

Audit Progress Report and Sector Update

Birmingham City Council

Year ending 31 March 2021

February 2021



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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 Engagement Lead or your Engagement Manager.

Financial Statements Audit 2019/20

Financial Statements Audit

We issued unqualified audit opinions on the financial statements of the Council on 8 January 2021.

We included an emphasis of matter within our audit opinion which referred to the disclosures that management had made regarding the material uncertainties in the valuations of land and buildings and the pension fund's property investments as at 31 March 2020. Our audit opinion was not modified as a result of this emphasis.

Value for Money opinion

We issued a qualified value for money opinion for the year ended 31 March 2020 on 8 January 2021.

Certification of the Audit

We have not yet certified the completion of the audit for 2019/20, as we have not been able to issue our assurance statement over the consistency of the Council's WGA submission with the financial statements. This work is substantially complete but due to issues with the central system, the Council have not been able to demonstrate that they have made required changes to their submission.

Certification of claims and returns

Teachers Pensions

We issued our report on the Council's Teachers Pensions Return for the 2019/20 year on 18 December 2020, in accordance with the procedures required by Teachers Pensions.

Housing Benefits

The Department for Work and Pensions (DWP) moved the reporting deadline from 31 November 2020 to 31 January 2021. We certified the Council's subsidy claim, in accordance with procedures agreed with the DWP, on 19 January 2021.

Pooling of Housing Capital Receipts

We are in the process of completing with procedures required by MHCLG on the Council's Pooling of Housing Capital Receipts Return for 2019/20. We hope to certify this return in the coming weeks.

Events

We provide a range of workshops, along with network events for members and publications to support the Council. Your officers have been invited to our Financial Reporting Workshop in February, which will help to ensure that members of your Finance Team are up to date with the latest financial reporting requirements for local authority accounts. We will be happy to discuss further, in an informal meeting with members, the detail behind the key changes to the audit this year, as set out later in this paper. Most significantly the new Value for Money responsibilities and the introduction of ISA540.

Further details of the publications that may be of interest to the Council are set out in our Sector Update section of this report.

Audit deliverables

2019/20 Deliverables	Planned Date	Status
Audit Findings Report	September 2020	Draft November 2020 Final December 2020
Auditors Report	September 2020	January 2021
Annual Audit Letter	October 2020	January 2021
2020/21 Deliverables		
Audit Plan	March 2021	Not yet due
Audit opinion	October 2021	Not yet due
Audit Annual Report	October 2021	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

Accounting estimates and related disclosures

The Financial Reporting Council issued an updated ISA (UK) 540 (revised): *Auditing Accounting Estimates and Related Disclosures* which 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

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.

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 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 detail:

- 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)

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 to the right:



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)



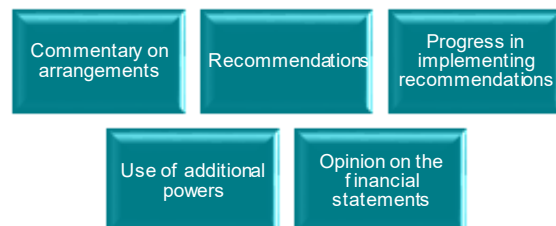
Governance

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



Auditor's Annual Report

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:



- **Commentary on arrangements:** This 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.

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 needed to perform further procedures on.

The risks we identify will be detailed in our Audit Plan, along with the further procedures we will perform.

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.

Further information

To review the new Code and AGN03, visit the NAO's website using the link below:

<https://www.nao.org.uk/code-audit-practice/code-of-audit-practice-consultation/>

