

Audit Progress Report and Sector Update

West Oxfordshire District Council
Year ending 31 March 2021

18 March 2021



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Introduction



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This paper provides the Audit and General Purposes 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; 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 General Purposes 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 Engagement Lead or Engagement Manager.

Progress at March 2021

Working with You

Meetings

We will continue discussions with management regarding emerging developments and to ensure the audit process is smooth and effective. This includes the new approach to VFM, and the timing of audit deliverables.

Working Arrangements

With the Country still in lockdown we envisage having to continue to work completely remotely for some time. Working with the Council, we managed this well at the last audit and we will seek to be in regular contact with your finance team in respect of the logistics of these arrangements, recognising that staff, service provision and resident welfare during the pandemic will be your priorities.

Our planning work is underway and our interim audit is planned for March 2021. We are in discussions about this with the finance team to ensure we maximise the use of this time and ensure limited impact on your staff at this busy time.

2020/21

The delivery of 2019/20 financial statements audits presented a significant challenge. Whilst West Oxfordshire District Council's opinion was signed by the end of November 2020 deadline, a number of opinions regionally and nationally have not yet being given. This is largely due to the impact of Covid19. This, and delayed Housing Benefit certification work, has had a significant impact on our ability to complete enough audit planning to issue a 2020/21 Audit Plan in time for the March Audit and General Purposes Committee.

Whilst we will formally present the Audit Plan at the next Audit and General Purposes Committee, we will look to issue the Plan in early April 2021 after we have completed sufficient audit planning to allow this.

Our interim audit is also due to take place in late March. This work will be focused on:

- Review of the Council's control environment;
- Updating our understanding of the Council's financial systems and business processes;
- Review of Internal Audit reports on core financial systems;
- Early work on any emerging accounting issues;
- Early substantive testing in significant risk areas where possible.

We will report any findings from our interim audit in these progress reports.

Events

Our annual accounts workshop for Chief Accountants took place in February 2021 and your finance team attended. This took place remotely due to the current homeworking requirements and covered topical issues and technical areas pertinent to the 2020/21 statutory accounts.

Value for Money

As communicated in our previous sector updates, 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 most significant change in the Code is the introduction of a new 'Auditor's Annual Report', which brings together the results of all the auditor's work across the year. The Code also introduced a revised approach to the audit of Value for Money. These changes are set out in more detail in the NAO's Auditor Guidance Note 03 which was published on 15 October 2020.

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

- A new set of key criteria, covering governance, financial sustainability 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.

We will complete our initial risk assessment in March 2021 and we will report any risks of significant weakness, in our Audit Plan.

Audit logistics and team



Peter Barber, Key Audit Partner

Peter is responsible for the overall delivery of the audit. He will meet regularly with senior management of the Council and will attend Audit and General Purposes Committee meetings.



Siobhan Barnard, Audit Manager

Siobhan oversees day to day planning and manages the work of the Audit Incharge and associates to ensure that the audit work is focussed on the key areas of the financial statements risks and compliance with relevant accounting standards and guidance.



Francesca Hitchman, Audit Incharge

Francesca is responsible for the on-site delivery of the audit work. He assigns activities across the team and ensures it is completed satisfactorily.

Audited body responsibilities

Where audited bodies do not deliver to the timetable agreed, we need to ensure that this does not impact on audit quality or absorb a disproportionate amount of time, thereby disadvantaging other audits. Where the elapsed time to complete an audit exceeds that agreed due to a client not meeting its obligations we will not be able to maintain a team on site. Similarly, where additional resources are needed to complete the audit due to a client not meeting their obligations we are not able to guarantee the delivery of the audit to the agreed timescales. In addition, delayed audits will incur additional audit fees.

Our requirements

To minimise the risk of a delayed audit, you need to ensure that you:

- produce draft financial statements of good quality by the agreed timetable you have agreed with us, including all notes, the Narrative Report and the Annual Governance Statement
- ensure that good quality working papers are available at the start of the audit, in accordance with the working paper requirements schedule that we have shared with you
- ensure that the agreed data reports are available to us at the start of the audit and are reconciled to the values in the accounts, in order to facilitate our selection of samples for testing
- ensure that all appropriate staff are available on site throughout (or as otherwise agreed) the planned period of the audit
- respond promptly and adequately to audit queries.

Audit of Financial Statements

Materiality

The concept of materiality

Materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law. Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Materiality for planning purposes

We have determined financial statement materiality based on a proportion of the gross expenditure of the Council for the financial year. In the prior year we used the same benchmark. Materiality at the planning stage of our audit is £1.000m (PY £0.920m) for the Council, which equates to approximately 1.9% of your prior year gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision which we have determined to be £0.050m for senior officer remuneration.

We reconsider planning materiality if, during the course of our audit engagement, we become aware of facts and circumstances that would have caused us to make a different determination of planning materiality.

Matters we will report to the Audit and General Purposes Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit and General Purposes Committee any unadjusted misstatements of lesser amounts to the extent that these are identified by our audit work. Under ISA 260 (UK) 'Communication with those charged with governance', we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 (UK) defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. In the context of the Council, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.050m (PY £0.046m).

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

Significant risks

We have not yet to complete all our planning work so cannot confirm at this stage the significant risks that we will be auditing. However, the section below are likely areas that we will expect our work to focus on.

Presumed significant risks

ISA (UK) 240 includes two presumed risks as follows:

- Revenue recognition may be misstated due to the improper recognition of revenue. This is a rebuttable risk if the auditor concludes that there is a low risk of material misstatement due to fraud relating to revenue recognition. We have determined that the risk of fraud arising from revenue recognition can be rebutted. This is because there is little incentive to manipulate revenue recognition, opportunities to manipulate revenue recognition are very limited and the culture and ethical framework of the Council means that all forms of fraud are seen as unacceptable.
- The risk of management over-ride of controls is present in all entities. We therefore identified management override of controls, in particular journals, management estimates and transactions outside the course of normal business as a significant risk.

Other expected areas of focus

- Valuation of land and buildings.
- Valuation of investment properties.
- Valuation of the pension fund net liability
- Covid -19 – the on-going impact that this is having on the Council.

Value for Money arrangements

Revised approach to Value for Money work for 2020/21

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.

The Code require auditors to consider whether the body has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. When reporting on these arrangements, the Code requires auditors to structure their commentary on arrangements under three specified reporting criteria. These are as set out below:



Improving economy, efficiency and effectiveness

Arrangements for improving the way the body delivers its services. This includes arrangements for understanding costs and delivering efficiencies and improving outcomes for service users.



Financial Sustainability

Arrangements for ensuring the body can continue to deliver services. This includes planning resources to ensure adequate finances and maintain sustainable levels of spending over the medium term (3-5 years)



Governance

Arrangements for ensuring that the body makes appropriate decisions in the right way. This includes arrangements for budget setting and management, risk management, and ensuring the body makes decisions based on appropriate information



Risks of significant VFM weaknesses

As part of our planning work, we will consider whether there are any risks of significant weakness in the body's arrangements for securing economy, efficiency and effectiveness in its use of resources that we need to perform further procedures on. We may need to make recommendations following the completion of our work. The potential different types of recommendations we could make are set out in the table below.

Potential types of recommendations

A range of different recommendations could be made following the completion of work on risks of significant weakness, as follows:



Statutory recommendation

Written recommendations to the body under Section 24 (Schedule 7) of the Local Audit and Accountability Act 2014. A recommendation under schedule 7 requires the body to discuss and respond publicly to the report.



Key recommendation

The Code of Audit Practice requires that where auditors identify significant weaknesses in arrangements to secure value for money they should make recommendations setting out the actions that should be taken by the body. We have defined these recommendations as 'key recommendations'.



Improvement recommendation

These recommendations, if implemented should improve the arrangements in place at the body, but are not made as a result of identifying significant weaknesses in the body's arrangements

Audit fees

The 2020/21 Code introduces a revised approach to our VFM work. This requires auditors to produce a commentary on arrangements across all of the key criteria, rather than the current 'reporting by exception' approach. Auditors now have to make far more sophisticated judgements on performance, as well as issue key recommendations if any significant weaknesses in arrangements are identified during the audit. We will be working with the NAO and other audit firms to discuss and share learning in respect of common issues arising across the sector.

The new approach will be more challenging, as well as rewarding, for audited bodies, involving discussions at a wider and more strategic level. Both the reporting, and the planning and risk assessment which underpins it, will require more audit time, delivered through a richer skill mix than in previous years.

Additionally, across all sectors and firms, the FRC has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge and to undertake additional and more robust testing, in relation to the revised ISA (UK) 540 (revised): Auditing Accounting Estimates and Related Disclosures.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and public sector financial reporting. Further detail on our proposed work and fees are set out below.

We are still in discussions with Public Sector Audit Appointments regarding fees for 2020/21 and will provide more detail in the Audit Plan.

	Actual Fee 2018/19	Actual Fee 2019/20	Proposed fee 2020/21
Council Audit	£40,027	£46,777	£TBC
Total audit fees (excluding VAT)	£40,027	£46,777	TBC

Assumptions

In setting the above fees, we have assumed that the Council will:

- prepare a good quality set of accounts, supported by comprehensive and well presented working papers which are ready at the start of the audit
- provide appropriate analysis, support and evidence to support all critical judgements and significant judgements made during the course of preparing the financial statements
- provide early notice of proposed complex or unusual transactions which could have a material impact on the financial statements.

Relevant professional standards

In preparing our fee estimate, we have had regard to all relevant professional standards, including paragraphs 4.1 and 4.2 of the FRC's [Ethical Standard \(revised 2019\)](#) which stipulate that the Engagement Lead (Key Audit Partner) must set a fee sufficient to enable the resourcing of the audit with partners and staff with appropriate time and skill to deliver an audit to the required professional and Ethical standards.

Audit Deliverables

2020/21 Deliverables	Planned Date	Status
Accounts Audit Plan We are required to issue a detailed accounts audit plan to the Audit and General Purposes Committee setting out our proposed approach in order to give an opinion on the Council's 2020-21 financial statements. This also includes the findings of our value for money initial risk assessment.	April 2021	Not yet due
Interim Audit Findings We will report to you the findings from our interim audit in our Audit Progress Report.	June 2021	Not yet due
Audit Findings Report The Audit Findings Report will be reported to the September Audit and General Purposes Committee.	September 2021	Not yet due
Auditors Report This is the opinion on your financial statements and annual governance statement.	September 2021	Not yet due
Auditor's Annual Report Under the new Code of Audit Practice this replaces the Annual Audit Letter and is the key output from local audit work on arrangements to secure VFM.	September 2021	Not due yet

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 and General Purposes 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

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 General Purposes 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, and investment properties
- Depreciation
- Year end provisions and accruals,
- Credit loss and impairment allowances
- Valuation of defined benefit net pension fund liabilities
- Fair value estimates

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. asset valuations and pensions liabilities. 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 service provider or 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 include:

- 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 enquiries are completed by management and confirmed by those charged with governance at an Audit and General Purposes Committee meeting. For our 2020/21 audit we will be making additional enquiries on your accounting estimates in a similar way (which will cover the areas highlighted above). We would appreciate a prompt response to these enquiries in due course.

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)

