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Gloucester City Council
Transforming Your City

Planning report to the Audit & Governance Committee for the year ending 31 March 2021

Issued on 26 February 2021 for Audit & Governance Committee meeting on 8 March 2021

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Audit lead introduction

The key messages in this report

I have pleasure in presenting our planning report to the Audit & Governance Committee for the audit of the 2020/21 financial statements. I would like to draw your attention to the key messages of this paper:

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the financial statements;
- A strong understanding of your internal control environment; and
- A well planned and delivered audit that raises findings early with those charged with governance.

Audit Plan

We have updated our understanding of the Council including discussion with management and review of relevant documentation from across the Council.

Based on these procedures, we have developed this plan in collaboration with the Council to ensure that we provide an effective audit service that meets your expectations and focuses on the most significant areas of importance and risk to the Council.

Key Risks

We have taken an initial view as to the significant audit risks the Council faces. These are presented as a summary dashboard on page 12.

Regulatory Change

The National Audit Office has issued a revised Code of Audit Practice for 2020/21, including a significantly revised approach to "Value for Money" work. This requires a wider scope of underlying work, and introduces narrative reporting for all bodies in a new public "Annual Auditor's Report" issued at the same time as the audit opinion.

The audit approach reflects changes to International Standards on Auditing (UK) on going concern (ISA (UK) 570) and management estimates (ISA (UK) 540), and Practice Note 10, effective for this year.

IFRS 16, Leases has been further delayed and will apply from 2021/22.

Our Commitment to Quality

We are committed to providing the highest quality audit, with input from our market leading specialists, sophisticated data analytics and our wealth of experience.

Michelle Hopton
Audit Lead

Responsibilities of the Audit & Governance Committee

Helping you fulfil your responsibilities

Why do we interact with the Audit & Governance Committee?

To communicate audit scope

To provide timely and relevant observations

To provide additional information to help you fulfil your broader responsibilities

As a result of regulatory change in recent years, the role of the Audit & Governance Committee has significantly expanded. We set out here a summary of the core areas of Audit & Governance Committee responsibility to provide a reference in respect of these broader responsibilities.

Oversight of external audit

- At the start of each annual audit cycle, ensure that the scope of the external audit is appropriate.
- Make recommendations as to the auditor appointment and implement a policy on the engagement of the external auditor to supply non-audit services.

Integrity of reporting

- Impact assessment of key judgements and level of management challenge.
- Review of external audit findings, key judgements, level of misstatements.
- Assess the quality of the internal team, their incentives and the need for supplementary skillsets.
- Assess the completeness of disclosures, including consistency with disclosures on business model and strategy and, where requested by the Committee, provide advice in respect of the fair, balanced and understandable statement.
- Assess and advise the board on the appropriateness of the Annual Governance Statement, including conclusion on value for money.

Internal controls and risks

- Review the internal control and risk management systems
- Explain what actions have been, or are being taken to remedy any significant failings or weaknesses.

Oversight of internal audit

- Monitor and review the effectiveness of the internal audit activities.

Whistle-blowing and fraud

- Ensure that appropriate arrangements are in place for the proportionate and independent investigation of any concerns that are raised by staff in connection with improprieties.

Our audit explained

We tailor our audit to your business and your strategy

Identify changes in your business and environment

We have spent time with management understanding the current year matters, such as Covid-19 arrangements and prepared our risk assessment for the audit. We will continue to keep this under review throughout the audit process.

Scoping

We anticipate our scope to be in line with the Code of Audit Practice issued by the NAO.

More detail is given on page 7.

In our final report

In our final report to you we will conclude on the significant risks identified in this paper, report to you our other findings, and detail those items we will be including in our audit report.

Determine materiality

We have determined a materiality of £2.272m (2019/20 £2.072m). This is based on 2% of total expenditure per the Council's yearend forecast. We will report to you any misstatements above £113k (2019/20 £103k). We will report to you misstatements below this threshold if we consider them to be material by nature (i.e. relating to senior staff remuneration). We note that our materiality calculation will be updated during the final audit based on total expenditure per the 2020/21 accounts.

Significant risk assessment

We have identified significant audit risks in relation to the Council. More detail is given on page 11 to 15.

Quality and Independence

We confirm all Deloitte network firms and engagement team members are independent of Gloucester City Council. We take our independence and the quality of the audit work we perform very seriously. Audit quality is our number one priority.

Your control environment

What we consider when we plan the audit

We expect management and those charged with governance to recognise the importance of a strong control environment and take proactive steps to deal with deficiencies identified on a timely basis.

Responsibilities of management

Auditing standards require us to only accept or continue with an audit engagement when the preconditions for an audit are present. These preconditions include obtaining the agreement of management and those charged with governance that they acknowledge and understand their responsibilities for, amongst other things, internal control as is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Responsibilities of the Audit & Governance Committee

As previously noted in the Responsibilities of the Audit & Governance Committee on page 6, the Audit & Governance Committee is responsible for:

- Reviewing the internal control and risk management systems (unless expressly addressed by separate board risk committee).
- Explaining what actions have been, or are being taken to remedy any significant failings or weaknesses.

As stakeholders tell us that they wish to understand how external audit challenges and responds to the quality of an entity's control environment, we are seeking to enhance how we plan and report on the results of the audit in response. We will be placing increased focus on how the control environment impacts the audit, from our initial risk assessment, to our testing approach and how we report on misstatements and control deficiencies.

Scope of work and approach

Scope: we have three key areas of responsibility under the Audit Code

Financial statements

We will conduct our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISA (UK and Ireland)") as adopted by the UK Auditing Practices Board ("APB") and Code of Audit Practice issued by the National Audit Office ("NAO"). The Council will prepare its accounts under the Code of Practice on Local Authority Accounting ("the Code") issued by CIPFA and LASAAC.

We are also required to issue a separate assurance report to the NAO on the Council's separate return required for the purposes of its audit of the Whole of Government Accounts and departmental accounts.

Annual Governance Statement

We are required to consider the completeness of the disclosures in the Annual Governance Statement in meeting the relevant requirements and identify any inconsistencies between the disclosures and the information that we are aware of from our work on the financial statements and other work.

As part of our work we will review the annual report and compare with other available information to ensure there are no material inconsistencies. We will also review any reports from other relevant regulatory bodies and any related action plans developed by the Council.

Value for Money (VfM) conclusion

We are required to satisfy ourselves that the Council has made proper arrangements for securing financial resilience and economy, efficiency and effectiveness in its use of resources.

The updated Code of Audit Practice changes the approach of external audit work away from the auditor performing a risk assessment, and then only performing further work if a significant risk were identified, to specifying procedures that will need to be undertaken in each of three areas:

– Financial sustainability;

- Governance and Improving economy; and

- Efficiency and effectiveness.

This will require a minimum level of work at every local public body, with additional risk based work where relevant.

Scope of work and approach
Our approach

Liaison with internal audit

The Auditing Standards Board's version of ISA (UK and Ireland) 610 "Using the work of internal auditors" prohibits use of internal audit to provide "direct assistance" to the audit. Our approach to the use of the work of Internal Audit has been designed to be compatible with these requirements.

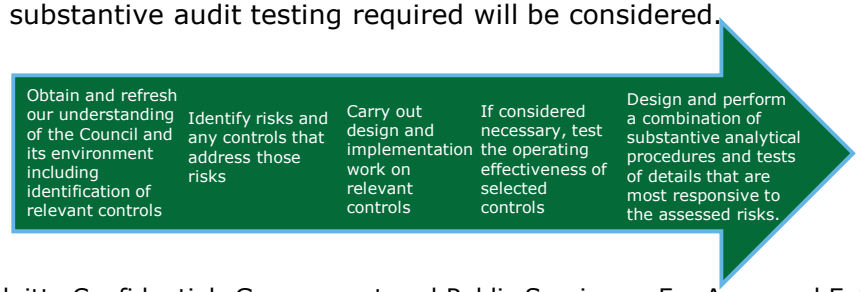
We will review their reports and meet with them to discuss their work where necessary. We will review the work plan for internal audit, and where they have identified specific material deficiencies in the control environment we consider adjusting our testing so that the audit risk is covered by our work.

Using these discussions to inform our risk assessment, we can work together with internal audit, where necessary, to develop an approach that avoids inefficiencies and overlaps, therefore avoiding any unnecessary duplication of audit requirements on the Council's staff.

Approach to controls testing

Our risk assessment procedures will include obtaining an understanding of controls considered to be 'relevant to the audit'. This involves evaluating the design of the controls and determining whether they have been implemented ("D&I").

The results of our work in obtaining an understanding of controls will be collated and the impact on the extent of substantive audit testing required will be considered.



Promoting high quality reporting to stakeholders

We view the audit role as going beyond reactively checking compliance with requirements: we seek to provide advice on evolving good practice to promote high quality reporting.

We recommend the Council complete the Code checklist during drafting of their financial statements.

We would welcome early discussion on the planned format of the financial statements, and whether there is scope for simplifying or streamlining disclosures, as well as the opportunity to review a skeleton set of financial statements and an early draft of the annual report ahead of the typical reporting timetable to feedback any comments to management.

Value for Money and other reporting

The Updated Code of Audit Practice changes the approach of external audit work away from the auditor performing a risk assessment, and then only performing further work if a significant risk were identified, to specifying procedures that will need to be undertaken in each of three areas – Financial sustainability; Governance and Improving economy, efficiency and effectiveness.

This will require a minimum level of work at every local public body, with additional risk based work where relevant. The National Audit Office (NAO) has recently issued an audit procedures scope and discussions on implementation are ongoing.

We will report by exception any matters we identify that indicate the Governance Statement does not comply with the CIPFA guidance, or is misleading or inconsistent with information of which we are aware from our audit. We are not required to consider, nor will we consider, whether the Annual Governance Statement addresses all risks and controls or that risks are satisfactorily addressed by internal controls.

Continuous communication and reporting

Planned timing of the audit

As the audit plan is executed throughout the year, the results will be analysed continuously and conclusions (preliminary and otherwise) will be drawn. The following sets out the expected timing of our reporting to and communication with you. Please note timing of the Grant work will be communicated separately.

Planning	Interim	Year end fieldwork	Reporting activities
Planning meetings to inform risk assessment; and agree on key judgemental accounting issues. Document our understanding of the Council and key controls and business cycle processes relating to the financial reporting process reporting. Review of key Council documents including Cabinet, Council and Audit & Governance Committee minutes.	Document design and implementation of key controls and update understanding of key business cycles for any changes. Substantive testing of limited areas including fixed asset additions, expenditure, payroll, certain areas of income. Value for Money work.	Substantive testing of all areas. Finalisation of work in support of value for money responsibilities. Detailed review of annual accounts and report, including Annual Governance Statement. Review of final internal audit reports and opinion. Completion of testing on significant audit risks.	Year-end closing meetings Reporting of significant control deficiencies Signing audit reports in respect of Financial Statements Issuing Annual Audit Letter Issuing audit completion certificate.
2020/21 Audit Plan		Final report to the Audit & Governance Committee	
December - January 2020	February – April 2021	June - September 2021	September 2021

Ongoing communication and feedback

Materiality

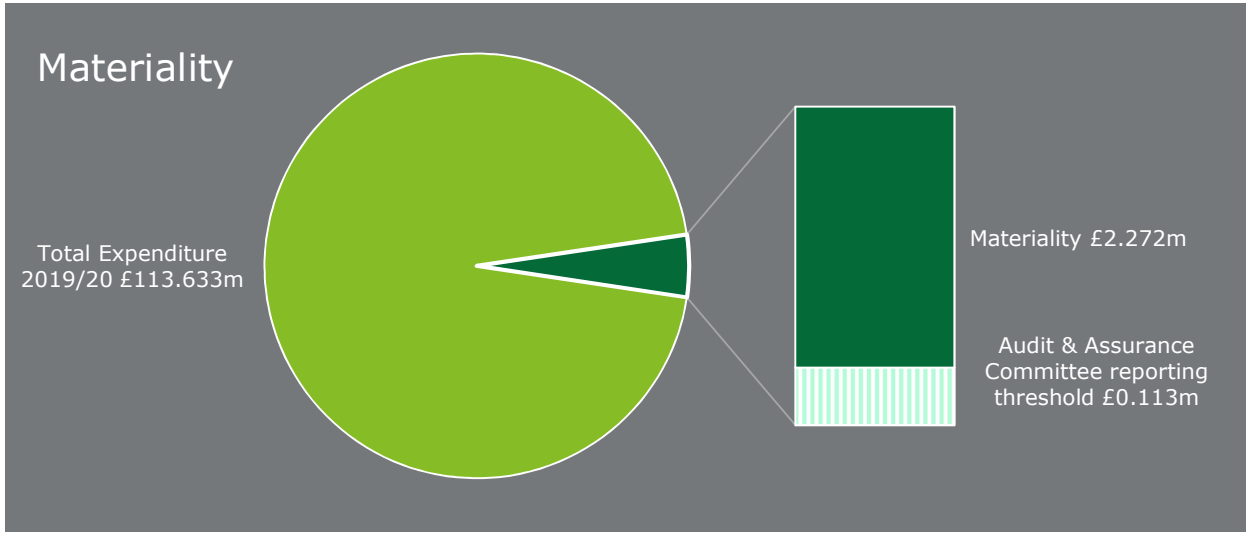
Our approach to materiality

Basis of our materiality benchmark

- The audit lead has determined materiality as £2.272m (2019/20 £2.072m), based on professional judgement, the requirement of auditing standards and the financial measures most relevant to users of the financial statements.
- We have used 2% of total expenditure based on the Council's 2019/20 actual expenditure as the benchmark for determining materiality.
- We will re-visit the determined materiality at year end to take into account of any additional expenditure for 2020/21 due to Covid-19.

Reporting to those charged with governance

- We will report to you all misstatements found in excess of £113k (2019/20 £103k).
- We will report to you misstatements below this threshold if we consider them to be material by nature.



Although materiality is the judgement of the audit lead, the Audit & Governance Committee must satisfy themselves that the level of materiality chosen is appropriate for the scope of the audit.

Significant risks

Our risk assessment process

We consider a number of factors when deciding on the significant audit risks. These factors include:

- the significant risks and uncertainties previously reported in the annual report and financial statements;
- the IAS 1 critical accounting estimates previously reported in the annual report and financial statements;
- our assessment of materiality; and
- the changes that have occurred in the business and the environment it operates in since the last annual report and financial statements.

Deloitte view

Management must carefully consider the principal risks, uncertainties and accounting estimates of the Council.

Expected principal risks

- Property valuations
- Impairment
- Pension Liability
- Provision for Business Rates Appeals
- Funding Settlement
- Regulatory

IAS 1 Critical accounting estimates

- Impairment
- Provisions and contingencies
- Property valuations

Changes in your business and environment

The Covid-19 pandemic broke out just prior to the end of the prior year, however the majority of the impact of the pandemic was incurred in 2020/21 financial year. This is due to the role that local government has played in the distribution and providing Covid-19 grants to local businesses and benefits to the local residents.
Furthermore, Gloucester City Council has obtained full Council approval for the development of all plots of the Kings Quarter – The Forum, development for a total cost of £107m.

The next page summarises the significant risks that we will focus on during our audit.

Significant Audit Risks

Dashboard

Risk	Material	Fraud risk	Planned approach to controls	Level of management judgement	Expected to be included in our report to the Audit and Governance Committee	Slide no.
Completeness of Creditors	✓	✓	D+I	⚠	✓	13
Property Valuations	✓		D+I	⚠	✓	14
Management Override of Controls	✓	✓	D+I	⚠	✓	15

D+I: Assessing the design and implementation of key controls

Low Level of Judgement ⚠

Medium Level of Judgement ⚠

High Level of Judgement ⚠

Significant Audit Risks

Risk 1 – Completeness of Creditors

Risk identified	Under UK auditing standards, there is a presumed risk of revenue recognition due to fraud. We have rebutted this risk, and instead believe that the fraud risk lies with the completeness of creditors. For 2020/21, the Council approved a budget with a net cost of service of £0.1m. As at December 2020, the Council reported a forecast spend of £69.8m, resulting in a forecast overspend of £0.2m. The Council did not achieve a balanced position in the prior year. Given the Council's current budget position and the pressures across the whole of the public sector, there is an inherent risk that the year-end position could be manipulated by omitting or misstating accruals.
Our response	Our work in this area will include the following: We will obtain an understanding of the design and implementation of the key controls in place in relation to recording completeness of creditors; We will perform focused testing in relation to the completeness of creditors by completing focused unrecorded liability testing; and We will review the year on year movement in accruals and will investigate any significant movements.

Significant Audit Risks

Risk 2 – Property Valuations

Risk identified	The Council held £69.36m of property assets (Other land and building) at 31 March 2020. The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Council has adopted a rolling revaluation model which sees all land and buildings revalued over a four year cycle. However the Council is completing a full revaluation in the current year. The Council has a capital plan which for 2020/21 of £8.86m. At month 9 the Council reported actual spend of £4.57m and a forecast spend of £7.03m for the year. There is a risk that new capital expenditure could result in an impairment either due to the valuation exercise or for the existing assets being replaced or upgraded. As well as that the Council is currently in the process of approving the next phase of the Kings Quarter development which will be significant. The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Council used a rolling revaluation model which sees all land and buildings revalued over a four year cycle, in the previous years but will go through a full revaluation of their portfolio by a mix of internal and external reviewers.
Our response	• We will test the design and implementation of key controls in place around the property valuation, as part of the interim audit. • We will test the inputs used in the valuation including the gross internal areas provided to the valuer. • We will use our valuation specialists, Deloitte Real Estate if required, to review and challenge the appropriateness of the assumptions used in the year-end valuation of the Council's Land and Buildings. • We will consider the presentation of revaluation movements and impairments, taking into account revaluation reserves for individual assets, and the disclosures included in the financial statements. • We will challenge management's assessment whether any impairment arises in respect of newly capitalised expenditure. We expect to include this risk in our audit report because it will have a significant effect upon our overall audit strategy, allocation of resources, and the direction of the efforts of the team.

Significant Audit Risks

Risk 3 – Management Override of Controls

Risk identified	In accordance with ISA 240 (UK) management override is a significant risk. This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Council's controls for specific transactions. The key judgments in the financial statements are those which we have selected to be the significant audit risks and areas of audit interest: completeness of creditors and valuation of the Council's estate and pension liability. These are inherently the areas in which management has the potential to use their judgment to influence the financial statements.
Our response	In considering the risk of management override, we plan to perform the following audit procedures that directly address this risk: We will test the design and implementation of key controls in place around journal entries and management estimates; We will risk assess journals and select items for detailed testing. A sample of journal entries will be selected using computer-assisted profiling based on areas which we consider to be of increased interest. The appropriateness of these journals will be assessed through detailed testing; We will review accounting estimates for biases that could result in material misstatements due to fraud; and, We will obtain an understanding of the business rationale of significant transactions that we become aware of that are outside of the normal course of business for the Council, or that otherwise appear to be unusual, given our understanding of the entity and its environment.

Other Areas of Audit Interest

Pensions Liability Valuation

Risk identified	The Council are part of the Local Government Pension Scheme operated by Gloucestershire County Council. The Council recognised a combined pensions liability of £69m at 31 March 2019 which decreased to £56m as at 31 March 2020. The Code requires that their year end carrying value should reflect the appropriate fair value at that date. Hymans Robertson act as the Pension Fund's expert actuary, who produce a report outlining the liability and disclosures required for each council. The pensions valuation is an area of audit interest due to the material values attached to the valuations and disclosures in the financial statements. This has not been classified as a significant risk as there are limited movements in the membership data, and we understand that the assumptions and methodologies used are consistent with those in the previous years. We also understand that there have been no significant changes in the membership of the scheme or accrual of benefits for the year.
Our response	We carry out a separate, detailed risk assessment of each of the individual components of the calculation (for example market assumptions, membership data, assets and liabilities) using a developed methodology which takes into account factors such as an assessment of the actuary. We scope our work, including the nature and extent of our actuarial specialists involvement, in a way which responds to this detailed risk assessment. Should our risk assessment change our overall audit approach in respect of testing pensions, we will notify the Committee. We will confirm the disclosure of the pension figures in the statement of accounts agree with those provided by the scheme actuary.

Value for Money
Areas of focus

Value for Money

The new Code of Audit Practice for 2020/21 onwards. The Code is applicable to NHS Trusts and Foundation Trusts, CCGs, and Local Authorities. This introduced significant changes to the requirements around Value for Money (the arrangements to secure economy, efficiency, and effectiveness in the use of resources). Auditor Guidance Note 03 (AGN03), Value for Money, setting out more detailed guidance on how the new requirements should be implemented. Key features of the requirements include:

For all bodies, the auditor will need to provide a public narrative commentary against the Value for Money criteria in a new "Auditor's Annual Report" (AAR), to be issued alongside the audit opinion for Local Authorities. This commentary will include a summary against each of the reporting criteria, setting out the work undertaken, and judgements and local context relevant to the findings. This commentary needs to be supported by more extensive work to understand the body's arrangements to secure economy, efficiency and effectiveness, to support this commentary and to identify whether there are risks of significant weaknesses in arrangements.

If a risk of significant weaknesses is identified, additional work is required to determine whether there are significant weaknesses and to make relevant recommendations if this is the case on a timely basis, which will also be explained in the Auditor's Annual Report. The AAR will also include follow up on previous recommendations in respect of significant weaknesses and whether they've been implemented satisfactorily. The audit opinion will continue to include reporting by exception, though now this will be where the auditor has identified a significant weakness in arrangements rather than an overall conclusion on arrangements. The three criteria that would be considered in Value for Money work are be:

Financial sustainability: How the body plans and manages its resources to ensure it can continue to deliver its services;

Governance: How the body ensures that it makes informed decisions and properly manages its risks; and

Improving economy, efficiency and effectiveness: How the body uses information about its costs and performance to improve the way it manages and delivers its services.

The National Audit Office and the audit firms are continuing to discuss the practical implementation of these new requirements and expectations as to the extent of procedures underpinning these requirements. Expectations in this area are likely to continue to evolve as practical issues emerge in implementation.

We will:

- Undertake VfM planning work under the revised procedures.
- We have agreed with management the timing for performing additional work in March, ahead of the year-end. When the national timetable is announced, we will discuss any implications with the Council.
- As the detailed impact on scope becomes clearer, we will discuss and agree the impact of the required scope changes with management.
- Our year-end reporting will include our draft findings ahead of issue of the Auditor's Annual Report and separate Value for Money opinion.

Maintaining audit quality

Responding to challenges in the current audit market

This is a time of intense scrutiny for our profession with questions over the role of auditors, market choice and the provision of non-audit services by an audit firm. We welcome the debate and are engaging fully with all parties who have an interest in the current audit market reform initiatives, so that our profession, our people, our clients and most importantly, the public interest, are served to the highest standards of audit quality and independence.

The role of audit	• Public confidence in audit has weakened over recent years and the expectation gap has widened with differences between what an audit does and what people think it should do (largely in areas of internal controls, fraud, front half assurance and long term viability) • Deloitte fully supports an independent review into the role of auditors • The Government's Brydon Review will consider UK audit standards and how audits should evolve
Would it be better to have audit only firms?	• Deloitte believes that multidisciplinary firms have more knowledge, greater access to technology and a deeper talent pool. The specialist input from industry, valuation, controls, pensions, cyber, solvency, IT and tax services are critical to an effective audit. • Our investment in audit innovation, training and technology is greater because of the multidisciplinary model
Is the current audit market uncompetitive?	• We recognise that the competition for large, complex clients is fierce, but we wholeheartedly support greater choice being available to stakeholders • There are barriers to entry in the listed market that are significant including the required global reach, unlimited liability, and the high cost of tendering • The audit profession has engaged with the Competition and Markets Authority with ideas on how to provide greater choice in the market, and responded to the CMA's suggested market remedies
Independence and conflicts from other services	• Legislation and the FRC's Ethical Standard restrict the services we may provide to audit clients • Deloitte invests heavily in systems, processes and people to check for potential conflicts • We have governance in place to assess any areas of potential conflict, including where required to protect the public interest • Fees for non-audit services to audit clients have fallen since 2008 (17% to 7.3% of firm revenue)
Deloitte	• Deloitte and Audit Service Line leadership are happy to meet the Board and management of our clients with respect to this important debate. We reaffirm our commitment to quality, independence and upholding the public interest • Our Impact Report and Transparency Report are available on our website https://www2.deloitte.com/uk/en/pages/about-deloitte-uk/articles/annual-reports.html • Our response to the latest AQR report is on slide 23.

Revisions to auditing standards coming into effect

ISA (UK) 570 – Going concern

The Financial Reporting Council (FRC) issued a revised going concern standard in September 2019, that takes effect for periods commencing on or after 15 December 2019. For NHS bodies, this will be March 2021 year ends and later.

The revision was made in response to recent enforcement cases and well-publicised corporate failures where the auditor's report failed to highlight concerns about the prospects of entities which collapsed shortly after.

We have summarised below the key areas of change in the standard:

- Risk assessment procedures and related activities, increasing consideration of the entity's business model, operations and financing
- The auditor's evaluation of management's assessment of the going concern assumption (which therefore requires a clearly documented assessment)
- Enhanced professional scepticism requirements, including around the evaluation of the sufficiency and appropriateness of audit evidence
- Considering the appropriateness of disclosures; and
- Reporting in enhanced audit reports.

The Public Audit Forum has issued a revised Practice Note 10, which reflects public sector considerations in the approach to going concern, and in particular where it may be appropriate to adopt a "continued provision of services" approach to the going concern assumption. The National Audit Office is intending to issue specific guidance for NHS and local authority audit, which together with Practice Note 10 will determine the ultimate impact of the ISA (UK) 570 changes.

"The revised standard means UK auditors will follow significantly stronger requirements than those required by current international standards."

FRC's press release, 30 September 2019

Revisions to auditing standards coming into effect

ISA (UK) 540 – Auditing Accounting Estimates and Related Disclosures

Since 2015, the International Auditing and Assurance Standards Board (IAASB) has sought to identify audit issues relating to accounting estimates for financial institutions and other entities. Initially, this focused on the impact of IFRS 9 *Financial Instruments*, because it would fundamentally change the way that banks and other entities account for loan assets and other credit exposures.

However, the IAASB concluded that most, if not all, issues identified for expected credit losses would be equally relevant when auditing other complex accounting estimates. Accordingly, a holistic revision of ISA 540 was undertaken and the new standard takes effect for periods commencing on or after 1 January 2020. For NHS bodies, this will be March 2021 year ends and later.

We summarise on the next few slides how this will impact our audit.

"There is a clear need to update ISA 540 to support better quality audits of increasingly complex accounting estimates"

FRC letter to the IAASB, July 2017

Area of change	Impact on our audit	Impact on the management
Assessment of oversight and governance relating to estimates	In connection with our planning work to understand the entity and its environment, including internal control, we will specifically inquire regarding management's processes, and the oversight and governance of those processes relating to accounting estimates.	You will need to consider the adequacy of your processes and controls over estimates, and documentation thereof.

Revisions to auditing standards coming into effect

ISA (UK) 540 – Auditing Accounting Estimates and Related Disclosures

Area of change	Impact on our audit	Impact on the management
Identification of inherent risk factors; separate assessment of inherent risk and control risk	Recognising a spectrum of inherent risk, we will assess risks of material misstatement in estimates with reference not only to estimation uncertainty, but also complexity, subjectivity or other inherent risk factors, and the interrelationship among them.	You will need to provide clear documented rationale for (a) the selection and application of the method, assumptions and data in making the accounting estimate, including any changes in the current year, and controls relating to those aspects; and/or (b) the selection of a point estimate and related disclosures for inclusion in the financial statements.
Objectives-based work effort requirements	We will specifically assess control risk relating to estimates, which may require us to evaluate the design and determine implementation of an increased number of internal controls. Our subsequent audit procedures will be responsive to this assessment, and designed to obtain evidence around the methods, significant assumptions, data and (where applicable) the selection of a point estimate and related disclosures about estimation uncertainty.	
Enhanced "stand back" requirement, to evaluate the audit evidence obtained	We will specifically design our procedures, to enhance our application of professional scepticism, so that they are not biased towards finding corroborative evidence; our overall evaluation of the evidence obtained will weigh both corroborative and contradictory evidence.	You should expect more challenge of the evidence provided in support of accounting estimates, use of external data sources and your consideration of contradictory evidence.

Revisions to auditing standards coming into effect

ISA (UK) 540 – Auditing Accounting Estimates and Related Disclosures

Area of change	Impact on our audit	Impact on the management
Enhanced requirements about whether disclosures are "reasonable"	The extant ISA 540 required us to evaluate whether disclosures were "adequate". The change to "reasonable" will involve greater consideration of the overall meaning conveyed through disclosures. For example, where estimation uncertainty associated with an estimate is multiple times materiality, we will consider whether the disclosures appropriately convey the high degree of estimation uncertainty and the range of possible outcomes.	You should expect more challenge on disclosures relating to estimates, particularly for where you have selected a point estimate from a range and those with high estimation uncertainty.
New requirements when communicating with those charged with governance	In accordance with ISA (UK) 260 and ISA (UK) 265, our communications from the audit have included significant qualitative aspects of your accounting practices and significant deficiencies in internal control. With the revised ISA (UK) 540, these communications will specifically include matters regarding accounting estimates and take into account whether the reasons for our risk assessment relate to estimation uncertainty, or the effects of complexity, subjectivity or other inherent risk factors.	You should expect increased reporting in relation to accounting estimates.

Areas where we consider the impact to be greatest:

Key areas impacted will include property valuations (discussed on page 14), revenue recognition and provisioning, accruals and provisions.

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our report is designed to establish our respective responsibilities in relation to the financial statements audit, to agree our audit plan and to take the opportunity to ask you questions at the planning stage of our audit. Our report includes:

- Our audit plan, including key audit judgements and the planned scope.

What we don't report

As you will be aware, our audit is not designed to identify all matters that may be relevant to the Council.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, the views on internal controls and business risk assessment in our final report should not be taken as comprehensive or as an opinion on effectiveness since they will be based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

Use of this report

This report has been prepared for the Council, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

Other relevant communications

We will update you if there are any significant changes to the audit plan.

We welcome the opportunity to discuss our report with you and receive your feedback.

Deloitte LLP

Bristol | 26 February 2021

Appendices

Fraud responsibilities and representations

Responsibilities explained

Your Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Our responsibilities:

- We are required to obtain representations from your management regarding internal controls, assessment of risk and any known or suspected fraud or misstatement.
- As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.
- As set out in the significant risks section of this document, we have identified the risk of fraud in relation to the completeness of expenditure and management override of controls as key audit risks for your organisation.

Fraud Characteristics:

- Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional.
- Two types of intentional misstatements are relevant to us as auditors – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.

We will request the following to be stated in the representation letter signed on behalf of the Board:

- We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.
- We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- We are not aware of any fraud or suspected fraud / We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity or group and involves:
  - (i) management;
  - (ii) employees who have significant roles in internal control; or
  - (iii) others where the fraud could have a material effect on the financial statements.
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

Fraud responsibilities and representations

Inquiries

We will make the following inquiries regarding fraud:

Management:

- Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Management's process for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to employees regarding its views on business practices and ethical behaviour.
- Whether management has knowledge of any actual, suspected or alleged fraud affecting the entity.
- We plan to involve management from outside the finance function in our inquiries.

Internal audit

- Whether internal audit has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain its views about the risks of fraud.

Those charged with governance

- How those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks.
- Whether those charged with governance have knowledge of any actual, suspected or alleged fraud affecting the entity.
- The views of those charged with governance on the most significant fraud risk factors affecting the entity.

Independence and fees

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of Gloucester City Council and will reconfirm our independence and objectivity to the Audit & Governance Committee for the year ending 31 March 2021 in our final report to the Audit & Governance Committee .
Fees	Details of the fees proposed for the period have been presented separately on the next page. There are no non-audit fees.
Non-audit services	In our opinion there are no inconsistencies between the FRC's Ethical Standard and the Council's approach for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.
Relationships	We have not other relationships with the Council, its directors, senior managers and affiliates, and have not supplied any services to other known connected parties.

Independence and fees

The professional fees expected to be charged by Deloitte LLP in the period from 1 April 2020 to 31 March 2021 are as follows:

	Current year £ (excluding VAT)	Current year £ (excluding VAT)
Gloucester City Council Financial Statements		
Financial statement audit including Whole of Government Accounts and procedures in respect of Value for Money assessment	TBC	48,857
Grant Audit		
Audit in accordance with DWP specification to include case checks from the headline cells and completion of the DWP workbooks.	10,000*	10,000*
Total audit	**TBC**	**58,857**
Total fees	**TBC**	**58,857**

*Where additional (40+) testing is required either under the CAKE requirements or due to detection of errors. Cases for testing will be selected by the audit team and communicated to the Authority's team for testing. Team will then perform limited subsampling of the results of this testing. Additional £1,500 of fees per cohort of 40+ testing will be required.
Furthermore, where drafting and agreeing a qualification letter is required, there will be additional fees of £1,500.

We confirm all Deloitte network firms are independent of the Council. We take our independence and the quality of the audit work we perform very seriously. Audit quality is our number one priority

Deloitte fees and planned timescales for completion of the audit are based on the following assumptions:

- the financial statements are provided in accordance with the agreed timescales, to the quality expected and have been subject to a robust quality assurance review;
- information provided to support the financial statements is in accordance with the agreed audit deliverables document;
- appropriate accommodation and facilities are provided to enable the audit team to deliver the audit in an efficient manner;
- all appropriate officials will be available during the audit;
- you have all the necessary controls and checks in place to enable the Responsible Financial Officer to provide all the assurances that are required in the Letter of Representation addressed to the engagement partner; and
- Internal Audit's planned programme of work is complete and management has responded to issues that may have affected the financial statements.

Our approach to quality

AQR team report and findings

Audit quality remains our number one priority and we have a relentless commitment to it. We continue to invest in and enhance our Audit Quality Monitoring and Measuring programme.

In July 2020 the Financial Reporting Council ("FRC") issued individual reports on each of the seven largest firms, including Deloitte, on Audit Quality Inspections providing a summary of the findings of its Audit Quality Review ("AQR") team for the 2019/20 cycle of reviews.

We greatly value the FRC reviews of our audit engagements and firm wide quality control systems, a key aspect of evaluating our audit quality.

We are pleased with our results for the inspections of FTSE 350 entities achieving 90% assessed as good or needing limited improvement, which included some of our highest risk audits. Our objective is for 100% of our audits to be assessed as good or needing limited improvement and we know we still have work to do in order to meet this standard. We are however, extremely disappointed one engagement received a rating of significant improvements required during the period. This is viewed very seriously within Deloitte and we have worked with the AQR to agree a comprehensive set of swift and significant firm wide actions.

We are also pleased to see the impact of our previous actions on prior year adjustments is reflected in the results of current year inspections with no findings in this areas. In addition the FRC identified good practice examples including in: risk assessment, group oversight, our comprehensive IFRS9 expected credit loss audit programme and our audit committee reporting.

Embedding a culture of challenge in our audit practice underpins the key pillars of our audit strategy. We invest continually in our firm wide processes and controls, which we seek to develop globally, to underpin consistency in delivering high quality audits whilst ensuring engagement teams exercise professional scepticism through robust challenge.

All the AQR public reports are available on its website. https://www.frc.org.uk/auditors/audit-quality-review/audit-firm-specific-reports

Our approach to quality

AQR team report and findings

The AQR's 2019/20 Audit Quality Inspection Report on Deloitte LLP

"We reviewed 17 individual audits this year and assessed 13 (76%) as requiring no more than limited improvements. Of the ten FTSE 350 audits we reviewed this year, we assessed nine (90%) as achieving this standard."

"We have highlighted in this report aspects of firm-wide procedures which should be improved, including strengthening the monitoring of the firm's audit quality initiatives."

"Our key findings related principally to the need to:

- Improve the extent of challenge over cash flow forecasts in relation to the impairment of goodwill and other assets.
- Enhance the effectiveness of substantive analytical review and other testing for revenue.
- Improve the assessment and extent of challenge regarding management's estimates, particularly for model testing."

"The firm has taken steps to address the key findings in our 2019 public reports, with actions that included focused training and standardising the firm's audit work programs. We have identified improvements, for example in the audit of potential prior year adjustments and related disclosures, a key finding last year. We also identified good practice in a number of areas of the audits we reviewed (including effective group oversight and robust risk assessment) and in the firm-wide procedures (including the firm's milestone program, with expected dates for the phasing of the audit monitored by the firm)."

Our approach to quality

AQR team report and findings

Improve the extent of challenge over cash flow forecasts in relation to the impairment of goodwill and other assets.

How we have addressed this area as a firm

- We expanded the scope of our impairment centre of excellence consultation requirement to include material intangible assets and property, plant and equipment balances where the valuation is supported by a value-in-use calculation, for FTSE 350 entities or other PIEs where there is a significant risk.
- We have also expanded the requirements when certain criteria are met, such as the engagement being considered higher risk, to include a further consultation and review by the specialist of the conclusions and how planned actions have been addressed. This also ensures that appropriate prioritisation has taken place.
- The Audit Blueprint will also support audit teams to be able to more consistently flag issues with management, Boards and Audit Committees when it is clear that the Council's information is not ready for audit in accordance with the agreed audit timetable.

In addition, we have taken, or are taking, the following supporting actions:

- We have updated our consultation template to reflect the most recent inspection findings. We also held training sessions in late 2019 for all the impairment specialists who perform the consultations, one of which was attended by the FRC, to share updates on recent inspection findings and areas to consider ahead of the December year-end consultations.
- We communicated the FRC findings to the wider audit practice via our monthly compulsory professional update in October 2019, which we record and distribute online and attendance is monitored. This included a presentation from the FRC inspection team.
- We discussed these enhanced requirements in a training session in January 2020 with all partners and practitioners who perform a quality review role, including those formally acting as Engagement Quality Control Reviewers.

This is recognised as a significant audit risk, Recognition of NHS clinical revenue, and is addressed on page 15 of this Plan.

Our approach to quality

AQR team report and findings

Enhance the effectiveness of substantive analytical review and other testing for revenue.

How we have addressed this area as a firm

To address this finding, we have done, or plan, the following:

- Included the approach to the audit of revenue as one of our Engagement Team Based Learning 'on the job' coaching sessions for the 2020 programme. These programmes tackle live audit matters and also gather teams after an audit to perform a learning debrief. Our intention is that focusing on the overall approach together as a team will ensure our teams understand transaction flows and together challenge the overall approach to ensure that tests are designed appropriately;
- We communicated in our monthly compulsory professional update in November 2019 the areas of challenge, and the FRC inspection team also presented their observations;
- In early 2020 we issued an updated practice aid for performing substantive analytical reviews, providing more guidance to those completing this work. This practice aid highlights the pitfalls identified in 2019/20 external inspections; and
- We plan to do a deep dive session as part of our monthly professional update on substantive analytical reviews in the summer, ahead of December year-end planning work. This will ensure that teams focus at the planning stage on whether substantive analytical review is appropriate, the independence of data sources and the overall body of evidence on revenue considering all elements of testing.

Our approach to quality

AQR team report and findings

Improve the assessment and extent of challenge regarding management's estimates, particularly for model testing.

How we have addressed this area as a firm

We are developing a guide which can be shared with audited entities to set out clear expectations of what is required from management in preparation for the audit of management estimates, and this is linked to our overall Audit Blueprint.

We are introducing a pilot of an additional document to capture in one place the partner-led challenge on management estimates at the end of the audit process, in advance of the implementation of ISA 540 revised which has a "step back" challenge.

In relation to the specific points noted by the FRC, we also highlight the following actions we have taken:

1. Given this was the first year of implementation of IFRS 9 and given the complexity of the expected credit loss estimates required under that standard, we were very pleased that the FRC considered the model audit programme that we developed to be of a high standard. We have continued to develop our audit approach to reflect the lessons we learned from our first year auditing expected credit losses including ensuring the findings raised by the FRC were addressed.

2. We have enhanced the audit training given to all specialists used in audits such as valuations, property, forensic accounting, insolvency, IT, pensions, tax and valuations in order to continually enhance those specialists knowledge of audit quality issues so that their specialist input is targeted accordingly and brings further challenge to the audit process.

3. We have increased the focus given to assessing the risks of material misstatement in the actuarial models used by life insurance companies and ensuring that the response to those risks is appropriate, whether performed by actuarial specialists or the core audit team.

4. We have provided additional guidance to teams on how to use independently developed ranges to assess the reasonableness of the estimates made by management.

The actions we have taken, in particular to enhance scepticism and challenge, will be ever more relevant as the impacts of COVID-19 further heighten the levels of estimation uncertainty which we have to address in audits.

This relates to an audit risk identified as an *Other Matter* Property Valuations, and is addressed on page 17 of this Plan.

We have ensured that all audit team members have been provided with our management estimates practice aid.

Deloitte.