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# Informing the audit risk assessment for Leicester City Council 2019/20



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## Purpose

The purpose of this report is to contribute towards the effective two-way communication between the Authority's external auditors and the Authority's Audit and Risk Committee, as 'those charged with governance'. The report covers some important areas of the auditor risk assessment where we are required to make inquiries of the Audit and Risk Committee under auditing standards.

### Background

Under International Standards on Auditing (UK and Ireland) (ISA(UK&I)) auditors have specific responsibilities to communicate with the Audit and Risk Committee. ISA(UK&I) emphasise the importance of two-way communication between the auditor and the Audit and Risk Committee and also specify matters that should be communicated.

This two-way communication assists both the auditor and the Audit and Risk Committee in understanding matters relating to the audit and developing a constructive working relationship. It also enables the auditor to obtain information relevant to the audit from the Audit and Risk Committee and supports the Audit and Risk Committee in fulfilling its responsibilities in relation to the financial reporting process.

### Communication

As part of our risk assessment procedures we are required to obtain an understanding of management processes and the Audit and Risk Committee's oversight of General Enquiries of Management; Fraud; Laws and Regulations; Going Concern; Related Parties; and Accounting Estimates.

### Purpose

This report includes a series of questions on each of these areas and the response we have received from the Authority's management. The Audit and Risk Committee should consider whether these responses are consistent with its understanding and whether there are any further comments it wishes to make.

## General Enquiries of Management

Question	Management response
1. What do you regard as the key events or issues that will have a significant impact on the financial statements for 2019/20?	There is no significant issues that will have an impact on the financial statements.
2. Have you considered the appropriateness of the accounting policies adopted by the City Council? Have there been any events or transactions that may cause you to change or adopt new accounting policies?	The Council has completed the annual review of their accounting policies to ensure appropriateness. There are no events or transactions that may cause us to change or adopt new accounting policies.
3. Is there any use of financial instruments, including derivatives?	The Council has no new types of financial instruments in addition to those in the accounts in 2018/19.
4. Are you aware of any significant transactions outside the normal course of business?	There is no significant transactions outside the normal course of business.

## General Enquiries of Management

Question	Management response
5. Are you aware of any changes in circumstances that would lead to impairment of non-current assets?	There are currently no circumstances that would lead to impairment of non-current assets.
6. Are you aware of any guarantee contracts?	There is a potential for a guarantee contract to be agreed prior to the end of the financial year, further detail of this will be provided during the audit.
7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements?	We are not aware of any loss contingencies.
8. Other than in house solicitors, can you provide details of those solicitors utilised by the City Council during the year. Please indicate where they are working on open litigation or contingencies from prior years?	The Council has used various solicitors during the year and will provide the detail to the auditors during the audit.
9. Have any of the City Council's service providers reported any items of fraud, non-compliance with laws and regulations or uncorrected misstatements which would affect the financial statements?	No.
10. Can you provide details of other advisors consulted during the year and the issue on which they were consulted?	This information will be provided as part of the audit working papers.

# Fraud

## Matters in relation to fraud

ISA(UK&I)240 covers auditors responsibilities relating to fraud in an audit of financial statements.

The primary responsibility to prevent and detect fraud rests with both the Audit and Risk Committee and management. Management, with the oversight of the Audit and Risk Committee, needs to ensure a strong emphasis on fraud prevention and deterrence and encourage a culture of honest and ethical behaviour. As part of its oversight, the Audit and Risk Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As the Authority's external auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error. We are required to maintain professional scepticism throughout the audit, considering the potential for management override of controls.

As part of our audit risk assessment procedures we are required to consider risks of fraud. This includes considering the arrangements management has put in place with regard to fraud risks including:

- assessment that the financial statements could be materially misstated due to fraud,
- process for identifying and responding to risks of fraud, including any identified specific risks,
- communication with the Audit and Risk Committee regarding its processes for identifying and responding to risks of fraud, and
- communication to employees regarding business practices and ethical behaviour.

We need to understand how the Audit and Risk Committee oversees the above processes. We are also required to make inquiries of both management and the Audit and Risk Committee as to their knowledge of any actual, suspected or alleged fraud. These areas have been set out in the fraud risk assessment questions herein together with responses from the Authority's management.

# Fraud risk assessment

Question	Management response
<p>1. Has the Authority assessed the risk of material misstatement in the financial statements due to fraud?</p> <p>How has the process of identifying and responding to the risk of fraud been undertaken and what are the results of this process?</p> <p>How does the Authority's risk management processes link to financial reporting?</p>	<p>Through independent challenge of the figures within the accounts and gaining assurance over controls from internal audit.</p> <p>If the Council identifies any concerns over internal controls then processes are reviewed and new controls are implemented. The Council has not identified any concerns over financial controls over the current year. We try to learn lessons from others experiences.</p> <p>When the Council identifies risks a review will be undertaken to identify any potential financial impact.</p>
<p>2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?</p>	<p>Procurement exercises/contracts, Right to Buy of council properties, small business rate relief and subletting council properties.</p>
<p>3. Are you aware of any instances of actual, suspected or alleged fraud, errors or other irregularities either within the Authority as a whole or within specific departments since 1 April 2019?</p> <p>As a management team, how do you communicate risk issues (including fraud) to those charged with governance?</p>	<p>The Council has a counter fraud team who are responsible for investigating instances of fraud.</p> <p>The team report to Audit and Risk Committee periodically, to provide an update on any instances of fraud and actions taken.</p>
<p>4. Have you identified any specific fraud risks?</p> <p>Do you have any concerns there are areas that are at risk of fraud?</p> <p>Are there particular locations within the Authority where fraud is more likely to occur?</p>	<p>The Council is at particular risk of fraud in the usual higher risk areas e.g repairs and maintenance, procurement and contract management.</p> <p>The Council has the relevant controls in place to try and prevent fraud. This is further supported by the reports of internal audit.</p>



# Fraud risk assessment

Question	Management response
<p>5. What processes does the Authority have in place to identify and respond to risks of fraud?</p>	<p>The Council has a clear governance framework summarised below;</p> <ul style="list-style-type: none"> <li>• Mayor, Executive &amp; Council</li> <li>• Decision Making</li> <li>• Risk Management</li> <li>• Scrutiny &amp; Review</li> <li>• Corporate Management Team</li> </ul> <p>Further to the Council has various codes and rules, including Financial Procedure Rules, Codes of Conducts, Anti-Fraud, Bribery &amp; Corruption Policy.</p> <p>Further to this the Council participates in the National Fraud Initiative.</p> <p>There are ongoing discussions with colleagues at Leicestershire County Council to explore the possibility of assessing each other's organisation using the CIPFA Code of Practice on Managing the Risk of Fraud and Corruption.</p>
<p>6. How would you assess the overall control environment for the Authority, including:</p> <ul style="list-style-type: none"> <li>• the process for reviewing the effectiveness the system of internal control;</li> <li>• internal controls, including segregation of duties;</li> <li>• exist and work effectively?</li> </ul> <p>If not where are the risk areas and what mitigating actions have been taken?</p> <p>What other controls are in place to help prevent, deter or detect fraud?</p> <p>Are there any areas where there is a potential for override of controls or inappropriate influence over the financial reporting process (for example because of undue pressure to achieve financial targets)?</p>	<p>The Council outsources its internal audit function to Leicestershire County Council to ensure regular review of it's control environment. The outcomes of audit reports are regularly reported, to Senior management and the Audit and Risk Committee.</p>

# Fraud risk assessment

Question	Management response
7. Are there any areas where there is potential for misreporting?	None that the Council are aware of.
<p>8. How does the Authority communicate and encourage ethical behaviours and business processes of it's staff and contractors?</p> <p>How do you encourage staff to report their concerns about fraud?</p> <p>What concerns are staff expected to report about fraud? Have any significant issues been reported?</p>	<p>The Council uses various options to communicate with employees including;</p> <ul style="list-style-type: none"> <li>• Staff intranet, established internal communication channels</li> <li>• Organisational development team, delivering staff training</li> <li>• Information assurance team to support data policies</li> </ul> <p>The Council encourages staff to report their concerns regarding fraud through the following policies;</p> <ul style="list-style-type: none"> <li>• Anti-fraud, Bribery &amp; Corruption Policy</li> <li>• Whistleblowing Policy</li> </ul>
<p>9. From a fraud and corruption perspective, what are considered to be high-risk posts?</p> <p>How are the risks relating to these posts identified, assessed and managed?</p>	<p>Director of Finance Treasury Manager</p> <p>Risks associated by the above posts are managed through having appropriate controls in place, to reduce the potential for fraud or corruption. LCC undertake ID checks on applicants and also fully participate in the NFI project. This provides further assurance as this allows the payroll file to be cross matched against the directorships of companies with whom the council do business. Work is ongoing to centralise the conflict of interest file and this will be checked against all new procurement exercises.</p>
<p>10. Are you aware of any related party relationships or transactions that could give rise to instances of fraud?</p> <p>How do you mitigate the risks associated with fraud related to related party relationships and transactions?</p>	<p>The Council is unaware of any related party relationships that could give rise to instances of fraud. The Council maintains information on any related parties to ensure any risks can be mitigated and appropriate controls are in place.</p>

## Fraud risk assessment

Question	Management response
<p>11. What arrangements are in place to report fraud issues and risks to the Audit and Risk Committee? How does the Audit and Risk Committee exercise oversight over management's processes for identifying and responding to risks of fraud and breaches of internal control? What has been the outcome of these arrangements so far this year?</p>	<p>Two reports are submitted to the Audit and Risk Committee annually to report on fraud issues with an additional report on the National Fraud Initiative each year. Along with this internal audit also report to committee on outcomes from internal audits.</p>
<p>12. Are you aware of any whistle blowing potential or complaints by potential whistle blowers? If so, what has been your response?</p>	<p>No</p>
<p>13. Have any reports been made under the Bribery Act?</p>	<p>No</p>

# Law and regulations

## Matters in relation to laws and regulations

ISA(UK&I)250 requires us to consider the impact of laws and regulations in an audit of the financial statements.

Management, with the oversight of the Audit and Risk Committee, is responsible for ensuring that the Authority's operations are conducted in accordance with laws and regulations including those that determine amounts in the financial statements.

As auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error, taking into account the appropriate legal and regulatory framework. As part of our risk assessment procedures we are required to make inquiries of management and the Audit and Risk Committee as to whether the entity is in compliance with laws and regulations. Where we become aware of information of non-compliance or suspected non-compliance we need to gain an understanding of the non-compliance and the possible effect on the financial statements.

Risk assessment questions have been set out below together with responses from management.

# Impact of laws and regulations

Question	Management response
<p>1. How does management gain assurance that all relevant laws and regulations have been complied with?</p> <p>What arrangements does the Authority have in place to prevent and detect non-compliance with laws and regulations?</p> <p>Are you aware of any changes to the Authority's regulatory environment that may have a significant impact on the Authority's financial statements?</p>	<p>The Council employs legal professionals to ensure it remains compliant with all relevant laws and regulations.</p> <p>Legal implications are included on all relevant decision-making reports, scrutiny reports and a number of internal briefing reports. On a case-by-case basis lawyers are embedded into the operational decision-making structures within client areas (child protection, adults safeguarding, HR etc)</p> <p>A Quarterly Governance Panel comprising the Chief Operating Officer and the two Statutory Officers has been set up to provide an additional layer of scrutiny to what are regarded as the Council's high-risk activities/schemes.</p>
<p>2. How is the Audit and Risk Committee provided with assurance that all relevant laws and regulations have been complied with?</p>	<p>Legal implications are included on all reports taken to Committee, including to the Audit and Risk Committee.</p>
<p>3. Have there been any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2019 with an on-going impact on the 2019/2020 financial statements?</p>	<p>There have been no known instances of significant non-compliance with law and regulation.</p>
<p>4. Is there any actual or potential litigation or claims that would affect the financial statements?</p>	<p>No</p>
<p>5. What arrangements does the Authority have in place to identify, evaluate and account for litigation or claims?</p>	<p>All legal work is undertaken on a single specialist case management software system. In individual client areas (e.g. debt recovery, care proceedings, employment law etc) regular client liaison meetings occur or data is shared. Elevation mechanisms within Legal Services ensure that high profile cases are referenced with senior management. Our insurance arrangements are closely managed to ensure that insurable claims are efficiently handled. All Judicial Review claims are brought to the attention of the City Barrister.</p>

## Impact of laws and regulations

Question	Management response
6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	No

# Going Concern

## Matters in relation to going concern

ISA(UK&I)570 covers auditor responsibilities in the audit of financial statements relating to management's use of the going concern assumption in the financial statements.

The going concern assumption is a fundamental principle in the preparation of financial statements. Under this assumption entities are viewed as continuing in business for the foreseeable future. Assets and liabilities are recorded on the basis that the entity will be able to realise its assets and discharge its liabilities in the normal course of business.

Going concern considerations have been set out below and management has provided its response.

## Going concern considerations

Question	Management response
<p>1. Has the management team carried out an assessment of the going concern basis for preparing the financial statements for both the Authority? What was the outcome of that assessment?</p>	<p>The Council does not formally complete a report on Going Concern. However the Council completes an Annual Budget report each year that goes to the Overview Select Committee (and other scrutiny committees) for scrutiny and then to Full Council for approval. This includes medium term forecasts and risks to those forecasts, as well as future action required to remain a going concern.</p>
<p>2. Are the financial assumptions in that report (e.g., future levels of income and expenditure) consistent with the Authority's Business Plan and the financial information provided to the Authority throughout the year?</p>	<p>The financial assumptions in the budget report are consistent with the financial information reported throughout the year. Nonetheless, the information also has to respond to changes.</p>
<p>3. Are the implications of statutory or policy changes appropriately reflected in the Business Plan, financial forecasts and report on going concern?</p>	<p>Any changes in statutory or policy changes with a financial impact are reflected and reported in the financial forecasts of the Council.</p>
<p>4. Have there been any significant issues raised with the Audit and Risk Committee during the year which could cast doubts on the assumptions made? (Examples include adverse comments raised by internal and external audit regarding financial performance or significant weaknesses in systems of financial control).</p>	<p>No</p>
<p>5. Does a review of available financial information identify any adverse financial indicators including negative cash flow or poor or deteriorating performance against the better payment practice code? If so, what action is being taken to improve financial performance?</p>	<p>No. Cash balances are buoyant.</p>



## Going concern considerations

Question	Management response
<p>6. Does the Authority have sufficient staff in post, with the appropriate skills and experience, particularly at senior manager level, to ensure the delivery of the Authority's objectives? If not, what action is being taken to obtain those skills?</p>	<p>Yes</p>
<p>7. Does the Authority have procedures in place to assess their ability to continue as a going concern?</p>	<p>The Council annually completes the Budget Setting process, and through this a forecast is done of the financial position. In the report assumptions and areas of risk are highlighted. The financial position is routinely monitored during the year, as is income collection.</p>
<p>8. Is management aware of the existence of events or conditions that may cast doubt on the Authority's ability to continue as a going concern?</p>	<p>Like all authorities, the Council has been severely affected by funding cuts. We have always managed to balance budgets, avoiding crisis cuts, and 20/21 is no exception. The medium term looks difficult, but we have a track record of managing cuts if more are required.</p>
<p>9. Are arrangements in place to report the going concern assessment to the Audit and Risk Committee? How has the Audit and Risk Committee satisfied itself that it is appropriate to adopt the going concern basis in preparing financial statements?</p>	<p>A Going Concern is not formally reported to Committee. But all elected members are on Full Council and vote on the budget report which highlight the Councils financial position.</p>

# Related Parties

## Matters in relation to Related Parties

Local Authorities are required to comply with IAS 24 and disclose transactions with entities/individuals that would be classed as related parties. These may include: entities that directly, or indirectly through one or more intermediaries, control, or are controlled by the Authority (i.e. subsidiaries);

- associates;
- joint ventures;
- an entity that has an interest in the authority that gives it significant influence over the authority;
- key management personnel, and close members of the family of key management personnel; and
- post-employment benefit plans (pension fund) for the benefit of employees of the authority, or of any entity that is a related party of the authority.

A disclosure is required if a transaction (or series of transactions) is material on either side, i.e. if a transaction is immaterial from the Authority perspective but material from a related party viewpoint then the Authority must disclose it.

ISA (UK&I) 550 requires us to review your procedures for identifying related party transactions and obtain an understanding of the controls that you have established to identify such transactions. We will also carry out testing to ensure the related party transaction disclosures you make in the financial statements are complete and accurate.

## Related Parties

Question	Management response
1. What controls does the Authority have in place to identify, account for and disclose related party transactions and relationships ?	Members & Directors are asked to complete an annual declaration. The Council also takes part in the National Fraud Initiative.
2. Who have the Council identified as related parties?	Currently no further related parties have been identified other than these included in the 2018/19 accounts. The full process to review will happen during February and March.

# Accounting estimates

## Matters in relation to Related Accounting estimates

Local Authorities apply appropriate estimates in the preparation of their financial statements. ISA (UK&I) 540 sets out requirements for auditing accounting estimates. The objective is to gain evidence that the accounting estimates are reasonable and the related disclosures are adequate.

Under this standard we have to identify and assess the risks of material misstatement for accounting estimates by understanding how the Authority identifies the transactions, events and conditions that may give rise to the need for an accounting estimate.

Accounting estimates are used when it is not possible to measure precisely a figure in the accounts. We need to be aware of all estimates that the Authority is using as part of its accounts preparation; these are detailed in appendix 1 to this report. The audit procedures we conduct on the accounting estimate will demonstrate that:

- the estimate is reasonable; and
- estimates have been calculated consistently with other accounting estimates within the financial statements.

We would ask the Audit and Risk Committee to satisfy itself that the arrangements for accounting estimates are adequate.

# Accounting Estimates

Question	Management response
1. Are management aware of transactions, events, conditions (or changes in these) that may give rise to recognition or disclosure of significant accounting estimates that require significant judgement (other than those in Appendix A)?	No
2. Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?	Yes
3. How is the Audit and Risk Committee provided with assurance that the arrangements for accounting estimates are adequate ?	The material estimates are reported in the Statement of Accounts. Further to this briefing & training sessions are completed with the Audit and Risk Committee to ensure they understand the arrangements used for completion including estimates. The Committee is encouraged to ask questions to gain assurance that officers are able to provide robust answers.

## Appendix A Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Property plant & equipment Valuations	<p>Non-dwelling property valuations are planned at the beginning of each financial year by Estates &amp; Building Services. The Valuer is asked to provide estimated property values as at the end of the financial year using forecast valuation indices. Programme of planned valuations maintained by Estates &amp; Building Services to ensure that all land and buildings are regularly revalued. Forward indices published by the Building Cost Information Service are used to forecast property values at the Balance Sheet date.</p>	<p>The Valuer reviews valuations at the Balance Sheet date to ascertain appropriateness of estimated valuations and therefore any material under- or overstatement.</p>	<p>RICS valuers are appointed to undertake the annual valuations</p>	<p>Actual indices will not vary greatly from forecast indices.</p>	<p>No</p>



## Appendix A

### Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Estimated remaining useful lives of PPE	Assets are depreciated over their useful lives, with remaining useful life being updated as and when assets are revalued.	Any changes in useful life's are reviewed by Finance to ensure any material movements are understood.	RICS valuers are appointed to undertake the annual valuations and update their useful life.	It is assumed that the remaining useful life of assets reflect the level of repairs and maintenance that will be made. All depreciable assets are depreciated assuming no residual value.	No
Bad Debt Provision	A bad debt provision is calculated based on the age & total of outstanding debt at the balance sheet date. Standard percentages and knowledge of individual circumstances are used.	Reviewed to ensure significant movements are understood and are prudent.	No	No policy or legal change affects the collection of this debt.	No



## Appendix A Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Insurance claims	This is estimated based on the claims received and which are expected to be settled.	The Insurance, claims database is used, providing the estimate. Actuaries have been used during 2019 to review the reasonableness of the estimates.	Insurance Company & Actuaries	The status of the Claim has been maintained.	No
Business rates	Business Rates appeals- Judgement is applied based on data from the Valuation Office Agency regarding outstanding appeals and the likelihood of success. The amount of the reduction and the backdating of the appeal have been based upon averages of historic settled appeals data and any other known information.	Different averages are calculated for the different types of appeals and property types.	Revenues Manager	The calculation is based on a range of sources including professional advice. If the volume and outcome of appeals differs significantly from the assumptions then this will impact on the level of provision	No





## Appendix A

### Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Liabilities under PFI Schemes	<p>Total payments due under existing PFI schemes are split between payments for services, reimbursement of capital expenditure, interest and lifecycle costs. The split being derived from detailed cash flow models provided at the commencement of each scheme. PFI liabilities are reduced by payments made during the year.</p> <p>Financial model detailing cash flows of schemes provided by KPMG.</p>	Changes to outstanding liabilities are measured against the financial model and split between current and non-current accordingly.	No	<p>It is assumed that the PFI schemes will progress as planned with specifications remaining unchanged.</p> <p>PFI unitary payments are being made as per the financial model.</p>	No



## Appendix A Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Pension Fund (LGPS) Actuarial gains/losses	Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets.	Checks to the reasonableness of assumptions in the actuaries report are made	Yes (actuary for LGPS administered by Leicestershire County Council)	The effects of the net pension liability of changes in individual assumptions can change the liability significantly. Eg an 0.5% decrease in the Real Discount rate would mean a 10% increase to the employers liability	No.





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