



Informing the audit risk assessment for Exeter City Council 2020/21

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Table of Contents

Section	Page
Purpose	4
General Enquiries of Management	6
Fraud	9
Fraud Risk Assessment	10
Laws and Regulations	15
Impact of Laws and Regulations	16
Related Parties	18
Accounting Estimates	20
Accounting Estimates - General Enquiries of Management	21
Appendix A – Accounting Estimates	24

Purpose

The purpose of this report is to contribute towards the effective two-way communication between Exeter City Council's external auditors and Exeter City 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), (ISA(UK)) auditors have specific responsibilities to communicate with the Audit Committee. ISA(UK) 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 Council's oversight of the following areas:

- General Enquiries of Management
- Fraud,
- Laws and Regulations,
- 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 Exeter City Council's management. The Audit 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 2020/21?	Covid-19 In-sourcing of leisure services
2. Have you considered the appropriateness of the accounting policies adopted by Exeter City Council? Have there been any events or transactions that may cause you to change or adopt new accounting policies?	Yes accounting policies reviewed and remain appropriate for 2020/21
3. Is there any use of financial instruments, including derivatives?	CCLA Property Fund and money market funds. Classified as FVTPL, but statutory reversal in place until 31 March 2023 for unrealised fair value movements
4. Are you aware of any significant transaction outside the normal course of business?	Various Covid-19 funding and grant schemes, both receivable by the Council and distributed to support businesses and those suffering financial hardship. Details have been provided to Grant Thornton in advance of closing the accounts in order to seek agreement on the appropriate accounting treatment. Judgements have been made in respect of whether the Council is acting as a principal or agent.

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?	No
6. Are you aware of any guarantee contracts?	A guarantee to the University of Exeter remains in place for a lease granted to Exeter Science Park Ltd
7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements?	No
8. Other than in house solicitors, can you provide details of those solicitors utilised by Exeter City Council during the year. Please indicate where they are working on open litigation or contingencies from prior years?	<p>Ashfords LLP: Construction dispute with Allies and Morrisons Architects in relation to the Royal Albert Memorial Museum (Litigation) (2020) (Concluded)</p> <p>Ashfords LLP: Construction dispute with Enelco Limited (aka Exeter Building Company) – Adjudication process (Litigation) (2020) (concluded)</p> <p>Ashfords LLP: Thornpark Rise/Bovemoors defects (Instructed by Exeter City Living Ltd, ECC's wholly owned limited company) (Ongoing)</p> <p>Trowers and Hamlins LLP: Repairs and Maintenance Procurement (2020) (Concluded)</p> <p>Anthony Collins Solicitors LLP: Advice on the provision of leisure services (2021) (Concluded)</p> <p>Davitt Jones Bould Ltd: Sale of Clifton Hill to Exeter City Living Ltd (ECC's wholly owned company) (2021) (Ongoing)</p> <p>Freeths LLP: City Point - Landowner's promotion agreement and subsequent property transactions (ongoing)</p>

General Enquiries of Management

Question	Management response
9. Have any of Exeter 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?	<p>Various consultants employed in respect of the capital projects, as the Council appoint multi-disciplined teams for QS, design, project management for certain schemes.</p> <p>Barnett Waddingham provide actuarial reports for Devon LGPS</p> <p>The Council subscribes to the Icharod (local government technical accounting service) for bulletins on emerging accounting issues</p> <p>VAT advice is provided by PSTax</p>

Fraud

Issue

Matters in relation to fraud

ISA (UK) 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 Exeter City Council'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 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 Exeter City Council's management.

Fraud risk assessment

Question	Management response
<p>1. Have Exeter City Council 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 do the Council's risk management processes link to financial reporting?</p>	<p>Yes</p> <p>A fraud risk assessment process has been undertaken and is recorded in a fraud risk table (copy attached)</p> <p>Any financial risks arising from the Council's risk management processes are taken into consideration as part of preparing the Council's medium term financial plan and help inform decisions on minimum General Fund and HRA working balances as a contingency. Under Section 25 of the Local Government Act 2003 the Section 151 officer has a duty to report on the robustness of estimates and adequacy of reserves, appropriate for the risks to which it is exposed.</p>
<p>2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?</p>	<p>High risk before mitigating actions are: Main Accounting, Income Management, Procurement, Creditors, Insurance, Private Sector Waste Services, Taxi Licensing, Social Housing, Right to Buy, NDR, Payments and Collection, Council Tax, Housing Benefits, Contract Management, Grants (incl. DFG, Covid Business) and ICT. The only area remaining high risk after mitigating controls being in place is ICT due to external high risks and constantly changing and emerging risks. (Please see fraud risk table for more details).</p>

Fraud risk assessment

Question	Management response
<p>3. Are you aware of any instances of actual, suspected or alleged fraud, errors or other irregularities either within Exeter City Council as a whole or within specific departments since 1 April 2020?</p> <p>As a management team, how do you communicate risk issues (including fraud) to those charged with governance?</p>	<p>No</p> <p>Reported in quarterly Internal Audit reports to Audit & Governance Committee</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 Exeter City Council where fraud is more likely to occur?</p>	<p>Housing Benefits, Right to Buy sales, Grants are identified as the highest risk areas</p> <p>This is reflected in the Audit plan and fraud risk table.</p> <p>Please see fraud risk table.</p>
<p>5. What processes do Exeter City Council have in place to identify and respond to risks of fraud?</p>	<p>Internal Audit regularly review and update fraud risk assessment, Counter Fraud Strategy regularly reviewed and updated, anonymous whistleblowing via website, self- assessment against Fighting Fraud Locally, DWP shared information, IIA information, NFI data matching.</p>

Fraud risk assessment

Question	Management response
<p>6. How do you assess the overall control environment for Exeter City Council, including:</p> <ul style="list-style-type: none"> the existence of internal controls, including segregation of duties; and the process for reviewing the effectiveness the system of internal control? <p>If internal controls are not in place or not effective 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>Internal Audit review the internal control processes and provide assurance to Management. The risk based audit plan determines the areas covered each year.</p> <p>Management have agreed remedial action for all high and medium risk issues identified within Internal Audit reports during the year.</p> <p>Counter fraud and whistleblowing e-learning, articles in staff newsletters, participation in the NFI, online reporting facilities for members of the public to raise concerns.</p> <p>Not that we are aware of</p>
<p>7. Are there any areas where there is potential for misreporting?</p>	<p>The Council is embarking on a number of Commercial activities, whilst we are not aware of any specific issues in this area, there is more scope for misreporting in this area.</p>

Fraud risk assessment

Question	Management response
<p>8. How do Exeter City Council 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?</p> <p>Have any significant issues been reported?</p>	<p>Codes of Conduct in place, counter Fraud/Whistleblowing training is undertaken as part of induction e-learning, articles in staff newsletter</p> <p>Raising awareness via staff newsletters. Internet information. Whistleblowing policy.</p> <p>Staff are encouraged to report any concerns they may have and all will be appropriately investigated</p> <p>No</p>
<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>S151, Accountants, Contract Managers, Procurement</p> <p>Their service areas are considered higher risk when establishing the internal audit plan</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>No</p> <p>Partnership Protocol in place, Conditions in Partnership/contract agreement, Pre-procurement vetting process (including bribery risks) in place, data matching and NFI,</p>

Fraud risk assessment

Question	Management response
<p>11. What arrangements are in place to report fraud issues and risks to the Audit Committee? How does the Audit 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>Internal Audit provide a quarterly progress report to the A&G Committee. Any concerns would be raised here. In addition fraud statistics are included in the Annual Internal Audit report.</p> <p>Quarterly Internal Audit progress report, reviews the work and findings of Internal Audit. Counter Fraud and Whistleblowing Policies regularly reviewed, updated and approved by A & G Committee</p> <p>No issues arising.</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) 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 Exeter City 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 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 Exeter City Council have in place to prevent and detect non-compliance with laws and regulations? Are you aware of any changes to the Council's regulatory environment that may have a significant impact on the Council's financial statements?</p>	<p>The Council's Monitoring Officer provides advice on all laws and regulations. The team provides professional support to services to assist with compliance. No system of assurance can provide 100% assurance.</p>
<p>2. How is the Audit Committee provided with assurance that all relevant laws and regulations have been complied with?</p>	<p>Any significant new laws and regulations are highlighted to Council along with the implications. Audit & Governance receive reports on new laws and consultations on Governance related issues.</p>
<p>3. Have there been any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2020 with an on-going impact on the 2020/21 financial statements?</p>	<p>The Monitoring Officer is not aware of any instances of non-compliance or suspected non-compliance with laws and regulations since 1 April 2020</p>
<p>4. Is there any actual or potential litigation or claims that would affect the financial statements?</p>	<p>Covid related delay notices have been received in respect of the bus and coach station, St Sidwell's Point and St Loyes, however whether there is an obligation that could lead to a transfer of economic benefits and therefore a sufficiently reliable estimate of the amount of the obligation cannot be made. The outcomes of a HSE prosecution also resulted in a financial penalty of £19,470, which has been paid in 2020/21.</p>

Impact of laws and regulations

Question	Management response
5. What arrangements does Exeter City Council have in place to identify, evaluate and account for litigation or claims?	The Monitoring Officer and section 151 Officer are both part of SMB and work closely together. Insurance is managed within Finance and regularly reports new claims.
6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	No

Related Parties

Matters in relation to Related Parties

Exeter City Council are required to 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 Exeter City Council;
- associates;
- joint ventures;
- an entity that has an interest in the authority 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) 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
<p>1. Have there been any changes in the related parties including those disclosed in Exeter City Council's 2019/20 financial statements? If so please summarise:</p> <ul style="list-style-type: none"> • the nature of the relationship between these related parties and Exeter City Council • whether Exeter City Council has entered into or plans to enter into any transactions with these related parties • the type and purpose of these transactions 	<p>The group boundary has been reviewed and there have been no changes in related parties</p>
<p>2. What controls does Exeter City Council have in place to identify, account for and disclose related party transactions and relationships?</p>	<p>Regular review of group boundary and assessment of relationships with the Council. Member Services also manage declaration of interests, so that Members/Officers omitted from participating in Council discussions/decisions where appropriate</p>
<p>3. What controls are in place to authorise and approve significant transactions and arrangements with related parties?</p>	<p>As above. Authorisation limits are in place and the Constitution sets out how decisions are made and procedures to be followed, including delegations to officers and deputies and financial regulations.</p>
<p>4. What controls are in place to authorise and approve significant transactions outside of the normal course of business?</p>	<p>As above.</p>

Accounting estimates

Matters in relation to Related Accounting estimates

ISA (UK) 540 (Revised December 2018) requires auditors to understand and assess an entity's internal controls over accounting estimates, including:

- The nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates;
- How management identifies the need for and applies specialised skills or knowledge related to accounting estimates;
- How the entity's risk management process identifies and addresses risks relating to accounting estimates;
- The entity's information system as it relates to accounting estimates;
- The entity's control activities in relation to accounting estimates; and
- How management reviews the outcomes of previous accounting estimates.

As part of this process auditors also need to obtain an understanding of the role of those charged with governance, which is particularly important where the estimates have high estimation uncertainty, or require significant judgement.

Specifically do Audit Committee members:

- Understand the characteristics of the methods and models used to make the accounting estimates and the risks related to them;
- Oversee management's process for making accounting estimates, including the use of models, and the monitoring activities undertaken by management; and
- Evaluate how management made the accounting estimates?

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

Accounting Estimates - General Enquiries of Management

Question	Management response
1. What are the classes of transactions, events and conditions, that are significant to the financial statements that give rise to the need for, or changes in, accounting estimate and related disclosures?	Critical judgements are disclosed in Note 3 to the accounts. Classes of transactions that are significant include; pension liability, valuation of PPE and business rates
2. How does the Authority's risk management process identify and addresses risks relating to accounting estimates?	We seek professional advice in respect of the accounting estimates
3. How do management identify the methods, assumptions or source data, and the need for changes in them, in relation to key accounting estimates?	We seek professional advice in respect of the key accounting estimates and assess the impact of emerging accounting standards as adopted by the Code
4. How do management review the outcomes of previous accounting estimates?	We seek professional advice in respect of whether previous assumptions and estimates need to be updated
5. Were any changes made to the estimation processes in 2020/21 and, if so, what was the reason for these?	No changes except a further report requested from Barnett Waddingham in relation to settlement and curtailment events, following amendments to the IAS 19 standard.

Accounting Estimates - General Enquiries of Management

Question	Management response
<p>6. How do management identify the need for and apply specialised skills or knowledge related to accounting estimates?</p>	<p>Accounting estimates that require specialist advice or knowledge are determined following a review of in-house expertise and capacity and are procured externally, where deemed necessary.</p>
<p>7. How does the Authority determine what control activities are needed for significant accounting estimates, including the controls at any service providers or management experts?</p>	<p>The instruction of Barnett Waddingham is co-ordinated on behalf of Devon authorities by Devon County Council, as the administering authority to the Devon County Council Pension Fund.</p>
<p>8. How do management monitor the operation of control activities related to accounting estimates, including the key controls at any service providers or management experts?</p>	<p>Specialist advice is provided by suitably qualified professionals</p>
<p>9. What is the nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates, including:</p> <ul style="list-style-type: none"> - Management's process for making significant accounting estimates - The methods and models used - The resultant accounting estimates included in the financial statements. 	<p>Accounting estimates are reported to Audit and Governance Committee as part of approving the annual Statement of Accounts</p>

Accounting Estimates - General Enquiries of Management

Question	Management response
10. 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)?	Critical judgements are disclosed in Note 3 to the accounts
11. Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?	No changes to accounting estimates, as set out in Appendix A
12. How is the Audit Committee provided with assurance that the arrangements for accounting estimates are adequate ?	Accounting estimates are reported to Audit and Governance Committee as part of approving the annual Statement of Accounts

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 and Equipment valuations	Fair value for land/buildings defined as 'existing use' by the Council, where there is no market based evidence of fair value because the specialist nature of the asset, depreciated replacement cost is used	Full valuations are performed on a rolling basis to cover 20% of assets per annum, but with the top 4 highest value assets re-valued every year. Assets not included in the full valuation are assessed at the reporting date in order to ensure that carrying amounts are not materially different to current values	In-house RICS valuers	Degree of uncertainty inherent with any revaluation. We employ professional valuers and rely on expert opinion	No
Depreciation	Straight line depreciation, except reducing balance method for vehicles	Significant components in relation to the total cost of an asset are depreciated separately and asset lives and residual values are also assessed and adjusted if appropriate	In-house RICS valuers	Depreciation reflects the consumption of assets and assumptions are made in respect of the level of repairs and maintenance in relation to individual assets. In-house valuers benefit from records of property condition, planned maintenance and capital enhancements.	No
Impairments	Impairment reviews are	Form integral part of the	In-house RICS	In line with RICS guidance	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?
Accruals	Accruals are made in line with the Council's accruals accounting policy	Regular budget monitoring, engagement with budget holders, increasing the use of purchase ordering and reviewing the invoice register all support the identification of accruals	Qualified accountants and budget holders	Accruals are made when a reliable estimate can be made.	No
Provisions	Provisions are measured at best estimate (including risks and uncertainties) of the expenditure required to settle the present obligation	Provisions are identified through regular budget monitoring and engagement with budget holders, which flags potential issues to management	VOA data in respect of NDR appeals	Each provision is assessed on an individual basis to ensure it meets criteria of a provision per IAS 37. The degree of uncertainty is assessed when determining whether a provision is the correct treatment for an item.	No



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