

Audit Progress Report and Sector Update

Cheltenham Borough Council
Year ending 31 March 2020

January 2020



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Introduction



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

The paper also includes:

- a summary of emerging national issues and developments that may be relevant to you as a local authority; 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, Compliance 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

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 January 2020

Financial Statements Audit

We issued our opinion on Cheltenham Borough Council's 2018/19 Statement of Accounts on 30 July 2019.

We will begin our planning for the 2019/20 audit in January and will issue a detailed audit plan, setting out our proposed approach to the audit of the Council's 2019/20 financial statements.

We will begin our interim audit in in early 2020. Our interim fieldwork includes:

- Updated review of the Council's control environment
- Updated understanding of financial systems
- Review of Internal Audit reports on core financial systems
- Early work on emerging accounting issues
- Early substantive testing

We will report our work in the Audit Findings Report and provide you with regular updates on the progress of the audit

Value for Money

The scope of our work is set out in the guidance issued by the National Audit Office. The Code requires auditors to satisfy themselves that; "the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources".

The guidance confirmed the overall criterion as: "in all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people".

The three sub criteria for assessment to be able to give a conclusion overall are:

- Informed decision making
- Sustainable resource deployment
- Working with partners and other third parties

Details of our initial risk assessment to determine our approach will be included in our Audit Plan.

We will report our work in the Audit Findings Report where we will provide our Value For Money Conclusion.

The NAO is consulting on a new Code of Audit Practice from 2020 which proposes to make significant changes to Value for Money work. Please see page 10 for more details.

Progress at January 2020 (Cont.)

Other areas

Certification of claims and returns

We certify the Council's annual Housing Benefit Subsidy claim in accordance with procedures agreed with the Department for Work and Pensions. The certification work for the 2018/19 claims for Cheltenham Borough Council was completed on 26 November 2019, in advance of the 30 November 2019 deadline. We have reported our findings to the Audit, Governance and Committee further on in this report on Page 6.

We will also be finalising the certification of the pooling of housing capital receipts claim in January 2020.

Meetings

We will meet with Finance Officers in January 2020 as part of our liaison meetings and continue to be in discussions with finance staff regarding emerging developments and to ensure the audit process is smooth and effective. We will also meet with your Chief Executive regularly to discuss the Council's strategic priorities and plans.

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 2020, 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.

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 Fees

During 2017, PSAA awarded contracts for audit for a five year period beginning on 1 April 2018. 2019/20 is the second year of that contract. Since that time, there have been a number of developments within the accounting and audit profession. Across all sectors and firms, the Financial Reporting Council (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.

Our work in the Local Government sector in 2018/19 has highlighted areas where financial reporting, in particular, property, plant and equipment and pensions, needs to improve. There is also an increase in the complexity of Local Government financial transactions and financial reporting. This combined with the FRC requirement that all Local Government audits are at or above the "few improvements needed" (2A) rating means that additional audit work is required.

We are currently reviewing the impact of these changes on both the cost and timing of audits. We will discuss this with your s151 Officer including any proposed variations to the Scale Fee set by PSAA Limited, before communicating fully with the Audit, Compliance and Governance Committee.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and local government financial reporting.

Certification of claims and returns

We completed the certification of Housing Benefit claims for Cheltenham Borough Council on 26 November 2019. Our findings are set out below:

Cheltenham Borough Council

The claim was qualified, and the following errors were noted in our report:

Cell 011 - Non HRA Rent Rebates – An error was identified in the prior year in relation to misclassification of expenditure. The full population of cell 11 was identified and the authority tested each claim. The test returned no errors and the CAKE test is considered as closed.

Cell 055 – HRA Rent Rebates – An error was identified in the prior year in relation to incorrect calculation of earned income. As it was not possible to correctly establish the error for amendment additional testing of 40 cases was completed for the error, resulting in an extrapolated error value of £33.

Cell 055 - HRA Rent Rebates - An error was identified in our initial testing in relation to calculation of State Pension. As it was not possible to correctly establish the error for amendment additional testing of 40 cases was completed for the error, resulting in an extrapolated error value of £2,388.

Cell 055 - HRA Rent Rebates - An error was identified in our initial testing in relation to misclassification of expenditure. As it was not possible to correctly establish the error for amendment additional testing of 40 cases was completed for the error, resulting in an extrapolated error value of £627.

Cell 094 - Rent Allowances - An error was identified in our initial testing and prior year testing in relation to incorrect calculation of earned income. As it was not possible to correctly establish the error for amendment additional testing of 40 cases was completed for the error, resulting in an extrapolated error value of £103.

Cell 094 - Rent Allowances - An error was identified in our initial testing in relation to incorrect calculation of Occupational Pension. As it was not possible to correctly establish the error for amendment additional testing of 40 cases was completed for the error, resulting in an extrapolated error value of £13.

Audit Deliverables

2018/19 Deliverables	Planned Date	Status
Audit Findings Report The Audit Findings Report was reported to the July and November Audit, Governance and Standards Committee.	July 2019	Complete
Auditors Report This is the opinion on your financial statement, annual governance statement and value for money conclusion.	July 2019	Complete
Annual Audit Letter This letter communicates the key issues arising from our work.	September 2019	Complete
2019/20 Deliverables	Planned Date	Status
Fee Letter Confirming audit fee for 2019/20.	April 2019	Complete
Accounts Audit Plan We are required to issue a detailed accounts audit plan to Audit, Compliance and Governance Committee setting out our proposed approach in order to give an opinion on the Council's 2019-20 financial statements.	March 2020	Not yet due
Interim Audit Findings We will report to you the findings from our interim audit and our initial value for money risk assessment within our Progress Report.	March 2020	Not yet due
Audit Findings Report The Audit Findings Report will be reported to the July Audit, Compliance and Governance Committee.	July 2020	Not yet due
Auditors Report This is the opinion on your financial statement, annual governance statement and value for money conclusion.	July 2020	Not yet due
Annual Audit Letter This letter communicates the key issues arising from our work.	September 2020	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, Compliance and Governance Committee members, as well as any accounting and regulatory updates.

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

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

A teal rectangular button with the text "Public Sector" in white.

Public Sector

A purple rectangular button with the text "Local government" in white.

Local
government

MHCLG – Independent probe into local government audit

In July, the then Communities secretary, James Brokenshire, announced the government is to examine local authority financial reporting and auditing.

At the CIPFA conference he told delegates the independent review will be headed up by Sir Tony Redmond, a former CIPFA president.

The government was “working towards improving its approach to local government oversight and support”, Brokenshire promised.

“A robust local audit system is absolutely pivotal to work on oversight, not just because it reinforces confidence in financial reporting but because it reinforces service delivery and, ultimately, our faith in local democracy,” he said.

“There are potentially far-reaching consequences when audits aren’t carried out properly and fail to detect significant problems.”

The review will look at the quality of local authority audits and whether they are highlighting when an organisation is in financial trouble early enough.

It will also look at whether the public has lost faith in auditors and whether the current audit arrangements for councils are still “fit for purpose”.

On the appointment of Redmond, CIPFA chief executive Rob Whiteman said: “Tony Redmond is uniquely placed to lead this vital review, which will be critical for determining future regulatory requirements.

“Local audit is crucial in providing assurance and accountability to the public, while helping to prevent financial and governance failure.”

He added: “This work will allow us to identify what is needed to make local audit as robust as possible, and how the audit function can meet the assurance needs, both now and in the future, of the sector as a whole.”



In the question and answer session following his speech, Brokenshire said he was not looking to bring back the Audit Commission, which appointed auditors to local bodies and was abolished in 2015. MHCLG note that auditing of local authorities was then taken over by the private, voluntary and not-for-profit sectors.

He explained he was “open minded”, but believed the Audit Commission was “of its time”.

Local authorities in England are responsible for 22% of total UK public sector expenditure so their accounts “must be of the highest level of transparency and quality”, the Ministry of Housing, Local Government and Communities said. The review will also look at how local authorities publish their annual accounts and if the financial reporting system is robust enough.

Redmond, who has also been a local authority treasurer and chief executive, is expected to report to the communities secretary with his initial recommendations in December 2019, with a final report published in March 2020. Redmond has also worked as a local government boundary commissioner and held the post of local government ombudsman.

The terms of reference focus on whether there is an “expectation gap” between the purpose of external audit and what it is currently delivering. It will examine the performance of local authority audit, judged according to the criteria of economy, effectiveness and efficiency.

Other key areas of the review include whether:

- 1) audit recommendations are effective in helping councils to improve financial management
- 2) auditors are using their reporting powers appropriately
- 3) councils are responding to auditors appropriately
- 4) Financial savings from local audit reforms have been realised
- 5) There has been an increase in audit providers
- 6) Auditors are properly responding to questions or objections by local taxpayers
- 7) Council accounts report financial performance in a way that is transparent and open to local press scrutiny

Financial Reporting Council – Summary of key developments for 2019/20 annual reports

On 30 October the Financial Reporting Council (FRC) wrote an Open Letter to Company Audit Committee Chairs. Some of the points are relevant to local authorities.

The reporting environment

The FRC notes that, “In times of uncertainty, whether created by political events, general economic conditions or operational challenges, investors look for greater transparency in corporate reports to inform their decision-making. We expect companies to consider carefully the detail provided in those areas of their reports which are exposed to heightened levels of risk; for example, descriptions of how they have approached going concern considerations, the impact of Brexit and all areas of material estimation uncertainty.” These issues equally affect local authorities, and the Statement of Accounts or Annual Report should provide readers with sufficient appropriate information on these topics.

Critical judgements and estimates

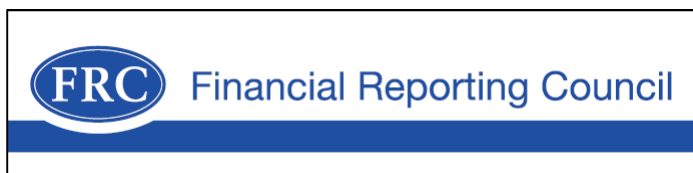
The FRC wrote “More companies this year made a clear distinction between the critical judgements they make in preparing their accounts from those that involve the making of estimates and which lead to different disclosure requirements. However, some provided insufficient disclosures to explain this area of their reporting where a particular judgement had significant impact on their reporting; for example, whether a specific investment was a joint venture or a subsidiary requiring consolidation. We will continue to have a key focus on the adequacy of disclosures supporting transparent reporting of estimation uncertainties. An understanding of their sensitivity to changing assumptions is of critical value to investors, giving them clearer insight into the possible future changes in balance sheet values and which can inform their investment decisions.” Critical judgements and estimates also form a crucial part of local authority statements of account, with the distinction often blurred.

IFRS 16 Leases

The FRC letter notes “IFRS 16 is effective for periods beginning on or after 1 January 2019. We recently conducted a thematic review looking at how companies reported on their adoption of the new standard in their June 2019 interim accounts. In advance of our detailed findings which will be published shortly, I set out what we expect to see by way of disclosures in the forthcoming accounts, drawing on the results of our work.

- Clear explanation of the key judgements made in response to the new reporting requirements;
- Effective communication of the impact on profit and loss, addressing any lack of comparability with the prior year;
- Clear identification of practical expedients used on transition and accounting policy choices; and
- Well explained reconciliation, where necessary, of operating lease commitments under IAS 17, ‘Leases’, the previous standard and lease liabilities under IFRS 16.”

The implementation of IFRS is delayed until 1 April 2020 in the public sector when it will replace IAS 17 Leases and the three interpretations that supported its application. Authorities will need information and processes in place to enable them to comply with the requirements. They will need to make disclosures in the 2019/20 accounts about the impact of IFRS 16 in accordance with IAS 8/ Code 3.3.4.3 requirements for disclosure about standards which are issued but are not yet effective.



What is the future for local audit?

Paul Dossett, Head of Local Government at Grant Thornton, has written in the Municipal Journal “Audit has been a hot topic of debate this year and local audit is no exception. With a review into the quality of local audit now ongoing, it’s critical that part of this work looks at the overarching governance and management of the audit regime. We believe there is a strong need for new oversight arrangements if the local audit regime is to remain sustainable and effective in the future.”

Paul goes on to write “Local (local authority and NHS) audit has been a key part of the oversight regime for public services for more than a century. The National Audit Office (NAO) has exercised this role in central government for several generations and their reporting to Parliament via the Public Accounts Committee is a key part of the public spending accountability framework.

Local audit got a significant boost with the creation of the Audit Commission in 1983 which provided a coordinated, high profile focus on local government and (from 1990) NHS spending and performance at a local level. Through undertaking value for money reviews and maintaining a tight focus on the generational governance challenges, such as rate capping in the 1980s and service governance failings in the 1990s, the Commission provided a robust market management function for the local audit regime. Local audit fees, appointments, scope, quality and relevant support for auditors all fell within their ambit.

However, the Commission was ultimately deemed, among other things, to be too expensive and was abolished in 2010, as part of the Coalition Government’s austerity saving plans. While the regime was not perfect, and the sector had acknowledged that reform of the Commission was needed, complete abolition was not the answer.

Since then, there has been no body with complete oversight of the local audit regime and how it interacts with local public services. The Ministry of Housing, Communities and Local Government; Department of Health; NHS; NAO; Local Government Association (LGA); Public Sector Audit Appointments Ltd (PSAA); the Financial Reporting Council (FRC); the Chartered Institute of Public Finance & Accountancy (CIPFA), audit firms and the audited bodies themselves all have an important role to play but, sometimes, the pursuit of individual organisational objectives has resulted in sub-optimal and even conflicting outcomes for the regime overall.

These various bodies have pursued separate objectives in areas such as audit fee reduction, scope of work, compliance with commercial practice, earlier reporting deadlines and mirroring commercial accounting conventions – to name just a few.

This has resulted in a regime that no stakeholder is wholly satisfied with and one that does not ensure local audit is providing a sufficiently robust and holistic oversight of public spending.

To help provide a more cohesive and co-ordinated approach within the sector, we believe that new oversight arrangements should be introduced. These would have ultimate responsibility for ensuring the sustainability of the local audit regime and that its component parts – including the Audit Code, regulation, market management and fees – interact in an optimal way. While these arrangements do not need to be another Audit Commission, we need to have a strategic approach to addressing the financial sustainability challenges facing local government and the NHS, the benchmarking of performance and the investigation of governance failings.

There are a number of possible solutions including:

- 1) The creation of a new arm’s length agency with a specific remit for overseeing and joining up local audit. It would provide a framework to ensure the sustainability of the regime, covering fees, appointments, and audit quality. The body would also help to create a consistent voice to government and relevant public sector stakeholders on key issues arising from the regime. Such a body would need its own governance structure drawn from the public sector and wider business community; and
- 2) Extending the current remit of the NAO. Give it total oversight of the local audit regime and, in effect, establish a local audit version of the NAO, with all the attendant powers exercised in respect of local audit. In this context, there would be a need to create appropriate governance for the various sectors, similar to the Public Accounts Committee.

While the detail of the new arrangements would be up for debate, it’s clear that a new type of oversight body, with ultimate responsibility for the key elements of local audit, is needed. It would help to provide much-needed cohesion across the sector and between its core stakeholders.

The online article is available here:

<https://www.themj.co.uk/What-is-the-future-for-audit/214769>

Grant Thornton's Sustainable Growth Index Report

Grant Thornton has launched the Sustainable Growth Index (formerly the Vibrant Economy Index) – now in its third year. The Sustainable Growth Index seeks to define and measure the components that create successful places. Our aim in establishing the Index was to create a tool to help frame future discussions between all interested parties, stimulate action and drive change locally. We have undergone a process of updating the data for English Local Authorities on our online, interactive tool, and have produced an updated report on what the data means. All information is available on our online hub, where you can read the new report and our regional analyses.

The Sustainable Growth Index provides an independent, data-led scorecard for each local area that provides:

- businesses with a framework to understand their local economy and the issues that will affect investment decisions both within the business and externally, a tool to support their work with local enterprise partnerships, as well as help inform their strategic purpose and CSR plans in light of their impact on the local social and economic environment
- policy-makers and place-shapers with an overview of the strengths, opportunities and challenges of individual places as well as the dynamic between different areas
- Citizens with an accessible insight into how their place is doing, so that they can contribute to shaping local discussions about what is important to them

The Index shows the 'tip of the iceberg' of data sets and analysis our public services advisory team can provide our private sector clients who are considering future locations in the UK, or wanting to understand the external drivers behind why some locations perform better than others.

Our study looks at over 50 indicators to evaluate all the facets of a place and where they excel or need to improve.

Our index is divided into six baskets. These are:

- 1 Prosperity
- 2 Dynamism and opportunity
- 3 Inclusion and equality
- 4 Health, wellbeing and happiness
- 5 Resilience and sustainability
- 6 Community trust and belonging

This year's index confirms that cities have a consistent imbalance between high scores related to prosperity, dynamism and opportunity, and low scores for health, wellbeing, happiness inclusion and equality. Disparity between the richest and poorest in these areas represents a considerable challenge for those places.

Inclusion and equality remains a challenge for both highly urban and highly rural places and coastal areas, particularly along the east coast from the North East to Essex and Kent, face the most significant challenges in relation to these measures and generally rank below average.

Creating sustainable growth matters and to achieve this national policy makers and local authorities need to do seven things:

- 1 Ensure that decisions are made on the basis of robust local evidence.
- 2 Focus on the transformational trends as well as the local enablers
- 3 Align investment decisions to support the creation of sustainable growth
- 4 Align new funding to support the creation of sustainable growth
- 5 Provide space for innovation and new approaches
- 6 Focus on place over organisation
- 7 Take a longer-term view

The online report is available here:

<https://www.grantthornton.co.uk/en/insights/sustainable-growth-index-how-does-your-place-score/>



Institute for Fiscal Studies – English local government funding: trends and challenges in 2019 and beyond

The Institute for Fiscal Studies (IFS) has found “The 2010s have been a decade of major financial change for English local government. Not only have funding levels – and hence what councils can spend on local services – fallen significantly; major reforms to the funding system have seen an increasing emphasis on using funding to provide financial incentives for development via initiatives such as the Business Rates Retention Scheme (BRRS) and the New Homes Bonus (NHB).”

The IFS goes on to report “Looking ahead, increases in council tax and additional grant funding from central government mean a boost to funding next year – but what about the longer term, especially given plans for further changes to the funding system, including an expansion of the BRRS in 2021–22?”

This report, the first of what we hope will be an annual series of reports providing an up-to-date analysis of local government, does three things in this context. First, it looks in detail at councils’ revenues and spending, focusing on the trends and choices taken over the last decade. Second, it looks at the outlook for local government funding both in the short and longer term. And third, it looks at the impact of the BRRS and NHB on different councils’ funding so far, to see whether there are lessons to guide reforms to these policies.

The report focuses on those revenue sources and spending areas over which county, district and single-tier councils exercise real control. We therefore exclude spending on police, fire and rescue, national park and education services and the revenues specifically for these services. When looking at trends over time, we also exclude spending on and revenues specifically for public health, and make some adjustments to social care spending to make figures more comparable across years. Public health was only devolved to councils in 2013–14, and the way social care spending is organised has also changed, with councils receiving a growing pot of money from the NHS to help fund services.”

The IFS reports a number of key facts and figures, including

- 1) Cuts to funding from central government have led to a 17% fall in councils’ spending on local public services since 2009–10 – equal to 23% or nearly £300 per person.
- 2) Local government has become increasingly reliant on local taxes for revenues.
- 3) Councils’ spending is increasingly focused on social care services – now 57% of all service budgets.

The IFS report is available on their website below:

<https://www.ifs.org.uk/publications/14563>



