

Informing the audit risk assessment Telford & Wrekin Council 2018/19



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Purpose

The purpose of this report is to contribute towards the effective two-way communication between auditors and the Council's Audit 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 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 Committee. ISA(UK&I) emphasise the importance of two-way communication between the auditor and the Audit Committee and also specify matters that should be communicated.

This two-way communication assists both the auditor and the Audit 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 Committee and supports the Audit 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 Committee's oversight of the following areas:

- fraud
- laws and regulations
- going concern
- related parties
- accounting estimates.

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

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 Committee and management. Management, with the oversight of the Audit 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 Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

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

Fraud risk assessment

Question

Has the Council assessed the risk of material misstatement in the financial statements due to fraud? What are the results of this process?

Management response

The risk of material misstatement in the financial statements due to fraud is low because:

- Arrangements are in place to prevent and detect fraud which includes the work undertaken by Internal Audit, The Investigation Team, Council Tax and Benefits Teams.
 - The Internal Audit plan covers the key systems which feed into the Statement of Accounts and audits are undertaken on a risk-based approach.
 - The Managing Director, Directors, Assistant Directors and Service Delivery Managers complete and sign assurance statements on an annual basis confirming that the governance framework has been operating within their areas of responsibility.
 - There is an Anti-Fraud and Corruption Policy in place which is monitored and reviewed. Periodic reports are provided to Senior Management Team and cascaded to teams.
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Fraud risk assessment (continued)

Question

How are the Audit Committee satisfied that the overall control environment is robust.

In particular what processes does the Council have in place to identify and respond to risks of fraud in the organisation?

Management response

Assurance is provided to the Audit Committee through:

- Quarterly internal audit reports are presented to the Committee providing an update on the work of internal audit with particular focus on Amber and Red reports.
- Directors/Assistant Directors/Service Delivery Managers attend, on request, to provide additional information where requested.
- External Audit provide an Annual Audit Letter to the Committee highlighting any areas of concern and recommendations following the annual audit of accounts.
- An Anti-Fraud Report is presented at the end of each financial year.
- The Strategic Risk Register is presented to Audit Committee.
- Finance & Legal comments in all reports; business case approval for major investments .

Processes in place to identify and respond to fraud:

- Internal Audit work plan.
- Internal Audit along with the Investigations Team undertake proactive fraud work based on a fraud risk register.
- Fraud and corruption activities are undertaken by Trading Standards.
- Anti-Fraud & Corruption Policy.
- Whistleblowing and fraud reporting procedures are in place which allow staff and members of the public to report concerns relating to fraud and error to the Investigation Team via a variety channels.

Fraud risk assessment (continued)

Question

Management response

Have any specific fraud risks, or areas with a high risk of fraud, been identified and what has been done to mitigate these risks?

Council Tax Support, Single Person Discount and Council Tax liability are areas where fraud is common. The Investigation Team undertake considerable work in this area. There are strong reporting channels where staff and members of the public report their concerns. The Revenues Service undertake an annual Single Person Discount review exercise by using credit data obtained from a third party, and they also take part in the National Fraud Initiative's single person discount review.

Direct Payment and Social Care is a growing area of fraud. Significant work has been undertaken by the Investigation Team to increase awareness of fraud in this area and encourage staff to report their concerns.

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)?

Management is not aware of any areas where there is potential for override of control or inappropriate influence over the financial reporting process.

Reconciliations are undertaken regularly and there is appropriate separation of duties in place with review/challenge by Senior Finance Officers.

How does the Audit Committee exercise oversight over management's processes for identifying and responding to risks of fraud and breaches of internal control?

The Audit Committee's terms of reference include a number of measures concerning internal control and fraud matters. In the main these include:

- Receiving regular updates on the work of internal audit which would include fraud risks
- Receiving an annual report on anti-fraud and corruption
- Approving the Councils Anti-Fraud & Corruption Policy and the Whistleblowing Policy

What arrangements are in place to report fraud issues and risks to the Audit Committee?

Fraud risk assessment (continued)

Question

Management response

How does the Council communicate and encourage ethical behaviour of its staff and contractors?

Training – Fraud module included for all new starters.
Core behaviours for all employees.
Induction of new employees.
Whistleblowing Policy.
Publicity on fraud matters that have been taken to court.
Anti-Fraud & Corruption Policy.

How do you encourage staff to report their concerns about fraud? Have any significant issues been reported?

The Whistleblowing Policy encourages staff to report any concerns regarding fraud and irregularity through a variety of channels.
The Council's Core behaviours encourage staff to report any fraudulent/otherwise unacceptable behaviour.
The authority receives a constant flow of allegations, most notably relating to Revenues related fraud by the general public. Referrals have also been received relating to Adult Social Care and a number of internal matters.

Are you aware of any related party relationships or transactions that could give rise to risks of fraud?

We are not aware of any party relationships or transactions that could give rise to fraud.
Related party transactions have to be disclosed by elected Members and senior officers.
All members and officers have to disclose relevant interests in the register of interests.

Fraud risk assessment (continued)

Question

Are you aware of any instances of actual, suspected, or alleged fraud either within the Council as a whole or within specific departments since 1 April 2018?

Are you aware of any whistleblower reports or reports under the Bribery Act since 1 April 2018?

If so how does the Audit Committee respond to these?

Management response

In terms of internal fraud against the council, one matter has been under investigation and has been passed over to the Police since April 2018.

External to the Council, there have been a number of allegations received regarding fraud by members of the public. These are largely related to Revenues matters. These matters are investigated by the Investigation Team.

No specific whistle blower reports or Bribery Act referrals have been made since April 2018.

Laws 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 Committee, is responsible for ensuring that the Council'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 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 noncompliance 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

What arrangements does the Council have in place to prevent and detect non-compliance with laws and regulations?

How does management gain assurance that all relevant laws and regulations have been complied with?

The Council has a robust Governance Framework in place.

The Council has a Monitoring Officer and Section 151 Officer who provide assurance both supported by adequately staffed and trained teams of professional officers.

Council/Cabinet reports include a Legal Comment which is completed and signed off by a senior officer in Legal Services.

Internal Audit Work.

How is the Audit Committee provided with assurance that all relevant laws and regulations have been complied with?

As above. The Monitoring Officer ensures lawfulness and fairness of decision making. The Monitoring Officer will report to Full Council if he considers that any proposal, decision or omission would give rise to unlawfulness. Other Statutory Officers of the authority also provide assurance in relation to their specific function.

Have there been any instances of non-compliance or suspected non-compliance with law and regulations since 1 April 2018, or earlier with an on-going impact on the 2018/19 financial statements?

No – the position will be reviewed again at the 31 March each year as part of the annual accounts process.

What arrangements does the Council have in place to identify, evaluate and account for litigation or claims?

Legal and Insurance work together to identify and evaluate any potential litigation or claims against the Council.

Potential liabilities are included in the Statement of Accounts.

Is there any actual or potential litigation or claims that would affect the financial statements?

There is one case where a claim has been made for £1m, the Council has made an offer of £20,000. This case is ongoing.

Have there been any reports from other regulatory bodies, such as HM Revenues and Customs which indicate noncompliance?

None

Impact of laws and regulations (continued)

Question

What arrangements does the Council have in place to prevent and detect non-compliance with laws and regulations?

How does management gain assurance that all relevant laws and regulations have been complied with?

Management response

The Council has a robust Governance Framework in place:

- The Council has a Monitoring Officer and Section 151 Officer who provide assurance both supported by adequately staffed and trained teams of professional officers.
- Council/Cabinet reports include a Legal Comment which is completed and signed off by a senior officer in Legal Services.
- Internal Audit Work.

Going concern

Matters in relation to laws and regulations

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.

Going concern is a fundamental principle in the preparation of financial statements. Under the going concern assumption, a council is viewed as continuing in operation for the foreseeable future with no necessity of liquidation or ceasing trading. Accordingly, the Council's assets and liabilities are recorded on the basis that assets will be realised and liabilities discharged in the normal course of business. A key consideration of going concern is that the Council has the cash resources and reserves to meet its obligations as they fall due in the foreseeable future.

We have discussed the going concern assumption with key Council officers and reviewed the Council's financial and operating performance. Below are key questions on the going concern assumption which we would like the Audit Committee to consider.

Going concern considerations

Question

Does the Council have procedures in place to assess the Council's ability to continue as a going concern?

Management response

There is a robust Service & Financial Planning process and Strategy in place.

Regular financial monitoring takes place with regular updates being presented to Senior Management Team and Cabinet; cost improvement plans are in place for areas of significant pressure.

Overall spend is within budget and the Council has a long track record of strong financial management being under budget for the past 11 years and will have delivered ongoing savings totalling £117m by the end of 2018/19 in accordance with the budgets approved for each year.

Is management aware of the existence of other events or conditions that may cast doubt on the Council's ability to continue as a going concern?

None known

Are arrangements in place to report the going concern assessment to the Audit Committee?

Yes - through the Statement of Accounts

How has the Audit Committee satisfied itself that it is appropriate to adopt the going concern basis in preparing the financial statements?

The Audit Committee receives both the draft and final Statement of Accounts and has opportunity to raise queries. Prior to approval of the final SOA officers provide an overview/training session highlighting key matters in the accounts and again providing opportunity for queries.

Members have access to all Council reports, including the budget and regular financial management reports which provide assurance on the current and projected financial position of the authority. The Council has a long track record of sound financial management having slightly underspent its budget for more than 10 consecutive years despite having to deliver £117m of ongoing budget savings.

Are the financial assumptions in that report (e.g., future levels of income and expenditure) consistent with the Council's Business Plan and the financial information provided to the Council throughout the year?

Yes – financial assumptions in the Statement of Accounts, revenue budget, capital programme, treasury management strategy and Council plan are all consistent.

Going concern considerations (continued)

Question	Management response
Are the implications of statutory or policy changes appropriately reflected in the Business Plan, financial forecasts and report on going concern?	Yes
Have there been any significant issues raised with the Audit 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).	No
Does a review of available financial information identify any adverse financial indicators including negative cash flow? If so, what action is being taken to improve financial performance?	No

Going concern considerations (continued)

Question

Does the Council have sufficient staff in post, with the appropriate skills and experience, particularly at senior manager level, to ensure the delivery of the Council's objectives?

If not, what action is being taken to obtain those skills?

Management response

Yes although given staffing reductions to meet savings targets, there are some single points of failure which are addressed through workforce planning processes as far as possible.

The recruitment process, including job descriptions and person specifications are designed to ensure the appropriate skills and experience are sought.

Restructuring/service transformation have a focus on ensuring skills and experience to deliver services are in place.

The Council is active in terms of workforce planning, which aligns with service planning and delivery of service objectives.

There is a comprehensive corporate learning programme in place for managers and other employees as well as specific training relevant to specific roles.

There is a strong focus on organisational development, including a Leadership programme.

The Council will engage external professionals where specific skills are required that are not available in-house, or agency workers will be engaged when necessary to fill essential roles on a short-term basis. A Use of Consultants Business Case has to be approved to ensure appropriate governance in place.

Related parties

Matters in relation to Related Parties

Local Authorities are required to comply with International Accounting Standard 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 Council (i.e. subsidiaries);
- associates and/or joint ventures;
- an entity that has an interest in the Council that gives it significant influence over the Council;
- 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 Council, or of any entity that is a related party of the Council.

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 Council's perspective but material from a related party viewpoint then the Council 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 party considerations have been set out below and management has provided its response.

Related parties considerations

Question

What controls does the Council have in place to identify, account for, and disclose related party transactions and relationships?

Management response

Register of Interests for Members and Officers.

Completion of annual declaration by Senior Officers and Members as part of Statement of Accounts process.

Governance Statement.

Who have the Council identified as related parties?

See the Statement of Accounts.

Accounting estimates

Matters in relation to Accounting Estimates

Local Authorities need to apply appropriate estimates in the preparation of their financial statements. ISA (UK&I) 540 sets out requirements for auditing accounting estimates. This 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 Council identified the transactions, events and conditions that may give rise to the need to 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 Council are using as part of their 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.

Accounting estimates considerations

Question	Management response
Are the management aware of transactions, events and conditions (or changes in these) that may give rise to recognition or disclosure of significant accounting estimates that require significant judgment?	No
Are the management arrangements for the accounting estimates, as detailed in Appendix 1 reasonable?	Yes – see Appendix 1 below.
How is the Audit Committee provided with assurance that the arrangements for accounting estimates are adequate?	The accounting policies and notes included in the Statement of Accounts provide information. External Audit provide assurance.

Appendix 1 - 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>Full valuation involving an inspection is carried out every 5 years on a rolling programme for operational properties. An impairment and valuation review is carried out as a desk value for properties not valued in year.</p> <p>Investment properties are valued annually.</p> <p>Valuations of vehicles, plant, furniture and equipment are based on current prices where there is an active second-hand market or latest list price adjusted for asset condition.</p> <p>Historical cost is used for infrastructure assets and community assets.</p>	Internal Valuer used	Use Estates & Investments Service (RICS Registered Valuers) for the property element of PPE valuations.	Valuations are based on recommendations by CIPFA and made in line with RICS guidance. Assumptions are set out in the valuer's report including comments on market uncertainty and alternative valuation methods that may return a different result.	No

Appendix 1 - 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.	<p>The following useful lives have been used in the calculation of depreciation:</p> <ul style="list-style-type: none"> • Other Land and Buildings – 5 to 60 years • Vehicles, Plant, Furniture & Equipment – 3 to 25 years • Infrastructure – 25 to 40 years 	<p>Specific asset lives applied to buildings. Consistent asset lives applied to each asset category.</p>	<p>Use Estates & Investment Service (RICS Reistered valuer) for buildings valuations. Other assets considered by Estates & Investment Service Delivery Manager and Group Accountant Corporate and Health & Well-Being Finance</p>	<p>The length of the life is determined at the point of acquisition or revaluation. Major components are depreciated separately when they meet the componentisation policy.</p>	No
Depreciation & Amortisation	<p>Depreciation is provided for all fixed assets with a finite useful life on a straight-line basis.</p>	<p>Consistent application of depreciation method across all assets.</p>	No	<p>The asset is not depreciated until it is available for use and each significant part of PPE is depreciated separately. Asset lives are determined at acquisition/revaluation. Depreciation is calculated on a straight line basis. The asset lives are recorded in the asset register.</p>	No

Appendix 1 - 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?
Impairments	<p>Assets are assessed at the year-end for any indication that an asset may be impaired. An impairment and valuation review is carried out as a desk exercise for properties not valued in the year. Where indications exist and any possible differences are estimated to be material, the recoverable amount of the asset is estimated and, where this is less than the carrying amount of the asset, an impairment loss is recognised for the shortfall.</p> <p>Assets are assessed at each year-end as to whether there is any indication that an asset may be impaired.</p> <p>This assessment is made by the internal valuer for land and buildings and by Property Services Manager and capital accountant (and other relevant officers for the asset type) for other assets.</p>	Impairment reviews at year end Internal Valuer used	Use Property Services (RICS Registered valuer) for buildings valuations.	Valuations are made in-line with RICS guidance.	No

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?
Overhead allocation.	Central support costs are apportioned to services based on an agreed criteria as detailed in the CEC Allocation spreadsheet.	All support service costs centres are allocated according to the agreed CEC Allocation spreadsheet.	No	Apportionment bases are reviewed annually.	No
Measurement of Financial Instruments	The Council values financial instruments at amortised cost. (The fair value of financial instruments are disclosed in the notes to the accounts).	Take advice from finance professionals .	External Treasury advisors & PWLB	Take advice from finance professionals and external Treasury advisors.	No

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?
Provisions for liabilities.	Provisions are made where an event has taken place that gives the Council a legal or constructive obligation that probably requires settlement by a transfer of economic benefits, but where the timing of the transfer is uncertain. Provisions are charged as an expense to the appropriate service line in the CI&ES in the year that the Council becomes aware of the obligation, and are measured at the best estimate at the balance sheet date of the expenditure required to settle the obligation, taking into account relevant risks and uncertainties.	Charged in the year the Council becomes aware of the obligation.	No	Estimated settlements are reviewed at the end of each financial year. Where it becomes less than probable that a transfer of economic benefits will now be required (or a lower settlement than anticipated is made), the provision is reversed and credited back to the relevant service. Where some or all of the payment required to settle a provision is expected to be recovered from another party (e.g. from an insurance claim), this is only recognised as income for the relevant service if it is virtually certain that reimbursement will be received by the Council.	No

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?
Bad Debt Provision.	A provision is estimated using a proportion basis of an aged debt listing.	Revenues provide the aged debt listing and Finance calculate the provision.	No	Consistent proportion used across aged debt as per the Code.	No
Accruals	Finance team collate accruals of expenditure and income. Activity is accounted for in the financial year that it takes place, not when money is paid or received.	Review financial systems and question service managers to identify where goods have been received but not paid for.	No	Accruals for income and expenditure often based on known values. Where accruals are estimated the latest available information is used.	No

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 liability	The Council is an admitted body to the Shropshire County Local Government Pension Scheme. The administering authority (Shropshire Council) engage the Actuary who provides the estimate of the pension liability.	Payroll data is provided to the Actuary. Management reconcile this estimate of contributions to the actuals paid out in the year.	Consulting actuary	As disclosed in the actuary's report. Complex judgements including the discount rate used, rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets.	No
Non adjusting events – events after the Balance Sheet date	Section 151 Officer makes the assessment. If the event is indicative of conditions that arose after the balance sheet date this is an un-adjusting event. A note to the accounts is included, identifying the nature of the event and where possible estimates of the financial effect.	The Section 151 Officer is notified by relevant managers.	This would be considered on individual circumstances.	This would be considered on individual circumstance.	No

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?
PFI Finance Lease Liability	The operator's financial model is used as the basis for calculating the liability.	The operator's financial model is used as the basis for calculating entries and this is reviewed by Finance on an annual basis.	No	The construction elements of the annual unitary charge is accounted for as a finance lease. Minimum lease payments are made under these leases and assets recognised under these leases are accounted for using the policies applied generally to such assets, subject to depreciation being charged over the lease term if this is shorter than the asset's estimated useful life.	No

