

Informing the audit risk assessment for Cheshire East Council

Year ended 31 March 2018

Jon Roberts

Partner

T +44 (0)121 232 5410

E jon.roberts@uk.gt.com

Scarlett Mayer

Audit Manager

T +44 (0) 121 232 5440

E: Scarlett.E.Mayer@uk.gt.com

Lisa Morrey

Audit In-Charge

T: +44 (0)121 232 5302

E Lisa.Morrey@uk.gt.com

Hamze Samatar

Audit In-Charge

+44 (0)121 232 5147

E hamze.mha.samatar@uk.gt.com



Contents

<u>Section</u>	<u>Page</u>
Purpose	3
Fraud	4
Fraud Risk Assessment	5
Laws and Regulations	16
Impact of Laws and Regulations	17
Going Concern	20
Going Concern Considerations	21
Accounting Estimates	25
Consideration of Accounting Estimates	26
Related Parties	27
Consideration of Related Parties	28
Appendix 1 – Accounting Estimates	29

Purpose

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

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

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

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 and Governance Committee should consider whether these responses are consistent with its understanding and whether there are any further comments it wishes to make.

This informing the risk assessment document covers both the Council and its group entities.

Fraud

Issue

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

As the 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 and Governance Committee regarding its processes for identifying and responding to risks of fraud
- communication to employees regarding business practices and ethical behaviour.

We need to understand how the Audit and Governance Committee oversees the above processes. We are also required to make inquiries of both management and the 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	Management response
<p>Has the Council assessed the risk of material misstatement in the financial statements due to fraud? What are the results of this process?</p>	<p>The Council's risk management process has identified the following as a Strategic Risk:</p> <p>Countering Fraud and Corruption: Risk that the Council fails to have proper, adequate, effective and efficient management arrangements, policies and procedures in place to mitigate the risk of fraud and corruption, particularly in a time of financial austerity, such that public money is misappropriated. This would result in a loss of funds to the Council, have a detrimental effect on services users, a negative impact on the Council's ability to achieve all of its priorities, value for money, and may have a negative impact on the Council's reputation.</p> <p>Risks are subject to ongoing review in accordance with the Council's Risk Management Strategy. The fraud risk was last formally reviewed in November 2017 when, following the identification and assessment of mitigating controls, the net risk was scored as medium.</p>
<p>What processes does the Council have in place to identify and respond to risks of fraud?</p>	<p>In addition to the strategic risk identified above, a detailed Fraud and Bribery Risk Assessment is in place in order to identify service specific risks to which the Council may be vulnerable.</p> <p>This assessment was initially produced by the Principal Auditor (Fraud) and took into account the areas identified in the Strategic Fraud Risk, local knowledge and also those risks identified in national publications such as Protecting the Public Purse and Fighting Fraud Locally. It was then shared with service managers to obtain their input and ensure that all significant risks had been identified and appropriate controls put in place to mitigate them.</p> <p>The outcome of this risk assessment has been used to inform proactive counter fraud work by Internal Audit. A piece of work is currently underway to carry out a detailed review of the risk assessment with a view to informing a programme of proactive work for 2018/19.</p>

Fraud risk assessment

Question	Management response
<p>Have any specific fraud risks, or areas with a high risk of fraud, been identified and what has been done to mitigate these risks?</p>	<p>The Internal Audit Plan for 2017/18 included proactive reviews to seek assurance as to the effectiveness of mitigating controls in place to manage the risk of fraud in areas identified as at risk in the risk assessment discussed in the response above.</p> <p>Further proactive reviews will be included within the 2018/19 Internal Audit Plan and, as stated above, the risk assessment will also be subject to review and update.</p>
<p>Are internal controls, including segregation of duties, in place and operating effectively? If not, where are the risk areas and what mitigating actions have been taken?</p>	<p>The AGS ensures a continuous review of the Council's governance arrangements, to give assurance on the effectiveness of the arrangements and/or to address identified weaknesses including the application of internal controls.</p> <p>The AGS is considered by the Corporate Leadership Team with the collection of evidence for, and the drafting of it being the responsibility of the Corporate Assurance Group (CAG). The review of governance arrangements in place is informed by the work of Internal Audit and senior managers and also comments made by the External Auditors and other review agencies/inspectorates.</p> <p>Sources of assurance include the Directors, Heads of Service and senior managers signing off the adequacy of controls within their service areas/directorate via disclosure statements. The disclosures are made available to, and considered by the Audit and Governance Committee as part of the evidence pack that supports the AGS.</p> <p>The production of the AGS also takes into account the annual internal audit opinion which provides assurance as to the adequacy of the Council's control environment and the action taken to ensure that any shortcomings are rectified promptly.</p> <p>With regards to the production of the AGS for 2017/18, a draft statement and action plan will be presented to the Audit and Governance Committee in May 2018 along with Internal Audit's Annual Report, and the final version will be presented to the July 2018 meeting of the Committee.</p> <p>Internal Audit work also provides assurance as to the effectiveness of internal controls and, where weaknesses are identified, mitigating actions are recommended to managers. Internal Audit follows up on the implementation of agreed recommendations to provide further assurance that improvements in the control environment have been made. Recommendations from external audit continue to relate to specific issues of segregation of duties within ICT, but these issues have been acknowledged and suitable mitigation is ongoing.</p>



Fraud risk assessment

Question	Management response
<p>Are internal controls, including segregation of duties, in place and operating effectively? If not, where are the risk areas and what mitigating actions have been taken? (continued)</p>	<p>A programme of audits is carried out in accordance with the Audit Plan that is approved by the Audit and Governance Committee. The work includes the Council's fundamental financial systems in order to gain assurance that the systems of financial control are in place and operating effectively.</p> <p>Internal Audit undertakes testing on internal controls by examining their effectiveness and in this way the Council can gain reasonable assurance with regard to the potential for override of management controls or other inappropriate influence over the financial reporting process. The outcome of each audit assignment is reported to management in order to:</p> <ul style="list-style-type: none"> • give an opinion on the risk and controls of the area under review, building up to the annual opinion on the control environment • prompt management to implement the agreed actions for change leading to improvement in the control environment and performance • provide a formal record of points arising from the audit, and where appropriate, of the agreements reached with management, together with appropriate timescales. <p>Interim reports on progress against and revisions to the Internal Audit Plan, together with a summary of work undertaken are received by the Audit and Governance Committee. The reports provide the Committee with an overview of the Council's response to internal audit activity to ensure any shortcomings in the control environment are rectified promptly. In May 2018 the Audit and Governance Committee will receive Internal Audit's annual opinion on the overall adequacy and effectiveness of the Council's control environment for 2017/18.</p>

Fraud risk assessment

Question	Management response
<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 receives quarterly performance monitoring reports from its ASDVs and this ensures that they receive detailed scrutiny in a similar fashion alongside in-house Council service areas. All financial reports are produced by Council staff who report to the Finance Manager using the same financial system and operating under the same control environment as in house service areas. Audit & Governance Committee have also received regular procurement updates, including details of all contract awards that required WARN (Waiver Approval & Record of Non-adherence) processes to be put in place.</p> <p>The Finance team is structured to provide specific support and guidance to the ASDVs. Accountants provide regular reports to the Company Boards. The commissioning or “client” finance role is undertaken by a Principal Accountant. Finance undertake a range of services which are ‘bought back’ by the ASDVs for an agreed rate. The financial package is designed to maintain financial robustness and meet statutory reporting requirements. An external review has recently been carried out of the Council’s ASDVs and the resultant report is due soon (late February 2018).</p> <p>Historic issues relating to procurement and land transactions have been subject to Internal Audit review during 2017/18 with further work underway to ensure that appropriate controls are now in place.</p>
<p>How does the Audit and Governance Committee exercise oversight over management’s processes for identifying and responding to risks of fraud and breaches of internal control? What arrangements are in place to report fraud issues and risks to the Audit and Governance Committee?</p>	<p>Audit and Governance Committee receive regular Risk Management Update reports relating to the Corporate Risk Register which includes the fraud risk.. The latest was received in December 2017 and a further report is being taken to the March 2018 meeting of the Committee.</p> <p>The AGS process, particularly the Head of Service Assurance Statements, provides the Committee with an understanding of the processes in place, any identified issues and mitigating actions.</p> <p>Internal Audit Update Reports to the Committee include details of Counter Fraud Work undertaken in accordance with the plan and in addition to this the Committee received/will receive the following reports:</p> <ul style="list-style-type: none"> • March 2017/2018 Informing the Risk Assessment for Cheshire East Council - this provides detailed information regarding the anti fraud and corruption arrangements and how the Council identifies and responds to the risk of fraud. • July 2018 Fraud and Corruption Update Report – this will provide Members with an overview of developments taking place nationally, an update on activity at Cheshire East, and, details of work planned to ensure compliance with best practice including the Code of Practice on Managing the Risk of Fraud and Corruption. <p>During 2017/18 additional resource was commissioned to support investigative work. Furthermore, the upcoming restructure of Internal Audit is intended to increase the amount of investigative/counter-fraud resource whilst maintaining the level audit resource thus safeguarding delivery of the 2018/19 plan.</p>

Fraud risk assessment

Question	
<p>How does the Council communicate and encourage ethical behaviour of its employees and contractors?</p>	<p>The Council ensures that the standards of conduct expected of staff are defined and communicated through, for example, Codes of Conduct, an Anti-Fraud and Corruption Policy and the Whistleblowing Policy. Such policies, together with the Council's Constitution, prescribe the arrangements that ensure all staff and contractors are aware of the standards expected of them.</p> <p>Cheshire East Council adopted a Code of Corporate Governance in 2009 which was updated in 2013 and again 2015 and is subject to annual review, and update, where necessary. A revised code was approved and adopted in January 2017 to ensure compliance with the CIPFA/Solace "Delivering Good Governance in Local Government – Framework" (2016 Edition).</p> <p>The Council undertakes an annual review of its governance arrangements to ensure continuing compliance with best practice as set out in the Framework. The Annual Governance Statement (AGS) is that review. The Council is required to prepare and publish the AGS.</p> <p>Principle A of the Council's Code of Corporate Governance is concerned with – "Behaving with integrity, demonstrating strong commitment to ethical values and respecting the rule of law" and sets out the supporting principles, behaviours and actions that demonstrate good governance and how this is evidenced in practice at Cheshire East Council.</p> <p>The Council has also taken part in a review of its culture which was conducted by the Local Government Association. Actions arising from the review will be addressed in accordance with agreed timescales.</p>

Fraud risk assessment

Question	
<p>How do you encourage employees to report their concerns about fraud? Have any significant issues been reported?</p>	<p>The Council's Anti Fraud and Corruption Policy states that each Member and officer of the Council is under a duty to report any reasonable suspicions and is encouraged to raise any concerns they may have in the knowledge that such concerns will be properly investigated. To this end, the Council has a Whistleblowing Policy, which was produced in accordance with best practice as set down in the PAS 1998:2008 Whistleblowing Arrangements Code of Practice which was produced by the British Standards Institute, to protect anyone who wishes to raise concerns about behaviour or practice.</p> <p>The Whistleblowing Policy is intended to cover major concerns that fall outside the scope of other procedures. These include:</p> <ul style="list-style-type: none"> • criminal offences • failure to comply with legal obligations • miscarriages of justice • dangers to health or safety, including risks to the public as well as other employees • damage to the environment • the unauthorised use of public funds • possible fraud and corruption • sexual or physical abuse of clients • other unethical conduct, or • deliberate concealment of any of the above categories <p>Concerns should be raised firstly with the supervisor/line manager or, where a person feels unable to do this, via other routes, for example:</p> <ul style="list-style-type: none"> • The Chief Executive, • Director of Legal Services, who is also the Monitoring Officer • Corporate Manager Governance and Audit. <p>The Council also has in place an online reporting form and a Whistleblowing email address. The Council ensures that any allegations received in any way, including by anonymous letters or telephone calls are taken seriously and investigated in an appropriate manner.</p> <p>The Council has recently commissioned Public Concern at work to undertake an external review of its whistleblowing arrangements. The outcome of this review and an updated Whistleblowing Policy is scheduled to be presented to the March 2018 meeting of the Audit and Governance Committee.</p>

Fraud risk assessment

Question	
Are you aware of any related party relationships or transactions that could give rise to risks of fraud?	<p>Council Officers are required to declare details of related party interests which are then reviewed by senior managers to ensure no staff members are in a position where they could unduly influence Council activity in relation to these parties. Senior Officers and Members are also required to complete an additional related parties disclosure to identify any relationships they or a close family member have with a potential Council trading partner.</p> <p>Reviews of such returns to date and in previous years have not indicated any relationships that would lead to a materially increased risk of fraud.</p>
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 2017?	None which have a material impact on the financial statements.
Are you aware of any whistleblower reports or reports under the Bribery Act since 1 April 2017? If so how does the Audit and Governance Committee respond to these?	<p>No reports have been made under the Bribery Act since 1 April 2017.</p> <p>Various whistleblowing reports have been received through the year but none which would have a material impact upon the financial statements. There were, however, a number of referrals during 2015/16 relating to the award of contracts and the use of waiver procedures that, whilst not material to the financial statements, attracted a great deal of public interest. These were shared with the External Auditor who agreed with the Council's response to them. These issues have subsequently resulted in a police investigation that remains ongoing.</p> <p>In addition, referrals have been received in relation to the payment of national minimum wage for sleep in shifts that have also been the source of an objection to the accounts. Audit and Governance Committee have been made aware of these matters formally and a significant amount of work has been undertaken to determine the extent of the issue with changes to payment arrangements implemented and back payments made to affected staff.</p> <p>Audit and Governance Committee receive regular reports detailing whistleblowing activity with the last one received in September 2017. The purpose of these reports is to allow the Committee to satisfy itself that appropriate management action is taken in response to whistleblowing referrals.</p>

Fraud risk assessment

Question	
<p>How is the Council strengthening its internal controls and following up on findings of internal audit and any external investigations into the Council, the conduct of specific former senior officers, governance process and weaknesses in internal controls?</p>	<ul style="list-style-type: none"> • Improved process for WARNs (Waiver Approval and Record of Non-adherence) with sign off required by Procurement, Finance and Legal prior to s151 and Monitoring Officer approval. There is also additional scrutiny by members of Audit and Governance Committee who receive regular procurement updates and copies of all WARM forms for information and comment. • Significant work has also been undertaken to ensure that there is an up to date Contracts register that is subject to monitoring to ensure that timely procurement is undertaken thus reducing the requirement for waivers and non compliant procurement. • Regular monitoring of both waivers and non adherences to Contract Procedure rules is undertaken with targets to reduce numbers. Regular reports are received by Corporate Leadership Team and a Procurement Board of both officers and Members was established to provide further transparency and scrutiny of procurement. The Procurement Board was replaced during 2017 by the Commissioning and Procurement Board which has a wider remit and aligns procurement and contract management processes. • Update of contract procedure rules to ensure that they are fit for purpose and fully understood by officers and members. • Processes around Officer Decision Records have also been improved with greater scrutiny and evidencing of supporting information by Chief Officers and the production of a central repository to record and retain all such records. • The Council has commissioned Public Concern at Work to provide a confidential advice service for employees who wish to raise concerns under the Whistleblowing process. PCAW have also undertaken a review of the Council's Whistleblowing arrangements and provided recommended actions for improvement. Progress on implementing these actions is being reported to the March 2018 meeting of Audit & Governance Committee along with a new Whistleblowing Policy that follows the best practice template provided by PCAW. • In addition to this review, the Council also recently commissioned the LGA to undertake an independent review of the culture of the organisation with particular focus on bullying. This outcomes from this review have been widely publicised both internally and externally and actions arising are being taken forward.

Fraud risk assessment

Question	
<p>How is the Council strengthening its internal controls and following up on findings of internal audit and any external investigations into the Council, the conduct of specific former senior officers, governance process and weaknesses in internal controls? (continued)</p>	<ul style="list-style-type: none">• Finally a major review and rewrite of the Council's Constitution has taken place to ensure that it is up to date, reflects best practice and is effective in setting out the way in which both Members and Officers are expected to conduct themselves and the business of the Council. The new Constitution went live in January 2018. <p>All of the specific matters referred to have been included within the 2016/17 Annual Governance Statement therefore acknowledging that they are issues and raising the profile of the importance of applying controls consistently and the implications of failing to do so.</p> <p>With regards to following up actions resulting from Internal Audit, these are subject to our normal follow up process with updates provided to Audit and Governance Committee via the Annual Audit Report and the Internal Audit Interim Report.</p> <p>For actions arising from external investigations, these are allocated to the appropriate manager for implementation and monitoring in accordance with normal procedures. However, for the Air Quality external investigation action plan Internal Audit has carried out a follow up review to provide assurance that these actions have been implemented.</p>

Fraud risk assessment

Question	
<p>More specifically, in light of the well-publicised issues of listed below, what actions have been undertaken by internal audit and other parts of the Council so far this financial year to ensure that CEC is free of fraud and complying with all applicable law and regulations in respect of these issues? This is in reference to:</p> <p>(1) Review of Contract Awards re Core Fit</p> <p>(2) Concerns and ongoing investigations relating to the conduct of Chief Executive and former Monitoring Officer</p> <p>(3) Alleged irregularities in the preparation of the Air Quality Annual Status Report</p>	<p>(1) This matter is still subject to police investigation. However, the improvements in procurement processes detailed above are intended to address the control weaknesses identified in this area. In order to obtain assurance that these improved processes are operating effectively, an Internal Audit review of the current arrangements within Procurement is currently underway and expected to be completed prior to the end of March 2018.</p> <p>(2) Interim arrangements have been put in place in response to the suspension of the Chief Executive, Chief Operating Officer and former Monitoring Officer (who has since left the Council). Formal IDC procedures are in progress and appropriate actions will be undertaken to address any control weaknesses or other actions identified following the completion of the formal disciplinary process. Recruitment to the position of Monitoring Officer is currently underway.</p> <p>(3) Following the Internal Audit of this area and the recommended external investigation, action plans were put in place to address control weaknesses in the following areas:</p> <ul style="list-style-type: none"> • Access control and version control of air quality data. This has now been addressed with access limited to one member of staff and strict version control implemented around data records. • Lack of Quality Assurance processes. The manual input of data has been replaced with an automated process with increased oversight from management. This provides assurance that data is accurate and has not been subject to manual intervention. • Poor Governance and oversight of air quality matters An Air Quality Steering Group consisting of both Members and Officers has been established to provide oversight and challenge to matters relating to air quality. As with other areas, the investigation and publicity around air quality has raised the profile across the Council of what the implications are of failing to follow due process.

Fraud risk assessment

Question (continued)	
<p>More specifically, in light of the well-publicised issues of listed below, what actions have been undertaken by internal audit and other parts of the Council so far this financial year to ensure that CEC is free of fraud and complying with all applicable law and regulations in respect of these issues? This is in reference to:</p> <p>(4) Legality of a £70K grant given to Berkeley Academy, Police investigation regarding this and resignation of the Deputy Leader in relation to this.</p> <p>(5) Historic underpayment of employees involved in provision of care services with sleep-in arrangements</p> <p>(6) Concerns raised over acquisitions following an internal audit review of the Council's arrangements for asset disposals and purchases in July 2017</p>	<p>(4) This was subject to a detailed Internal Audit investigation that was subsequently referred to the police and separate internal procedures. The risk of similar issues arising is mitigated by the improvements in governance described above and the increased scrutiny of the decision making processes.</p> <p>(5) Again, this matter has been subject to not only a significant amount of cross service work to determine the extent of the underpayments but also a detailed Internal Audit review to identify whether the underpayments were deliberate. With regards to the wider piece of work, this resulted in back dated payments being made to those staff identified as having been underpaid. In addition, service specific NMW compliant sleep in rates have been introduced and the Payroll system updated to ensure that correct rates are applied for all payments of this nature. Further clarification on this matter is expected when the 'Mencap appeal' is heard in late March 2018 and any further actions resulting from this will be addressed by the Council.</p> <p>(6) In response to these concerns Internal Audit has completed a number of detailed reviews relating to specific land transactions to determine whether due process was followed and if there was any wrongdoing on behalf of any officers or elected members. It should be noted that Land Transactions had been included in the 2017/18 Audit Plan and that this led to the more detailed investigations being undertaken. As a result of this work additional referrals to the police have been made.</p> <p>The detailed investigation work has been the priority with additional audit resource commissioned to ensure that resource was not diverted to the detriment of the Audit Plan. Upon completion of these individual reviews, a consolidated report detailing the control weaknesses identified and mitigating actions for implementation will be issued. A further piece of internal audit work will then be completed in early 2018/19 to test the current arrangements in place around land transactions to seek assurance as to the robustness of the controls. Appropriate actions will be raised as a result of this review and will be subject to our follow up processes.</p>



Laws and regulations

Issue

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 Governance 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 and Governance 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>What arrangements does the Council have in place to prevent and detect non-compliance with laws and regulations?</p>	<p>The Council has in place , within the Constitution, various procedure rules which set out how budget and policy decisions are made. Officers are required to ensure compliance with relevant laws and regulations and that lawful expenditure is delivered. Such arrangements are designed to provide reasonable assurance with regard to compliance rather than absolute certainty, because systems are susceptible to human error and poor judgment , controls can be deliberately circumvented or over-ridden.</p> <p>Reports provide a section for legal implications, and reports cannot go before Cabinet or Council without this being addressed. The Council's Statutory Officers have a positive responsibility to report to the Council, in respect of:</p> <ul style="list-style-type: none"> - co-ordination of functions, staff and management matters – the Head of Paid Service - financial administration, probity and propriety – the Section 151 Officer - legality and administration – Monitoring Officer
<p>How do management gain assurance that all relevant laws and regulations have been complied with?</p>	<p>Internal Audit's annual plan contains a programme of work that includes reviews of compliance with policies, procedures, laws and regulations. Management, therefore, gain assurance that relevant laws and regulations have been complied with via Internal Audit opinion and interim reports. Furthermore, as part of the AGS process the Directors, Heads of Service and Senior Managers are required to sign off on the adequacy of controls within their service areas/directorate via disclosure statements. The disclosures are made available to and considered by the Audit and Governance Committee in order that Members may discharge their duties with regard to approving the AGS.</p> <p>Progress against the actions in the AGS Action Plan is monitored throughout the year by the Corporate Assurance Group and reported to Audit and Governance Committee.</p> <p>In addition to these internal reviews, key areas of activity across the Council are subject to external assessment by bodies such as Ofsted, Care Quality Commission and the Information Commissioner.</p>

Impact of laws and regulations

Question	Management response
Have there been any instances of non-compliance or suspected non-compliance with law and regulation since 1 April 2017 with an on-going impact on the 2017/18 financial statements?	Since 1 April 2017 no instances of non-compliance are known to exist that will have an ongoing impact on the 2017/18 financial statements.
What arrangements does the Council have in place to identify, evaluate and account for litigation or claims?	<p>Legal Services assess litigation claims in conjunction with Finance Officers.</p> <p>The process to identify any litigation or claims in year that would affect the financial statements is completed as part of the closure of the accounts. This includes a year end review undertaken by the Director of Legal Services & Monitoring Officer and the Finance Managers.</p> <p>Where the Council believes that there is a potentially legitimate legal claim against it then this will be recognised on the balance sheet as a provision using the Council's best estimate of the likely costs it may incur. Where a claim is less likely to be successful but if successful could be material then it will be disclosed in the financial statements as a contingent liability.</p> <p>The status of insurance claims are reviewed regularly. In 2014/15 an actuarial investigation of the claims reserves was undertaken. The results have been factored into the Council's assessment of the level of its self-insurance and the procurement of external insurance.</p>
Is there any actual or potential litigation or claims that would affect the financial statements ?	Following changes in case law regarding sleep ins, payments have been increased to staff to meet the National Minimum Wage requirements going forward and where any breaches have been identified back pay has been made to those staff for a period of 2 years. The current liability of these cases could go back a total of 6 years in back pay. But following external counsel advice it has been recommended we hold this line pending the outcome of the Mencap appeal in March when it also might become clearer whether the government is willing to provide some extra funding for this national problem.

Impact of laws and regulations

Question	Management response
Have there been any reports from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance ?	There have been no reports from HMRC which indicate non-compliance. Following an inspection in 2017 the Council received confirmation from HMRC that they consider Cheshire East Council and associated companies to be low risk which reduces the chances/frequency of future inspections. There are no outstanding issues relating to the inspection.

Going Concern

Issue

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.

The Code of Practice on Local Authority Accounting in the United Kingdom (the Code) requires an authority's financial statements to be prepared on a going concern basis. Although the Council is not subject to the same future trading uncertainties as private sector entities, consideration of the key features of the going concern assumption provides an indication of the Council's financial resilience.

As auditor, we are responsible for considering the appropriateness of use of the going concern assumption in preparing the financial statements and to consider whether there are material uncertainties about the Council's ability to continue as a going concern that need to be disclosed in the financial statements. We discuss the going concern assumption with management and review the Council's financial and operating performance.

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

Going concern considerations

Question	Management response
<p>Does the Council have procedures in place to assess the Council's ability to continue as a going concern ?</p>	<p>Yes, the Council undertakes a review of its status in advance of producing the Annual Statement of Accounts and has procedures in place to make that assessment including the following:</p> <p>The Council's Medium Term Financial Strategy 2017/20 and Treasury Management Strategy were approved by Council on 23 February 2017, for the 2017/18 Financial Year. In addition a balanced budget was approved by Council on 22nd February 2018 for the 2018/19 financial year.</p> <p>The Three Year Summary Position identified the forecast expenditure on services compared to the continued grant funding streams from government and future levels of council tax, business rates and income received direct from services users. The report also considered the robustness of the estimates and the adequacy of reserves allowed for in the budget proposals, so that members had authoritative advice available to them when they made their decisions.</p> <p>The Council has also published Guidance and Data on the Financial Resilience of the Council. The Council's Three-Quarter Year Review of Performance was reported to Cabinet in February 2018. This predicted a small overspend of £0.1m against budget.</p> <p>Financial Resilience is identified as a key risk in the Corporate Risk Register:</p> <p><i>Financial Resilience: The reduction in funding from Central Government means the Council projects significant funding gaps over the next four years, there is a possibility that the Council does not adapt its financial plans in sufficient detail quickly enough, either by deferring the difficult decisions about services, using over-optimistic planning assumptions, or not rethinking sources of income. This may result in difficulties in closing and managing the budget gaps, financial stress and may impede the Council's ability to meet its statutory requirements, and deliver all of its intended outcomes and objectives in full.</i></p> <p>As part of the approval process for the Statement of Accounts the Section 151 Officer will provide assurance regarding the key risks, policies and concepts applicable to the accounts and any such disclosures that are necessary to present fairly the financial position of the Council at its year end.</p> <p>All wholly owned companies benefit from a number of guarantees put in place by the authority. Their payments to the Cheshire Pension Fund (based on defined contributions towards current service costs) are guaranteed by the Council, and the Council retains responsibility for past service deficits and accounting for pensions assets and liabilities. Each company receives regular payments in advance from the Council to cover known expenses. To cover unforeseen events each company also has access to an automatic loan facility from the Council, repayable on commercial terms.</p>

Going concern considerations

Question	Management response
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?	<p>Any events or conditions which could impact on the Council's status as a going concern are raised with Management as part of the financial cycle of planning, monitoring and reporting. There are currently no outstanding issues.</p> <p>The financial stability of the Council, which determines the amount of money available for service expenditure, should be exposed to less risk from further Government funding shortfalls in the medium term. This has been strengthened by the submission to DCLG of the 4 Year Efficiency Plan in October 2016. This confirmed the Council's acceptance of the 2016/17 Finance Settlement funding levels which are now guaranteed up to the end of 2019/20. These were reconfirmed in the Provisional Finance Settlement released on 19th December 2017 and the Final Settlement released on 6th February 2018.</p>
Are arrangements in place to report the going concern assessment to the Audit and Governance Committee?	Yes, as part of the reporting process to the Audit and Governance Committee which includes the Treasury Management Strategy and Annual Report; the Statement of Accounts and Annual Governance Statement and regular updates on the Corporate Risk Register.
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?	<p>The Council has set a balanced budget for 2018/19 and this takes into account relevant financial assumptions and financial information provided throughout the year.</p> <p>At the third quarter stage of 2017/18, the Council's reserves strategy remains effective with a small forecast overspend of £0.1m (0.04%) against a budget of £264.8m. Portfolio Holders and the Corporate Leadership Team continue to focus on managing this position to avoid any impact on the Council's general reserves at year end.</p>

Going concern considerations

Question	Management response
Are the implications of statutory or policy changes appropriately reflected in the Business Plan, financial forecasts and report on the going concern?	Yes, the Councils Corporate Plan and reports to Cabinet throughout the year set out the implications of statutory or policy changes. All reports to Cabinet contain a section on Financial Implications authorised by the Section 151 Officer. The Corporate Plan for 2017- 20 was reported to Cabinet / Council in February 2017.
Have there been any significant issues raised with the Audit and Governance 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 significant issues have been reported to date in 2017/18 which would cast doubt on the assumptions made. The Audit and Governance Committee receives regular reports from internal and external audit throughout the year and will receive the Statement of Accounts and the Annual Governance Statement for approval on the earlier deadline of 31 July 2018.
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?	Financial information on revenue and capital expenditure is reported to managers via a suite of financial reports on a monthly basis. Performance on treasury management is reported quarterly to Cabinet through the Financial Performance Report. The Council receives quarterly performance monitoring reports from all its ASDVs. No adverse financial indicators have been identified.

Going concern considerations

Question	Management response
<p>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?</p> <p>If not, what action is being taken to obtain those skills?</p>	<p>Yes. The Council has established the three directorates of People, Place and Corporate. The Team Plans within each directorate are focused on the achievement of the Strategic Outcomes within the Corporate Plan 2017/20. Performance of Team Plan owners, at 3rd Tier, are held to account by the Executive Directors who are also members of the Corporate Leadership Team.</p> <p>The Council has a corporate leadership team in place with the following Chief Officers; a number of interim arrangements are in place for 2017/18:</p> <p>Kath O'Dwyer – Acting Chief Executive Mark Palethorpe– Acting Executive Director of Peoples Services Jan Willis – Interim Executive Director of Corporate Services (S151 Officer) Frank Jordan - Executive Director of Place and Acting Deputy Chief Executive</p> <p>Other statutory posts include Dan Dickinson (Acting Director of Legal Services and Monitoring Officer) and Fiona Reynolds (Director of Public Health).</p>

Accounting estimates

Issue

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. 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 Council 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 Council is using as part of its accounts preparation; these are detailed in appendix 1 to this report. We would ask the Audit and Governance Committee to satisfy itself that the arrangements for accounting estimates are adequate. 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.

Consideration of accounting estimates

Question	Management response
Are 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?	Yes, as part of the Closure of Accounts process, a review is undertaken to identify accounting estimates that require significant judgement and the note is updated accordingly. Discussions take place with Directors/Head of Service as part of budget monitoring and outturn meetings, and will be agreed with management prior to inclusion in the accounts.
Are the management arrangements for the accounting estimates, as detailed in Appendix 1 reasonable?	Yes, further details are provided in the table on Accounting Estimates.
How is the Audit and Governance Committee provided with assurance that the arrangements for accounting estimates are adequate?	Any amendments to the accounting estimates are reported and approved by the Audit & Governance Committee prior to inclusion in the Statement of Accounts. Members of the Committee also receive training prior to approving the Statement of Accounts so any issues and queries on the accounting estimates can be raised.

Related Parties

Issue

Matters in relation to Related Parties

ISA (UK&I) 550 covers auditor responsibilities relating to related party transactions. Many related party transactions are in the normal course of business and may not carry a higher risk of material misstatement. However in some circumstances the nature of the relationships and transaction may give rise to higher risks.

For local government bodies the Code of Practice on Local Authority Accounting in the United Kingdom (the Code) requires compliance with IAS24: related party disclosures. The Code identifies the following as related parties:

- Subsidiaries;
- Associates;
- Joint ventures
- An entity that has an interest in the authority that gives it significant influence;
- Key management personnel and close family members; and
- Pension fund for the benefit of employees

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.



Consideration of Related Parties

Question	Management response
<p>What controls does the Council have in place to identify, account for and disclose related party transactions and relationships ?</p>	<p>A number of arrangements are in place for identifying the nature of a related party and reported value including:</p> <ul style="list-style-type: none">Annual return from senior managers and members stating details of any known related party interests.Review of minutes of decision making meetings to identify any member declarations and therefore related parties.Finance staff review information collated in each service to identify potential related parties.Review of in-year income and expenditure transactions with known identified related parties from prior year information.

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 and equipment valuations	Based on Current or Fair Value – dependent on the class of assets will determine EUV, MV or DRC, MEA	A 3 stage QA process with Deloitte, Assets and finally Finance , quality assuring and challenging the valuations	Deloitte have been appointed on a 5 year contract	When completing the valuation process and in line with the RICs and CIPFA standards all valuations are considered on number of basis before a decision is made to take a particular one.	No
Estimated remaining useful lives of PPE	For Buildings and Land Deloitte use Building Surveyor information to determine a useful life. With all other PPE valued at cost the service user determines the useful life of an asset.	Part of the challenge process above particularly if a life has significantly increased or decreased. For other PPE ensure they are in line with our accounting policies.	Yes for Buildings and Land	The valuers and service users provide the estimate for the remaining useful life	No
Depreciation and amortisation	Straight line method	In line with CIPFA Code, accounting standards and the Council's accounting policies	No (except where used to determine asset life)	The length of the life is determined at the point of acquisition or revaluation.	No
Impairments	Conduct an impairment review annually, review helpdesk queries to establish whether any buildings have suffered an impairment and confirm whether the repairs have been remediated.	Quality Assurance from Valuation Team in conjunction with Facilities Management officers	Yes- in house valuation team	The same process as with a valuation – if an impairment has occurred Deloitte would be required to give a valuation based on the reason for the impairment of the asset	No

Appendix 1 - Accounting Estimates (continued)

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 Cheshire Local Government Pension Scheme. The administering authority (Cheshire West and Chester 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 - Hymans	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
Long term obligations under PFI schemes	The Council has assessed these arrangements under IFRIC 12 – recognizing the assets used to deliver the services on the Council's balance sheet along with a corresponding liability.	The model developed by Grant Thornton is used to calculate the relevant accounting entries.	Deloitte have been appointed to revalue the buildings.	The initial recognition of the asset/liability is based on costs within the operator's financial model and the embedded finance lease repayments are estimated by deducting service and lifecycle costs from the Unitary Charge.	No

Appendix 1 - Accounting Estimates (continued)

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?
Impairment of receivables (bad debt provision)	A review of balances is carried out annually and an impairment provision for doubtful debts is made in accordance with the accounting policy.	In accordance with the accounting policy.	No	Calculation takes into account historical experience, current trends and other relevant factors.	No
Accruals	Auto Accruals Process and Commitment Accounting Reports used to identify expenditure incurred	In accordance with the Council's accounting policies and controlled through the budget monitoring process.	No	None	No
Provision and contingent liabilities	Identified from discussions with management to identify obligations. 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.	In accordance with CIPFA guidance and accounting standards	No	None	No

Appendix 1 - Accounting Estimates (continued)

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?
Investments in companies valuations	Estimates are based on the use of accepted valuation models. These are prepared by the Council based on the audited financial statements of the companies and include: Alderley Park Holdings Ltd Manchester Science Parks Ltd	These will be based on the audited financial statements and reviewed by the corporate finance team.	When necessary external advice will be sought.	None	No
Non-adjusting events – events after the BS date	A review is completed at year end requesting information from Corporate Leadership Team, Heads of Services and Finance.	Peer review to check all non-adjusting events have been captured.	No	None	No

Appendix 1 - Accounting Estimates (continued)

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?
Measurement of Financial Instruments - PWLB loans	PWLB loans – fair values based on information provided by PWLB	Part of established year end plan for dealing with financial instrument valuations.	Yes – Arlingclose Ltd	Does not give rise to any material differences in the accounts – expertise of company with access to market information used, no alternatives considered	No
Measurement of Financial Instruments - Investments	Investments - fair values based on equivalent loans from (where possible) the same borrowers based on the outstanding maturity period of each loan. Investments held in CD's – market value based on an equivalent CD from the same issuer with similar maturity characteristics available on or close to 31st March.	Part of established year end plan for dealing with financial instrument valuations.	Yes – Arlingclose Ltd	Does not give rise to any material differences in the accounts – expertise of company with access to market information used, no alternatives considered	No
Measurement of Financial Instruments - Market LOBO loans	Market LOBO loans – fair values based on discounting the contractual cash flows over the whole life of the instrument at the appropriate interest rate swap rate and adding the value of the embedded options.	Part of established year end plan for dealing with financial instrument valuations.	Yes – Arlingclose Ltd	Does not give rise to any material differences in the accounts – expertise of company with access to market information used, no alternatives considered	No

