paper provides the Audit 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 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.

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 manager or engagement lead.



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Progress at January 2021

2019/20

We issued an unqualified audit opinion on the Council and the Group's financial statements on 19 November 2020.

We included an emphasis of matter within our audit opinion which referred to the disclosures that management had made regarding the material uncertainties for the valuations of property, plant and equipment and pension fund pooled property funds. Our audit opinion was not modified as a result of this emphasis.

2020/21

We will now begin to look to the 2020/21 financial year and begin our planning processes for the audit.

Our formal work will begin later in the year and in the meantime we will:

- continue to have regular discussions with management to inform our risk assessment for the 2020/21 financial and value for money audits
- review papers and latest financial and operational performance reports
- consider any reports from regulators

We expect to issue our audit plan summarising our approach to key risks on the audit in April 2021.

Value for Money

On 1 April 2020, the National Audit Office introduced a new Code of Audit Practice which comes into effect from audit year 2020/21. The Code introduced a revised approach to the audit of Value for Money. (VFM)

There are three main changes arising from the NAO's new approach:

- A new set of key criteria, covering financial sustainability, governance and improvements in economy, efficiency and effectiveness
- More extensive reporting, with a requirement on the auditor to produce a commentary on arrangements across all of the key criteria, rather than the current 'reporting by exception' approach
- The replacement of the binary (qualified / unqualified) approach to VFM conclusions, with far more sophisticated judgements on performance, as well as key recommendations on any significant weaknesses in arrangements identified during the audit.

Further detail on the NAO's revised approach to VFM work can be found here: <https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2019/12/AGN-03-Auditors-Work-on-Value-for-Money-Arrangements.pdf>

Due to the change in approach, a fee variation will be needed for 2020-21 and your Engagement Team should be in touch shortly to discuss this.

The new Code of Audit Practice issued by the NAO can be found here: https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2020/01/Code_of_audit_practice_2020.pdf

Other areas

Meetings

We met with Finance Officers in January 2021 as part of audit planning for 2020/21. We continue to be in discussions with finance staff regarding emerging developments and to ensure the audit process is smooth and effective.

Certification of claims and returns

Housing Benefit Subsidy claim - in accordance with procedures agreed with the Department for Work and Pensions (DWP). We are currently working with the Housing Benefits team to complete the work.

The DWP has moved the reporting deadline back to 31 January 2021. We will report our findings to the Audit Committee in our Certification Letter in April 2021.

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

Audit deliverables

2019/20 Deliverables

	Planned Date	Status
Audit Findings Report The Audit Findings Report will be reported to the November Audit Committee.	November 2020	November 2020
Auditors Report This is the opinion on your financial statement, annual governance statement and value for money conclusion.	November 2020	November 2020
Annual Audit Letter This letter communicates the key issues arising from our work.	January 2021	January 2021

2020/21 Deliverables

Fee Letter	April 2021	Not yet due
Audit Plan	April 2021	Not yet due
Audit opinion	tbc	Not yet due
Audit Annual Report	tbc	Not yet due

Sector update

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 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](#)

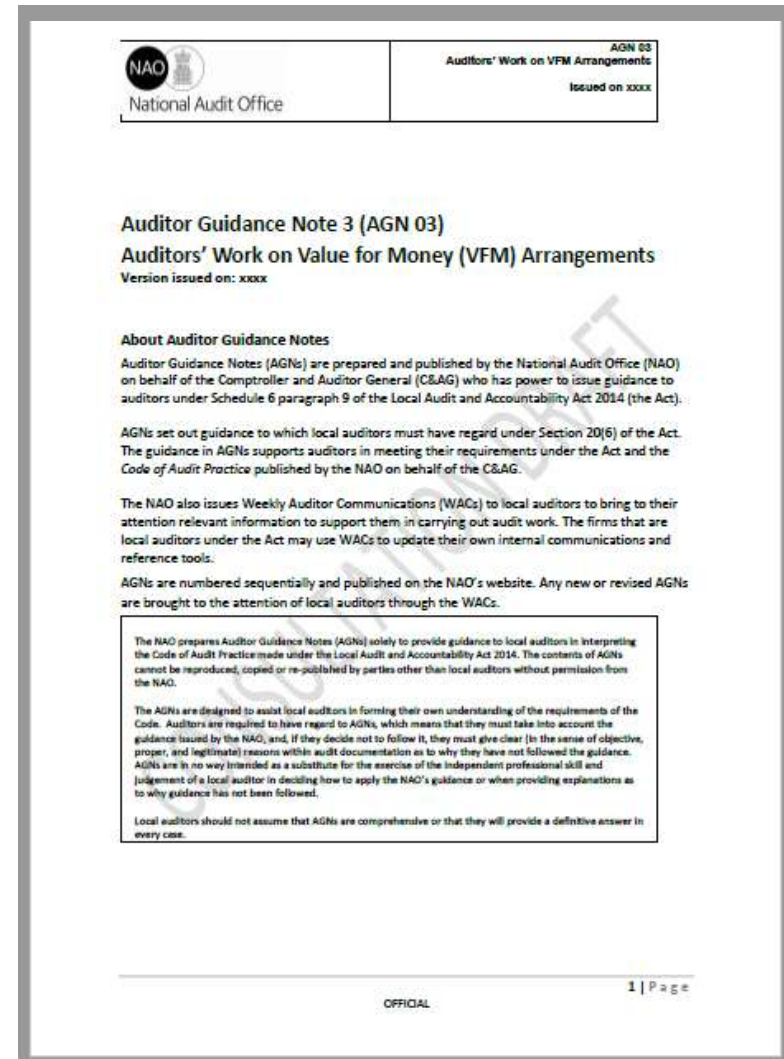
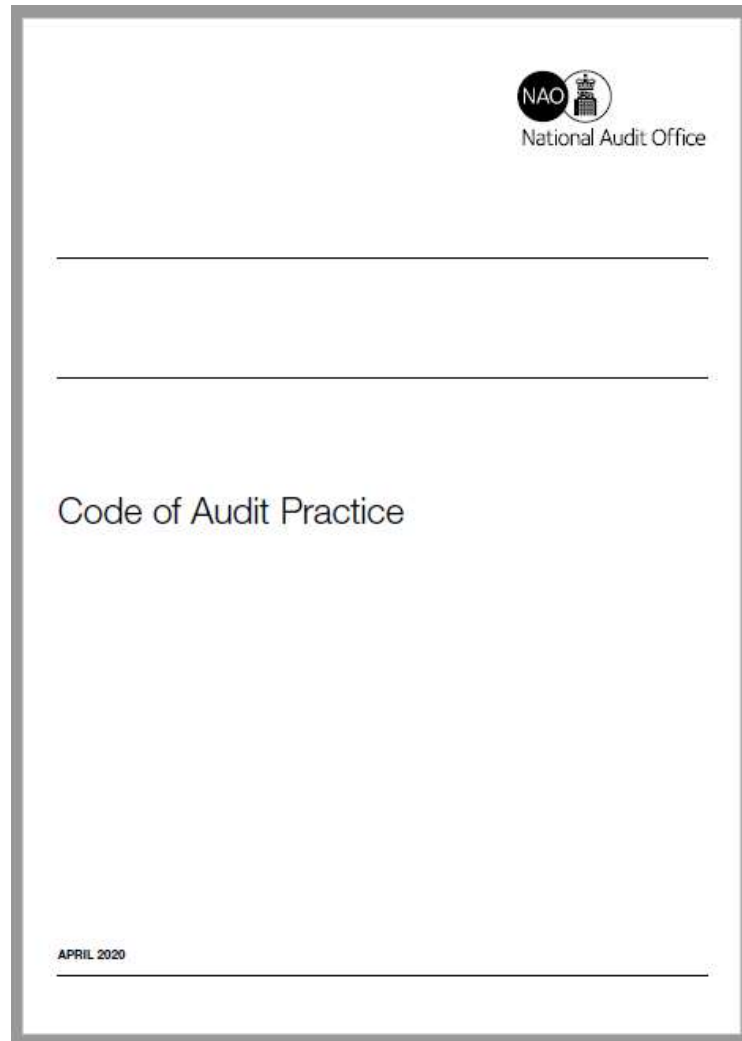
NAO



**Value for Money
update for Audit Committee
on new arrangements 2020-21**



How have the NAO changed value for money work ?

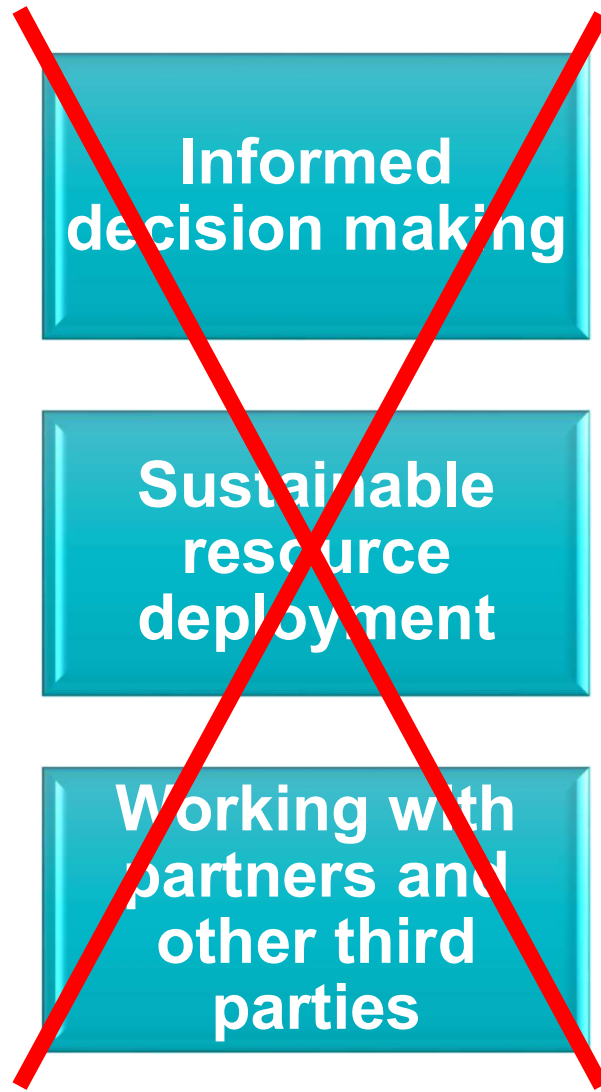


How is value for money work changing ?



VFM arrangements commentary and recommendations

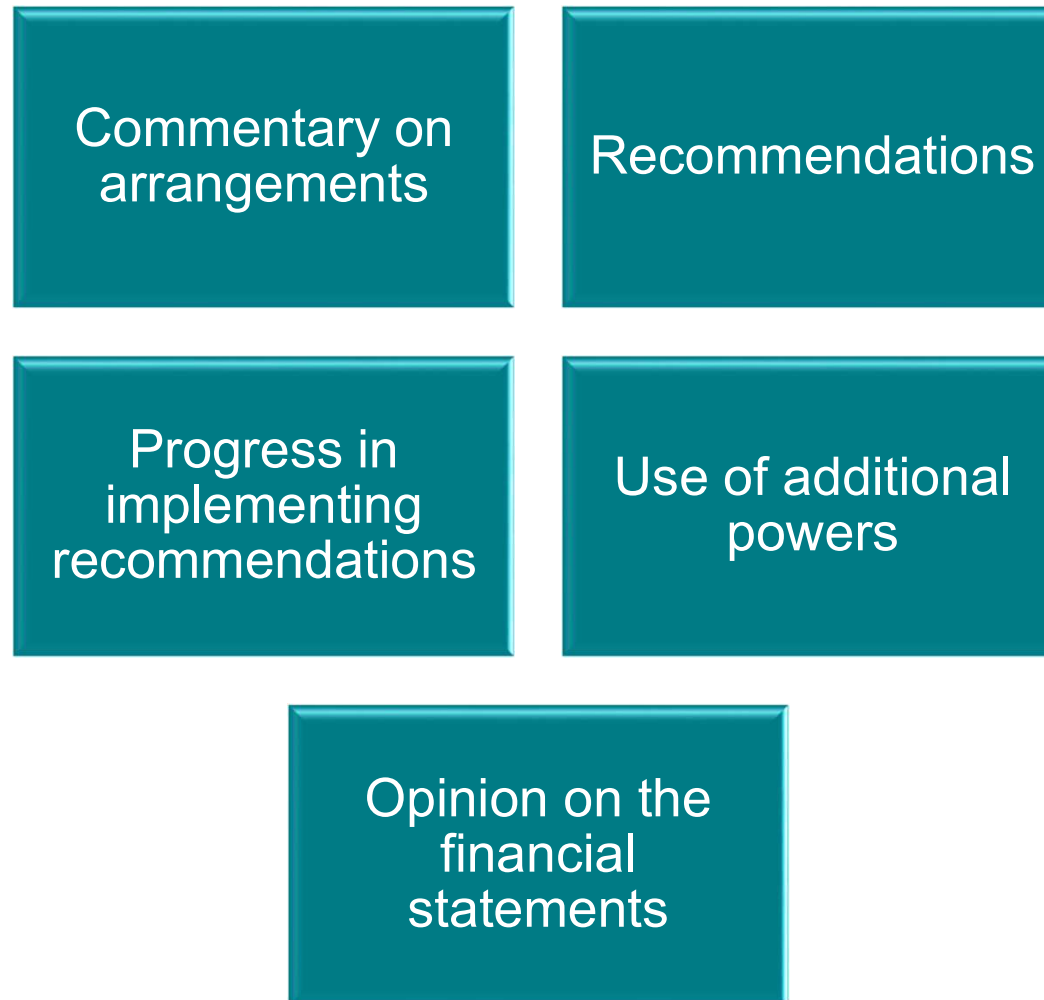
The three criteria have changed...



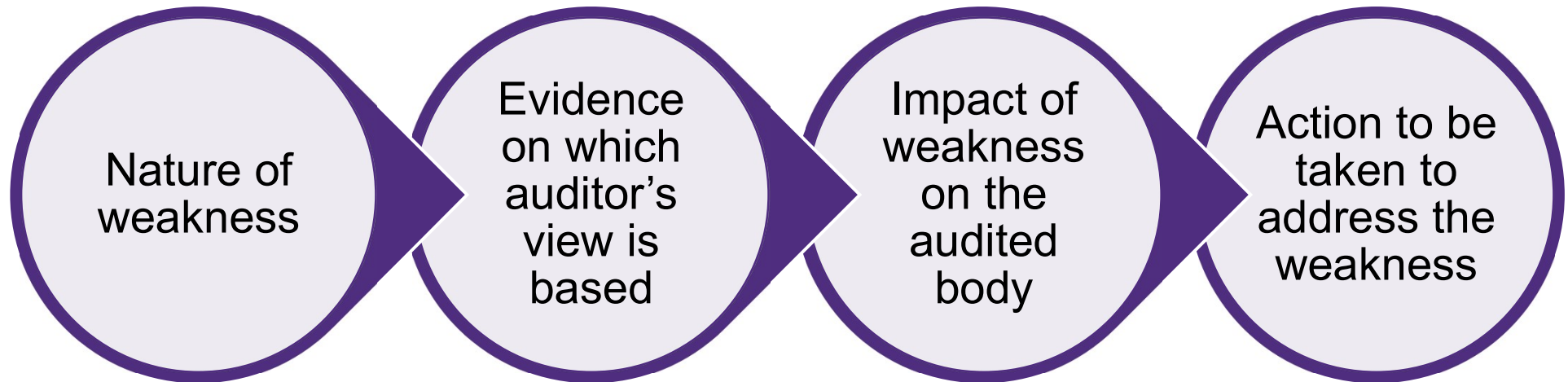
A key change in reporting...



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 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, Cornwall Airport, 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 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)

