Grant Thornton

The Annual Audit Letter for Exeter City Council

Year ended 31 March 2020

9 December 2020

Contents

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Executive Summary

Purpose

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at Exeter City Council (the Council) and its subsidiaries (the group) for the year ended 31 March 2020.

This Letter is intended to provide a commentary on the results of our work to the Group and external stakeholders, and to highlight issues that we wish to draw to the attention of the public. In preparing this Letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'. We reported the detailed findings from our audit work to the Council's Audit and Governance Committee as those charged with governance in our Audit Findings Report on 19 November 2020 and the subsequent addendum.

Respective responsibilities

We have carried out our audit in accordance with the NAO's Code of Audit Practice, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

- give an opinion on the Council and group's financial statements (section two)
- assess the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources (the value for money conclusion) (section three).

In our audit of the Council and group's financial statements, we comply with International Standards on Auditing (UK) (ISAs) and other guidance issued by the NAO.

Our work

Materiality	We determined materiality for the audit of the Council's financial statements to be £2,169,000 (Group £2,171,000), which is 2% of the group's gross expenditure.
Financial Statements opinion	We gave an unqualified opinion on the group's financial statements on 30 November 2020. We included an emphasis of matter paragraph in our report in respect of the uncertainty over valuations of the Council's land and buildings, investment properties and the property assets of the pension fund assets given the Coronavirus pandemic. This does not affect our opinion that the statements give a true and fair view of the group's financial position and its income and expenditure for the year. This was a national issue arising from the pandemic and the Council's valuer followed the national guidance issued by RICs in this area.
Whole of Government Accounts (WGA)	We completed work on the Council's consolidation return following guidance issued by the NAO.
Use of statutory powers	We did not identify any matters which required us to exercise our additional statutory powers.
Value for Money arrangements	We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources. We reflected this in our audit report to the Council on 30 November 2020.
Certificate	We certified that we have completed the audit of the financial statements of Exeter City Council in accordance with the requirements of the Code of Audit Practice on 30 November 2020.

Working with the Council

We would like to take this opportunity to record our appreciation for the assistance and timely collaboration provided by the finance team and other staff during these unprecedented times.

Grant Thornton UK LLP
November 2020

Audit of the Financial Statements

Our audit approach

Materiality

In our audit of the group's financial statements, we use the concept of materiality to determine the nature, timing and extent of our work, and in evaluating the results of our work. We define materiality as the size of the misstatement in the financial statements that would lead a reasonably knowledgeable person to change or influence their economic decisions.

We determined materiality for the audit of the group financial statements to be £2,171,000, which is 2**%** of the group's expenditure. We determined materiality for the audit of the Council's financial statements to be £2,169,000, which is 2**%** of the Council's gross expenditure. We used this benchmark as, in our view, users of the group and Council's financial statements are most interested in where the group and Council has spent its revenue in the year.

We also set a lower level of specific materiality for senior officer remuneration which we determined to be 2% of the amount disclosed for Senior Officer remuneration.

We set a lower threshold of £108,000, above which we reported errors to the Audit and Governance Committee in our Audit Findings Report.

The scope of our audit

Our audit involves obtaining sufficient evidence about the amounts and disclosures in the financial statements to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error. This includes assessing whether:

- the accounting policies are appropriate, have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management are reasonable; and
- the overall presentation of the financial statements gives a true and fair view.

We also read the remainder of the Statement of Accounts to check it is consistent with our understanding of the Council and group and with the financial statements included in the Statement of Accounts on which we gave our opinion.

We carry out our audit in accordance with ISAs (UK) and the NAO Code of Audit Practice. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach was based on a thorough understanding of the group's business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks and the results of this work.

Audit of the Financial Statements

Significant Audit Risks

These are the significant risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Covid-19 The global outbreak of the Covid-19 virus pandemic has led to unprecedented uncertainty for all organisations, requiring urgent business continuity arrangements to be implemented. We expected current circumstances would have an impact on the production and audit of the financial statements for the year ended 31 March 2020, including and not limited to: • remote working arrangements and redeployment of staff to critical front line duties that may impact on the quality and timing of the production of the financial statements, and the evidence we could obtain through physical observation; • volatility of financial and property markets which would increase the uncertainty of assumptions applied by management to asset valuations and receivable recovery estimates, and the reliability of evidence we could obtain to corroborate management estimates; • financial uncertainty would require management to reconsider financial forecasts supporting their going concern assessment and whether material uncertainties for a period of at least 12 months from the anticipated date of approval of the audited financial statements had arisen; and • disclosures within the financial statements could require significant revision to reflect the unprecedented situation and its impact on the preparation of the financial statements as at 31 March 2020 in accordance with IAS1, particularly in relation to material uncertainties. We therefore identified the Covid-19 pandemic as a significant risk.	We: • worked with management to understand the implications that the response to the Covid-19 pandemic had on the Council's ability to prepare the financial statements and update financial forecasts, and assessed the implications on our audit approach. We received draft financial statements in advance of the revised national timetable, but later than originally planned; • liaised with other audit suppliers, regulators and government departments to co-ordinate practical cross sector responses to issues as and when they arose. An example is in respect of the material valuation uncertainty disclosed by the Council's valuation experts in respect of land and buildings and investment properties which was a national issue; • evaluated the adequacy of the disclosures in the financial statements in light of the Covid-19 pandemic; • evaluated whether sufficient audit evidence using alternative approaches could be obtained for the purposes of our audit whilst working remotely; • evaluated whether sufficient audit evidence could be obtained to corroborate significant management estimates such as asset valuations and recovery of receivable balances; and • evaluated management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment.	The Covid-19 pandemic resulted in land and building, Council Dwelling and investment property valuations being reported on a 'material uncertainty' basis. This was also the case for the investment properties held by the Devon Pension Fund on behalf of the Council. This was a national issue related to the Covid-19 pandemic and the Council followed national guidance from RICS in it's valuations. The accounts disclosures were updated to reflect the increased estimation uncertainty and we included an Emphasis of Matter in our audit report in respect of this matter to draw the reader's attention to the Council's disclosures.

Audit of the Financial Statements

Significant Audit Risks - continued

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Management override of internal controls Under ISA (UK) 240, there is a non-rebuttable presumed risk that the risk of management override of controls is present in all entities. The Council faces external scrutiny of its spending and this could potentially place management under undue pressure in terms of how they report performance. We therefore identified management override of control, in particular journals, management estimates, and transactions outside the course of business as a significant risk.	We: • evaluated the design effectiveness of management controls over journals; • analysed the journals listing and determined the criteria for selecting high risk and unusual journals; • tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration; • gained an understanding of the accounting estimates and critical judgements applied made by management and considered their reasonableness with regard to corroborative evidence; and • evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions.	We did not identify any significant matters to bring to the attention of those charged with governance.

Audit of the Financial Statements

Significant Audit Risks - continued

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Valuation of pension fund net liability The pension fund net liability, as reflected in the Council's balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements. The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£106.2m) and the sensitivity of the estimate to changes in key assumptions.	We: • updated our understanding of the processes and controls put in place by management to ensure that the Council's pension fund net liability is not materially misstated, and evaluated the design of the associated controls; • evaluated the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work; • assessed the competence, capabilities and objectivity of the actuary who carried out the Council's pension fund valuation; • assessed the accuracy and completeness of the information provided by the Council to the actuary to estimate the liability; • tested the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuary's report; and • undertook procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performed additional procedures suggested within the report.	We did not identify any matters to bring to the attention of those charged with governance.

Audit of the Financial Statements

Significant Audit Risks - continued

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Valuation of land and buildings, Investment property and HRA dwellings The Council re-values its land and buildings on a five-yearly rolling basis to ensure that carrying value is not materially different from fair value. HRA dwellings and investment properties are valued annually. This represents a significant estimate by management in the financial statements due to the size of the numbers involved (£261.6m for Council Dwellings, £127.9m for other land and buildings and £54.8m for investment properties) and the sensitivity of the estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value of assets not revalued as at 31 March 2020 in the Council's financial statements is not materially different from the current value at the financial statements date, where a rolling programme is used. The Council's valuer undertakes a desktop exercise for all assets not valued as part of the rolling programme to ensure that this is the case.	We: • evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work; • evaluated the competence, capabilities and objectivity of the valuation experts; • wrote to the valuers to confirm the basis on which the valuations were carried out; • selected a sample of in-year valuations to test; • tested the sampled revaluations made during the year to see if they had been input correctly into the Council's asset register; • challenged information and assumptions used by the valuers for the sampled assets to assess completeness and consistency with our understanding; and • evaluated the assumptions made by management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value at year end.	Guidance from RICS in its valuation of land, buildings and investment properties instructed valuers, nationally, to include a material uncertainty paragraph in their valuation reports with regards to the movement of property prices and valuations as a result of Covid-19. Given the magnitude of the Council Dwellings, land and buildings and investment property valuations to the balance sheet and the caveat made by the valuers in their valuation reports, we highlighted the material uncertainty in our audit report in an Emphasis of Matter (EOM) paragraph, drawing attention to the disclosures made in the statement of accounts in Note 5. We requested the disclosures be made clearer in the accounts in respect of the material uncertainty for land and buildings, Council dwellings and investment property valuations and this was actioned in the final version of the Statement of Accounts. The EOM paragraph does not qualify the opinion but refers to management's disclosure on the material uncertainty that, in our judgement, is of such importance that it is fundamental to users' understanding of the financial statements. We did not identify any other matters to bring to the attention of those charged with governance.

Audit of the Financial Statements

Audit opinion

We gave an unqualified opinion on the Group's financial statements on 30 November 2020.

Preparation of the financial statements

The Council presented us with draft financial statements in August 2020 in advance of the revised national timetable, and provided a good set of working papers to support them. The finance team responded promptly and efficiently to our queries during the course of the audit.

New remote access working arrangements i.e. remote accessing of financial systems, video calling, and procedures to confirm the completeness and accuracy of information produced by the entity proved to be a challenge for all auditors. Additional work was also required on the Council’s property valuations and pensions estimates in line with regulator expectations, with additional time and consultation also experienced on the prior year adjustment identified. All of this meant the that the audit took longer than planned.

Issues arising from the audit of the financial statements

We reported the key issues from our audit to the Council’s Audit and Governance Committee on 25 November 2020 and provided a short summary addendum on 30 November 2020 prior to issuing our audit report.

Annual Governance Statement and Narrative Report

We are also required to review the Council’s Annual Governance Statement and Narrative Report. It published them on its website in the draft Statement of Accounts in August 2020.

Both documents were prepared in line with the CIPFA Code and relevant supporting guidance. We confirmed that both documents were consistent with the financial statements prepared by the Council and with our knowledge of the Council.

Whole of Government Accounts (WGA)

We carried out work in line with instructions provided by the NAO. We issued an assurance statement which confirmed the Council was below the audit threshold.

Other statutory powers

We also have additional powers and duties under the Act, including powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about the Council's accounts and to raise objections received in relation to the accounts.

We issued a statement of reasons in response to an objection raised as part of the 2018/19 audit. This was presented to the Audit and Governance Committee on 25 November 2020.

No statutory powers were exercised in respect of the 2019/20 audit.

Certificate of closure of the audit

We certified that we have completed the audit of the financial statements of Exeter City Council in accordance with the requirements of the Code of Audit Practice on 30 November 2020.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice, following the guidance issued by the NAO in April 2020 which specified the criterion for auditors to evaluate:

In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.

Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the risks where we concentrated our work.

The risk we identified and the work we performed is set out overleaf.

Overall Value for Money conclusion

We are satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2020.

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan
Financial sustainability The Council's 2020/21 financial plan includes identified savings of £2.3m. There remains a requirement to find additional savings of £3.7m over the following three financial years. All non-statutory services are under pressure to deliver savings and there is a risk that the Council could fail to set balanced budgets in the future.
How we responded to the risk
As part of our work we considered: • the Council's arrangements for setting it's 2019/20 budget and five year medium term financial plan to 31 March 2024; • how these evolved through discussion and reporting; • the Council's monitoring and flexing of the budget through 2019/20; • the Council's 2019/20 financial outturn; and • the Council's response to the Covid-19 pandemic on it's income and expenditure streams.
Findings and conclusions
Planning and assumptions The Council set it's 2019/20 budget and updated its five year Medium Term Financial Plan (MTFP) in January 2019. At this point the Council was forecasting that it required additional savings of £2.6m by 2022/23. In the report the Council set out it's assumptions as follows: • inflationary pressures of £0.6m • decreased income resources of £0.4m • additional spending pressures of £1.1m • identified savings of £2m The resulting budget was balanced, though the projected total additional savings required by 2022/23 of £2.6m were not yet identified. **2019/20 Outturn** Monitoring throughout year demonstrated that the budget was being met with quarter 2 forecasting an underspend of £0.1m and quarter 3 monitoring indicating that there was likely to be an underspend of £0.8m. The outturn for 2019/20 resulted in a transfer of the £1.5m underspend to theGeneral Fund, primarily as a result of

Value for Money conclusion

Value for Money Risks

Findings and conclusions (CONTINUED)

the waiving of the 2019/20 Voluntary Revenue Provision charge and a clawback of previous year's voluntary amounts set aside. This was considered prudent when anticipating the expected income losses for 2020/21 resulting from the Covid-19 lockdown, and was deemed to be in accordance with the regulations in respect of such charges.

Identified savings were reported as part of the budget setting and were built into the Council's budget forecasts. Savings targets in year were achieved with few minor variances on expenditure being reported in the outturn.

Medium term financial plan

In January 2020 the Council revised its Medium Term Financial Plan and was forecasting that it required additional savings of £3.6m by 2023/24. This was subsequently overtaken by the effects of the Covid-19 pandemic. In March 2020 the Council's Section 151 officer was reporting that it had become evident that there were significant risks to the Council's income streams for 2020/21, in light of Covid-19 and in particular in relation to car parking, markets and halls and commercial rents due to the anticipated significant reduction in footfall.

Following the national lockdown, in June 2020 the Council's Section 151 officer reported that the Council faced a projected £10.4m shortfall against which the Government had provided £1.4m in grant. Although Government funding has been made available it does not address all of the lost income and the forecast effects going forward. In October 2020 a revised budget was agreed for 2020/21 which relied on the use of £1.4m of reserves to break-even, however at the end of Quarter 1 2020/21 this had fallen to a forecast use of reserves of £0.9m.

The ongoing repercussions of Covid-19 restrictions and the second lockdown will prove a challenge to the Council. Government support to date has been welcomed but does not mitigate all of the negative financial impacts and with an expected one-year settlement announcement for 2021/22, financial planning into the medium term continues to be challenging.

However the Council remains in a reasonable position. Its General Fund balance at 31 March 2020 was £5.9m, almost twice the minimum level set of £3m. It also held £8.9m of earmarked reserves and the HRA reserve stood at £10.5m. Taking into account the Q2 2020/21 forecast of a use of balances of £0.9m, the Council would still have sufficient General Fund reserves in line with it's agreed policy. The reserves provide the Council with the time required to identify savings and to consider new ways of working to allow it to meet the projected financial challenges over the medium term.

Auditor view

Exeter is a reasonable position to address the challenges arising from Covid-19 and has taken steps to re-forecast it's finances to provide the Council with the time required to develop it's longer term financial response to the pandemic. The Council currently has a good level of reserves, however there is an identifiable funding gap going forward which will need to be addressed.

As such, we issued an unqualified Value for Money conclusion for 2019/20.

A. Reports issued and fees

We confirm below our final reports issued and fees charged for the audit.

Audit fees	Proposed fee
Council scale fee	44,573
Additional proposed audit fee at planning stage	9,850
Total proposed audit fees (excluding VAT) at planning	**54,523**
Further additional fees proposed at completion	8,165
Total proposed audit fees (excluding VAT) on completion	**62,688**

Reports issued

Report	Date issued
Audit Plan Addendum to the Audit Plan	March 2020 May 2020
Audit Findings Report and addendum	November 2020
Annual Audit Letter	December 2020

The Audit Plan presented in March 2020 included £9,850 of proposed additional fees to take account of the additional scepticism required on the audit, the raising of the bar by our regulator and the further work arising from local developments, including the group accounts now produced by the Council since the original scale fee setting. This is reflected in the total proposed audit fees at planning above.

Since the presentation of the audit plan, we added a significant risk to the audit following the impact of Covid-19. We have now reflected on the time taken to discharge our responsibilities this year and are proposing a further increase in fees of £8,180 in addition to those proposed at the planning stage of the audit. This brings the total proposed audit fee up to £62,703. Further details on the breakdown is provided on the next pages.

This further charge has not been entered into lightly but reflects only a proportion of the significant additional work we have had to undertake this year to discharge our responsibilities.

We have been discussing this issue with PSAA over the last few months and note these issues are similar to those experienced in the commercial sector and NHS. In both sectors there has been a recognition that audits will take longer, with commercial audit deadlines being extended by four months and the NHS deadline extended by a month. The FRC has also issued guidance to companies and auditors setting out its expectation that audit standards remain high and of additional work needed across all audits. The link attached https://www.frc.org.uk/covid-19-guidance-and-advice (see guidance for auditors) sets out the expectations of the FRC.

We have discussed and agreed these additional fees with the Director Finance. Please note that these proposed additional fees are subject to approval by PSAA in line with the Terms of Appointment.

A. Reports issued and fees

We confirm below our final reports issued and fees charged for the audit.

Audit area	£	Rationale for fee variation
PSAA scale fee	44,573	
Raising the bar	2,500	The Financial Reporting Council (FRC) has highlighted that the quality of work by all audit firms needs to improve across local audit. This will require additional supervision and leadership, as well as additional challenge and scepticism in areas such as journals, estimates, financial resilience and information provided by the entity.
Pensions – valuation of net pension liabilities under International Auditing Standard (IAS) 19	1,750	We have increased the granularity, depth and scope of coverage, with increased levels of sampling, additional levels of challenge and explanation sought, and heightened levels of documentation and reporting.
PPE Valuation – work of experts	1,750	We have increased the volume and scope of our audit work to ensure an adequate level of audit scrutiny and challenge over the assumptions that underpin PPE valuations.
Harbour accounts	950	The audit of the Authority's harbour accounts requires a separate Letter of Engagement and audit procedures over and above the Authority's statutory audit.
Group accounts	1,500	Since the original scale fee was determined by Public Sector Audit Appointments, the Authority produces group accounts and this requires additional audit work.
New Accounting Standards	1,500	You are required to respond effectively to new accounting standards and we must ensure our audit work in these new areas is robust. This year we will be responding to the introduction of IFRS16. There is a requirement, under IAS8, to disclose the expected impact of this change in accounting treatment in the 2019/20 financial statements.
Revised scale fee at planning (approved by PSAA)	**54,523**	

A. Reports issued and fees

Audit area	£	Rationale for fee variation
Revised scale fee (approved by PSAA, from previous page)	**54,523**	
Additional fees incurred as a result of Covid-19 additional work	7,680	Over the past six months the current Covid-19 pandemic has had a significant impact on all of our lives, both at work and at home. The impact of Covid-19 on the audit of the financial statements for 2019/20 has been multifaceted. This includes: • Revisiting planning - we have needed to revisit our planning and refresh risk assessments, materiality and testing levels. This has resulted in the identification of a significant risk at the financial statements level in respect of Covid-19 necessitating the issuing of an addendum to our original audit plan as well as additional work on areas such as going concern and disclosures in accordance with IAS1, particularly in respect of material uncertainties. • Management's assumptions and estimates - there is increased uncertainty over many estimates including pension and other investment valuations. Many of these valuations are impacted by the reduction in economic activity and we are required to understand and challenge the assumptions applied by management. • Financial resilience assessment – we have been required to consider the financial resilience of audited bodies. Our experience to date indicates that Covid-19 has impacted on the financial resilience of all local government bodies. This has increased the amount of work that we need to undertake on the sustainable resource deployment element of the VFM criteria necessitating enhanced and more detailed reporting in our ISA260. • Remote working – the most significant impact in terms of delivery is the move to remote working. We, as other auditors, have experienced delays and inefficiencies as a result of remote working, including delays in receiving accounts. These are understandable and arise from the availability of the relevant information and/or the availability of key staff (due to shielding or other additional Covid-19 related demands). In many instances the delays are caused by our inability to sit with an officer to discuss a query or working paper. Gaining an understanding via Teams or phone is more time-consuming.
Prior Year adjustment	500	The Council's 2019/20 Statement of Accounts includes a Prior Period Adjustment and includes a third balance sheet. This required additional review and internal consultation as part of our audit procedures.
Revised Fee (subject to PSAA approval)	**62,703**	

A. Reports issued and fees continued

Fees for non-audit services

Service	Fees £
Audit related services	
- Housing Benefit Subsidy return	17,298*
- Pooling of Capital receipts return 2019/20	5,000
Non-Audit related services	
- None	

*proposed fee, our work has yet to be concluded on the Council's Housing Benefits Subsidy return for 2019/20.

Non-audit services

For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Group. The table left summarises all non-audit services which were identified.

We have considered whether non-audit services might be perceived as a threat to our independence as the Group's auditor and have ensured that appropriate safeguards are put in place.

The identified non-audit services are consistent with the Group's policy on the allotment of non-audit work to your auditor.

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