

# Audit Progress & Technical Update

North East Lincolnshire Council

July 2020



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# AUDIT PROGRESS

## Purpose of this report

This report provides the Audit Committee with an update on progress in delivering our responsibilities as your external auditor.

The audit plan is also part of the agenda of this meeting. Since its issue, a number of the timescales have changed as a consequence of the Covid-19 impact, which includes an updated draft accounts target of 31 August 2020 and audit opinion target of 30 November 2020. We have a team in place to complete this work in September 2020 and will update the committee on progress at the next meeting in September.

## Covid-19 Financial Reporting Issues

There are a number of key financial reporting issues arising as a direct result of Covid-19. As at the date of writing, the most significant are set out below and have been shared with management.

### Valuation of Land & Buildings

- [RICS guidance](#) has been issued which indicates that valuers are likely to conclude that there is “material uncertainty” over the valuation of land and buildings at the balance sheet date. We will need to consider the implications as part of our testing and conclusions.

### Financial Assets (receivables)

- Whilst the Government has introduced a number of measures to ease financial hardship, the Council will consider the impact on expected credit losses or impairment of financial assets

### Sources of estimation uncertainty, including pension fund assets and liabilities

- The Council is required to provide disclosures regarding the key sources of estimation uncertainty that management has made in preparing the financial statements, specifically those with a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the ensuing financial year.
- Information on pension assets and liabilities are obtained via the pension fund and we will consider the implications of any matters arising through the pension fund audit in our work.

## Progress to date

To-date we completed our interim work including:

- updating work on planning and walking through the Council’s main financial and supporting feeder systems; and
- testing expenditure and journals.

There are no matters to report to you in respect of this testing.

## 2. NATIONAL PUBLICATIONS

	Publication/update	Key points	Page
<b>Public Sector Audit Appointments</b>			
1	<b>Publication of 2020/21 scale of audit fees</b>	PSAA has written to all Councils setting out the next year's external audit fees	5
<b>National Audit Office</b>			
2	<b>New Code of Audit Practice 2020/21</b>	Publication of the Code of Practice that prescribes the focus of the external audit and auditor reporting for five years from 2020/21	6
3	<b>Round-up for Audit Committees</b>	Updated 'round-up' of resources for Audit Committees	6
4	<b>Local authority investment in commercial property</b>	Report on the developments of LA investments in commercial property	6
<b>Chartered Institute of Public Finance and Accountancy (CIPFA)</b>			
5	<b>Local Government Financial Resilience index</b>	Online data tool which measures local authorities against a range of indicators to assess their level of resilience.	7
6	<b>IFRS9 Financial Instruments: A guide for Local Authority practitioners</b>	Updated guidance to assist Councils to comply with the requirements of IFRS9	7
7	<b>IFRS 16 Leases: An Early Guide for Local Authority Practitioners</b>	Guidance to assist the preparations for the 2020/21 application of IFRS16	8
<b>Ministry of Housing, Communities &amp; Local Government (MHCLG)</b>			
8	<b>Final local government finance settlement: England, 2020 to 2021</b>	Announcement of the finance settlement for 2020/21	9
9	<b>Northamptonshire County Council: fourth commissioners' report</b>	Report from the appointed commissioner	9
<b>Other</b>			
10	<b>Statement on Covid-19, Financial Reporting Council and other Regulators</b>	Statement on the impact of the Covid-19 pandemic on accounting, reporting and auditing	9

## 2. NATIONAL PUBLICATIONS – PSAA

### 1. PSAA 2020/21 scale of audit fees, March 2020

PSAA has published the fee scale for the audit of the 2020/21 accounts of opted-in principal local government and police bodies, and wrote to those bodies to notify them of the fee.

The 2020/21 fee scale document sets out the scale of fees for the audit work to be undertaken by appointed auditors in respect of the 2020/21 financial statements at relevant principal authorities that have opted into PSAA's national auditor appointment arrangements.

PSAA describes in their letter that local audit and audit more widely is subject to a great deal of turbulence with significant pressures on fees. In their letter they conclude that

“we do not expect the final audit fee to remain at that level for most if not all bodies because of a variety of change factors, the impact of which cannot be accurately or reliably estimated at this stage. The impact of these changes is likely to vary between bodies depending on local circumstances, and information to determine that impact with any certainty is not yet available. Our view is that it would also be inappropriate to apply a standard increase to all authorities given the differing impact of these changes between bodies. As the impact of these changes is understood, fee variations will need to be identified and agreed reflecting the impact on each audit.”

<https://www.psa.co.uk/audit-fees/2020-21-audit-fee-scale/>

## 2. NATIONAL PUBLICATIONS – NATIONAL AUDIT OFFICE

### 2. New Code of Audit Practice 2020/21, February 2020

The NAO have published their final draft of the Code following the consultation process. The Code has now been laid before Parliament and, subject to Parliamentary approval, will come into force on 1 April 2020. The new Code will apply from audits of local bodies' 2020/21 financial statements onwards.

Accompanying the Code is a document that sets out the issues the NAO considered as a result of the feedback to Stage 2 of the consultation on the exposure draft of the Code, and highlights the key changes made to the text of the final draft of the Code.

[https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2020/01/Code\\_of\\_audit\\_practice\\_2020.pdf](https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2020/01/Code_of_audit_practice_2020.pdf)

[https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2020/01/Code\\_of\\_audit\\_practice-consultation\\_response.pdf](https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2020/01/Code_of_audit_practice-consultation_response.pdf)

### 3. Round-up for Audit Committees, November 2019

This interactive round-up of NAO publications is intended to help Audit Committees, Boards and other users by outlining the latest NAO resources for governance and oversight, risk management and strategic management issues. It also sets out how to keep in touch with NAO insight on specific issues and/or sectors.

This round-up is designed to make it easy for Audit Committees, Boards and other users to find the NAO resources most helpful for the strategic management of public sector organisations. It includes an introduction by Gareth Davies, Comptroller and Auditor General, and draws particular attention to publications most useful for governance, oversight and risk management. It is published each autumn and spring, covering NAO publications over the previous six months.

<https://www.nao.org.uk/report/round-up-for-audit-committees/>

### 4. Local authority investment in commercial property, February 2020

In response to substantial falls in funding since 2010/11, local authorities have made reductions in revenue spending on services. Increasingly, authorities have also sought to offset funding reductions by generating new income through a range of strategies. A key component within these responses has been a rapid expansion in the acquisition of commercial property, often funded by borrowing.

The NAO estimates that authorities spent £6.6 billion on purchasing commercial property from 2016/17 to 2018/19 – 14.4 times more than in the preceding three years. This includes an estimated £3.1 billion on acquiring offices; £2.3 billion on retail property, including £759 million on shopping centres or units within them and £957 million on industrial property. The majority of the £6.6 billion was spent by only 49 local authorities, with those authorities accounting for 80% of the spend. Many authorities have borrowed to finance these purchases. The NAO estimates that between 38% and 91% of spending on these purchases across the sector was financed by borrowing in this period.

The report concludes that although there is evidence of authorities mitigating these risks, such as by recruiting specialist staff, undertaking due diligence on their purchases, drawing on external expertise and establishing contingency funds, there was room for improvement in the governance and risk mitigation arrangements of some authorities.

The Ministry of Housing, Communities and Local Government (MHCLG) is responsible for the framework of statutory codes and guidance that set the parameters for local authority borrowing and capital spending. MHCLG has made changes to aspects of the framework in response to the recent increased investment in commercial property. Recent activity has raised questions about the extent to which MHCLG can rely on the present framework to support authorities to make decisions which demonstrate good value for money.

The NAO recommends that MHCLG improves the relevance and quality of data and analysis it has on authorities' acquisition of commercial property to understand more fully any risks and to provide greater assurance that authorities are complying with the framework. It also recommends that the Ministry should review whether the current framework is still achieving its intended aims.

<https://www.nao.org.uk/report/local-authority-investment-in-commercial-property/>

## 2. NATIONAL PUBLICATIONS – CIPFA

### 5. Local Government Financial Resilience index, CIPFA, December 2019

The resilience index is an online data tool which measures local authorities against a range of indicators to assess their level of resilience against financial shocks and to support financial decision making. Upper tier authorities are judged against nine indicators including social care.

The indicators measured include:

- levels of reserves;
- change in reserves;
- reserves sustainability;
- interest payable/net revenue expenditure;
- gross external debt;
- social care ratio;
- fees and charges to service expenditure ratio;
- council tax requirement/net expenditure ratio; and
- growth above baseline.

The tool allows for year on year comparisons of each authority's performance, as well as comparisons with similar and neighbouring authorities. Trend analysis is also available for some of the indicators outlined above.

<https://www.cipfa.org/about-cipfa/press-office/latest-press-releases/cipfa-launches-local-government-financial-resilience-index>

### 6. IFRS 9 Financial Instruments: A Guide for Local Authority Practitioners, CIPFA, December 2019

The Code of Practice on Local Authority Accounting in the UK adopted IFRS 9 Financial Instruments in its 2018/19 edition, with an application date of 1 April 2018.

In order to allow practitioners to prepare in good time, CIPFA issued guidance in 2017 in advance of the 2018/19 Code being published, based on a companion publication to the 2017/18 Code: Forthcoming Provisions for IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers in the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.

This publication updates the 2017 guidance to reflect:

- provisions in the 2018/19 Code that were not included in the Forthcoming Provisions publication
- changes to the 2019/20 Code resulting from amendments to IFRS 9
- experience of implementing IFRS 9 in the 2018/19 annual accounts.

This guidance provides comprehensive coverage of the requirements of the Code, including recognition, measurement, treatment of gains and losses, derecognition and presentation and disclosure in the financial statements. It also covers statutory reversals and the continuing impact of transitional provisions.

<https://www.cipfa.org/policy-and-guidance/publications/i/frs-9-financial-instruments-a-guide-for-local-authority-practitioners>

## 2. NATIONAL PUBLICATIONS – CIPFA

### 7. IFRS 16 Leases: An Early Guide for Local Authority Practitioners, CIPFA, December 2019

Although changes will not have an effect until the 2020/21 financial statements, CIPFA/LASAAC consulted in the summer of 2018 on amendments to the Code of Practice on Local Authority Accounting for IFRS 16 Leases. The Standard is expected to have a potentially significant practical and financial effect for local authorities, and it was considered that early notice of the technical requirements was advisable.

It will be of wide interest because of the prevalence of leasing in local government and the risk that the changes could have a budgetary impact if not managed effectively.

This guidance provides comprehensive coverage of the proposed requirements for lessees, including the accounting definition of a lease, recognition of assets and liabilities, measurement, derecognition and presentation, and disclosure in the financial statements. Although there have not been significant changes to the requirements for lessors, the guidance includes extensive commentary of this area.

The guidance covers in particular:

- identifying arrangements that meet the accounting definition of a lease
- determining the term of a lease where there are options to extend or terminate
- for lessees:
  - recognising right-of-use assets and lease liabilities, and their initial and subsequent measurement
  - reassessment of lease liabilities and treatment of lease modifications
- for lessors, distinguishing between finance and operating leases and accounting accordingly
- dealing with sale and leaseback transactions
- presenting lease transactions and balances in the financial statements
- disclosure of information about leases in the notes to the accounts
- harmonising with statutory accounting requirements
- the mechanics of making the transition in the 2020/21 financial statements (including the application of transitional provisions and the preparation of relevant disclosure notes).

<https://www.cipfa.org/policy-and-guidance/publications//ifrs-16-leases-an-early-guide-for-local-authority-practitioners>

## 2. NATIONAL PUBLICATIONS – MHCLG/OTHER

### 8. Final local government finance settlement: England, 2020 to 2021, February 2020

Following the provisional settlement, the Ministry of Housing, Communities and Local Government published the collection of documents that comprise the final settlement for Local Government.

<https://www.gov.uk/government/collections/final-local-government-finance-settlement-england-2020-to-2021>

### 9. Northamptonshire County Council: fourth commissioners' report, January 2020

MHCLG have published the fourth commissioner's report into Northamptonshire County Council. This report sets out the progress made to stabilise the council's finances, and to strengthen the council's scrutiny and governance processes. The commissioner's work continues to support the setting up of the 2 new shadow authorities from May 2020.

<https://www.gov.uk/government/publications/northamptonshire-county-council-fourth-commissioners-report>

### 10. Statement on Covid-19, Financial Reporting Council and other Regulators, March 2020

A joint statement was issued by the Financial Reporting Council, the Financial Conduct Authority and Prudential Regulation Authority in response to the current situation.

The statement sets out that:

*“Successful and sustainable businesses underpin our economy and society by providing employment and creating prosperity. Equity and debt capital markets play a vital role providing finance to these businesses and will aid the recovery. Governments and regulators around the world remain focused on keeping capital markets open and orderly.*

*Capital markets rely on timely, accurate information. Investors and other stakeholders rely on financial reporting – backed by high-quality auditing. However, companies and their auditors currently face unprecedented challenges in preparing and auditing financial information”*

The statement highlights:

- The likelihood of an increase in the number of modified audit opinions (where there are difficulties in obtaining evidence or other issues);
- Increased going concern assumption considerations and uncertainties; and
- Guidance for companies and auditors.

<https://www.fca.org.uk/news/statements/joint-statement-fca-frc-pra>