

Informing the audit risk assessment for South Lakeland District Council 2020/21

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Purpose

The purpose of this report is to contribute towards the effective two-way communication between South Lakeland District Council's external auditors and South Lakeland District 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 South Lakeland District 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 |
|---|--|
| <p>1. What do you regard as the key events or issues that will have a significant impact on the financial statements for 2020/21?</p> | <p>Covid-19 has had the following impacts:</p> <ul style="list-style-type: none"> a) Amended governance arrangements: virtual meetings, live streaming, additional resources to support b) Financial implications: <ul style="list-style-type: none"> a) Loss of income, especially from car parking charges, NNDR and delays in Council tax collection b) Additional government grants <ul style="list-style-type: none"> a) non-ring fenced for general costs, b) sales fees & charges c) S31 grants: business support, NNDR reliefs etc d) Ring-fenced grants: reopening high street c) Impact on longer term financial sustainability d) Changes in valuations of assets and liabilities including PPE and pensions e) Increases in demand: over £100m of grants paid to support businesses and individuals c) Prioritisation of resources around business as usual / Covid / projects <p>An update of the Covid-19 impact assessment will be shared shortly</p> <p>Other key events:</p> <ul style="list-style-type: none"> 1) Customer Connect: continued transition of staff into new ways of working & roll out of MyAccount (especially for NNDR/council tax in February 2021) 2) Local Government Reorganisation – the Council has participated in the preparation and submission of a bid to form a new unitary authority “The Bay” with Lancaster City Council and Barrow Borough Council. This may not have an impact on the financial accounts for 2020/21 but may have an impact from 2021/22 onwards depending on the decision of the Secretary of State 3) Kendal Town Hall / South Lakeland House were closed to the public and undergoing renovation for part of the year: KTH has now largely reopened (subject to Covid restrictions) while the top and ground floor of SLH are now being renovated with the first floor now complete and reopened (subject to Covid). |

General Enquiries of Management

| Question | Management response |
|--|--|
| <p>2. Have you considered the appropriateness of the accounting policies adopted by South Lakeland District Council? Have there been any events or transactions that may cause you to change or adopt new accounting policies?</p> | <p>Yes; revised Accounting policies were considered by Audit Committee on 22 April 2021: no major changes but the applicability of each policy was considered beside Covid changes.</p> <p>Since IFRS 16 Leases has been delayed again for another year there are no major changes but the opportunity has been taken to update the presentation and content of policies to make the accounts more understandable to users.</p> |
| <p>3. Is there any use of financial instruments, including derivatives?</p> | <p>The Council has very straightforward financial arrangements. There is no use of short term borrowing at the year-end. All long term borrowing is through fixed interest, maturity loans from the PWLB and there has been no new borrowing in year.</p> <p>All investments are in accordance with the TM policies approved annually in February as part of the budget approval process. Exceptionally Council approved the amendment of the TM policies as part of the Covid-19 budget review to raise the limit for Money Market Funds from £5m to £10m and to permit funds to be left at the Council's main bank where the money was received as earmarked grants (this change made permanent in the TM policies approved in February 2021).</p> |
| <p>4. Are you aware of any significant transaction outside the normal course of business?</p> | <p>Covid-19 grants and business rate reliefs, including the NNDR Collection Account deficit @ 31/3/2021 is expected to be around £28m with the SLDC share around £11m due to timing of recognition of Covid-19 grants.</p> <p>Kendal ERDF Flood Relief Scheme underway: treated as agency spend as the Council has no control over the programme, the values or the timing of work which is controlled by MHCLG and delivered by the EA.</p> <p>In March 2020 the Council received £2.48m from Highways England relating to the building of a roundabout at Cross-a-Moor, near Ulverston: this was repaid to Highways England in October 2020. The Council is currently negotiation agreements with Cumbria LEP and Highway England for delivery of the scheme and received £0.9m of Growth Deal grant on 31 March 2021.</p> |

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? | <p>We carry out an impairment review on our non-current assets as part of our final accounts process.</p> <p>Renovation of South Lakeland House/Kendal Town Hall – KTH reopening in May 2021. SLH is open but 2/3 is currently with the contractors – in May they handed back the first 1/3rd. We have proposed the Town Hall is treated as an asset under construction, SLH will be revalued on existing use: a detailed proposal has been shared with Hebe.</p> <p>Car Parks – mainly valued based on turnover, income has been very low for the majority of the year although tourist areas did well during the summer. There has been some variation in car park values at 31 March 2021: finance specialists reviewed the valuations and the methodology and data behind these values.</p> <p>Kendal Leisure Centre has been closed for the majority of the financial year and the main hall was used by the NHS as a recovery centre but this did not involve permanent changes to the fabric of the building and it is not expected to have an impact on the valuation.</p> <p>There have been no material insurance claims related to PPE during the year.</p> |
| 6. Are you aware of any guarantee contracts? | <p>The Council has agreed a guarantee for a road-improvement scheme at Cross-a-Moor near Ulverston: approved by Council in October 2020. Funds have been set aside in the capital programme to fully fund the guarantee from capital receipts should it be called upon. Further guarantees have been sought relating to Growth Deal funding for the same scheme, full details were reported on Council on 30th March 2021.</p> <p>Other guarantees relate to the LSVT in March 2012: there has been no change in the circumstances around these guarantees in 2020/21.</p> |
| 7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements? | <p>None that are material. NHS trust business rates claim has now been excluded.</p> <p>MMI settlement scheme – suggestion that there could be a further levy: a reserve has been established to meet any costs.</p> |

General Enquiries of Management

| Question | Management response |
|--|--|
| 8. Other than in house solicitors, can you provide details of those solicitors utilised by South Lakeland District Council during the year. Please indicate where they are working on open litigation or contingencies from prior years? | See appendix 1 |
| 9. Have any of South Lakeland District 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>VAT: Lancashire County Council and PS Tax as required</p> <p>Treasury including valuation of financial instruments: Link Asset Services</p> <p>Local Government Reorganisation: Connect PA</p> <p>Asset management and valuations: LSH</p> <p>Leisure services partner (GLL) open book review: Knight Kavanagh Page</p> <p>For more details see appendix 2</p> <p>External advisors are used for some technical areas of operational activity including viability assessments for planning applications, quantity surveyors for construction schemes etc which are not included in this list but can be provided if required.</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 South Lakeland District 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 South Lakeland District Council's management.

Fraud risk assessment

| Question | Management response |
|--|--|
| <p>1. Have South Lakeland District 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>Although there is ongoing risk of fraud being committed against the Council, arrangements are in place to both prevent and detect fraud. This includes a dedicated counter fraud officer to investigate allegations of fraud.</p> <p>The risk of material misstatement of the accounts due to undetected fraud is assessed to be low. Although there is an on-going risk of fraud being committed against the Council, clear and effective arrangements are in place to prevent and detect fraud. No material instances of fraud have been identified in 2020/21.</p> <p>The Counter Fraud specialist undertakes reactive, and proactive investigations across the organisation, which includes higher risk areas such as housing benefits and council tax. The risk of material misstatement of the accounts due to un-detected Fraud is considered low.</p> |
| <p>2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?</p> | <p>There are no material instances of fraud that have been identified during the year. There are some areas that are inherently at risk from fraud such as:</p> <ul style="list-style-type: none"> • Covid related grants and reliefs • Council Tax, including Single person discount, and NNDR including Small Business Rate Relief • Income streams such as sales, fees and charges. • Cyber related fraud • Procurement. <p>The Council is a participant in the National Fraud Initiative and review matches as they become available (NFI data sets and app check).</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 South Lakeland District 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>Not beyond the routine housing benefits / grant / discounts frauds seen every year.</p> <p>Risk of fraud has been reviewed as part of the fraud risk assessment process which supports the fraud strategy and the work of the Fraud Specialist. Material changes to activity will result in a re-alignment of work of the Fraud Specialist: for example the quantity and value of Covid-19 grants to businesses. Fraud risk assessment will also influence the internal audit plan – Covid-19 grants is included in the plan for 2021/22.</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 South Lakeland District Council where fraud is more likely to occur?</p> | <p>Covid-19 business grants, grants to individuals and business rate reliefs.</p> <p>Including:</p> <ul style="list-style-type: none"> a) Claiming businesses were closed while still trading b) Claiming to be the business owner / operator and claiming monies due to others c) Claiming second homes were actually holiday lets (this area of potential fraud was highlighted to Government, proposals have now been made to restrict the ability to classify homes as holiday lets unless there is evidence of letting activity.) <p>Excluding Covid-19, the main areas of business at risk of fraud are housing benefit and council tax benefit claims, business rate grants and relief, creditor payments. Individual service fraud risk assessments can be made available.</p> <p>No locations have been identified as a greater fraud-risk</p> |
| <p>5. What processes do South Lakeland District Council have in place to identify and respond to risks of fraud?</p> | <p>The Council employs a Fraud Specialist to monitor and review systems and processes to identify and address fraud risks. She also gives advice and guidance to officers and carries out fraud risk assessments and investigates suspected fraud. She coordinates the National Fraud Initiative submissions and responses.</p> <p>Fraud is included in internal training (including induction training).</p> |

Fraud risk assessment

| Question | Management response |
|--|--|
| <p>6. How do you assess the overall control environment for South Lakeland District 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 – rolling 3year programme to review key risks including core financial and governance systems. Include reviews of appropriateness and application of Financial Procedure Rules & Contract Procedure Rules.</p> <p>Integra finance system requires separation of raising and authorising of purchase orders. Invoices received centrally for payment and matched to PO/GRN.</p> <p>Separation of duties in review and approval of Covid-19 grants through ESB agile system. Limits on signing of contracts: require review by Monitoring Officer or legal services team.</p> <p>Additional checks are undertaken in relation to payment of certain Covid-19 checks where payee details were checked against external databases in accordance with the requirements of the Government’s Business Grants Team (Jointly Department for Business, Energy and Industrial Strategy and Ministry of Housing, Communities and Local Government) and other grant making bodies.</p> <p>There are no areas were there is potential for override of controls or inappropriate influence over the financial reporting process. No pressure is placed on officers to achieve financial targets.</p> |

Fraud risk assessment

| Question | Management response |
|---|---|
| 7. Are there any areas where there is potential for misreporting? | <p>Three main reasons for misreporting:</p> <ol style="list-style-type: none"> 1. Error 2. Omission 3. Misjudgement <p>Significant payments (over £10,000) checked by bank signatory before payment (it should be noted that due to the number of Covid-19 grant payments in 2020 there were spot-checks of each grant payment run rather than 100% check on each payment).</p> <p>Staff involved in the preparation of the accounts are qualified and keep their CPD up-to-date which includes attending the CIPFA year-end training sessions and sessions offered by Grant Thornton. Gov.uk and CIPFA email alerts are used to ensure changes to proper practice are identified and followed. All elements of the accounts are reviewed by a second senior finance officer to check for error, omission and misjudgement. Changes between years are reviewed to identify particular areas for review.</p> <p>For 2020/21 the areas with greatest risk are:</p> <ul style="list-style-type: none"> • Non-current assets, particularly valuations of land and property, due to the number of assets, the complexity of the accounting treatments and the values involved. • Collection fund accounting: particularly the value and treatment of additional Covid grants and the tax income guarantee calculation and treatment of deficits • Non-collection fund Covid grants and the treatment (agency v. principle, cost of services or general taxation). • Housing benefit subsidy – no new issues but large values. • Pension valuations – no new issues but had material uncertainty in 2019/20 |

Fraud risk assessment

| Question | Management response |
|--|--|
| <p>8. How do South Lakeland District 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>Leadership team development values and behaviours which have been incorporated into the Council Plan refresh approved in February 2021. Team leader training is being roll-out in all teams.</p> <p>Leadership team have received training on corporate governance and this has been rolled out to all staff with the training recorded and available on the internal training website.</p> <p>Corporate governance is a standing item on Corporate Management Team agendas.</p> <p>The Constitution includes officer and member codes of practice.</p> <p>The Fraud Specialist publishes guidance and updates on fraud awareness and gives training including publication of fraud reporting phone number. There is also e-learning on fraud prevention available to all staff.</p> <p>The Council also has policies on whistleblowing, anti-bribery/corruption and money laundering available on SharePoint and on the main Council website.</p> <p>No significant issues have been reported.</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>Leadership team / Finance Specialists / Bank signatories / Legal / Procurement / Revenues staff / Benefits staff / System administrators / IT staff / Planning, building control, licensing, environmental health staff</p> <p>Staff involved in assessing and approving Covid-19 grants</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>Training on requirements of officer and member codes of conduct</p> <p>Members interests recorded and publicly available</p> <p>Registers of gifts and hospitality</p> <p>Internal audit review carried out in 2021 on Members Interest and Declarations: reported to Audit and to Standards Committees in April 2021.</p> <p>Annual reviews of related parties via questionnaires.</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?</p> <p>What has been the outcome of these arrangements so far this year?</p> | <p>Usually an annual report to the Audit Committee summarises arrangements for identifying and responding to fraud risk and the anti-fraud activity that has taken place over the previous 12 months. This report was last considered by Audit Committee in September 2019 and the next report will be taken in July 2021. This also includes the outcome of participation in NFI data matching exercises.</p> <p>Audit Committee receives all internal and external audit reports, which would highlight any actual fraud as well as identifying potential fraud.</p> <p>Audit Committee received a Covid-19 update in September 2020 which included reference to potential fraud around business grants.</p> <p>Right of Head of Internal Audit / S151 Officer / Monitoring Officer to report to Audit Committee (including private meeting annually between audit and Audit Committee).</p> <p>Right of Head of Internal Audit / S151 Officer / Monitoring Officer to report directly to Chief Executive on any material concern.</p> <p>Material individual concerns communicated by S151 of relevant member of CMT and to Monitoring Officer.</p> <p>No material frauds have been identified. If a material fraud were identified, the Chair of Audit Committee would be informed along with auditors.</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

Issue

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 South Lakeland District 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 South Lakeland District Council have in place to prevent and detect non-compliance with laws and regulations?</p> <p>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>This is dealt with in the annual governance statement.</p> <p>All reports to committees contain a section covering the legislation on the matter under consideration, which are reviewed by legal staff for decision reporting.</p> <p>The Monitoring Officer is responsible for ensuring that the council is compliant with laws and regulations. These responsibilities include:</p> <ul style="list-style-type: none"> • Report on contraventions or likely contraventions of any enactment or rule of law • Report on any maladministration or injustice where Ombudsman has carried out an investigation • Investigate and report any misconduct in compliance with regulations • Advice on vires issues, maladministration, financial impropriety, probity and policy framework and budget issues to all members <p>The Monitoring Officer has access to all committee reports and also raises awareness on legal requirements at meetings where needed. In addition, in terms of any specific issue, they would get involved at an early stage, including vetting reports for legal issues.</p> |
| <p>2. How is the Audit Committee provided with assurance that all relevant laws and regulations have been complied with?</p> | <p>Through the Annual Governance Statement process.</p> <p>The S151 officer is responsible for preparing the accounting statements in accordance with relevant legal and regulatory requirements. The Monitoring Officer (or representative) attends Audit Committee meetings and advises members on any areas of concern. Regular updates of the Council's risk register are considered by CMT and the Audit Committee. The financial and legal implications are set out in the committee reports.</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>No</p> |

Impact of laws and regulations

| Question | Management response |
|---|--|
| 4. Is there any actual or potential litigation or claims that would affect the financial statements? | No |
| 5. What arrangements does South Lakeland District Council have in place to identify, evaluate and account for litigation or claims? | The process is consistent with the prior year. The Monitoring Officer is responsible for identifying and evaluating claims in the first instance. If the Council could not deal with claims in-house then an external solicitor is engaged. |
| 6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance? | No |

Related Parties

Issue

Matters in relation to Related Parties

South Lakeland District 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 South Lakeland District 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 South Lakeland District 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 South Lakeland District Council whether South Lakeland District Council has entered into or plans to enter into any transactions with these related parties the type and purpose of these transactions | <p>Note 34 to the accounts details the material related parties: board member of Ulverston Community Enterprise (which operates Coronation Hall and Ulverston Markets and a separate member who is director of a leisure company in the area with operations on Lake Windermere). During 2019/20 an internal audit report has been prepared on Members Interests and Declarations. A copy was reported to Audit Committee in April 2021: https://democracy.southlakeland.gov.uk/ieListDocuments.aspx?CId=135&MId=5042&Ver=4 and was assessed as "reasonable assurance" with 3 recommendations. The report was also considered by Standards Committee in April 2021: https://democracy.southlakeland.gov.uk/ieListDocuments.aspx?CId=139&MId=5041&Ver=4</p> |
| <p>2. What controls does South Lakeland District Council have in place to identify, account for and disclose related party transactions and relationships?</p> | <p>Officers received and collate questionnaires on related parties from officers and members. Any discrepancies from previous years declarations, appointments or officer knowledge are identified then these are chased up individually. Transactions are checked for all related parties identified. The council nominates representatives to organisations which are approved via Cabinet or Council. Reports on representation on organisations boards are reported to the Council. The Council also has relationships with South Lakes Housing following the LSVT in March 2012.</p> |
| <p>3. What controls are in place to authorise and approve significant transactions and arrangements with related parties?</p> | <p>Members receive training to support the appropriate governance of their role and their compliance with laws, regulations and the requirements of the role. This includes training on related party transactions, and the expectations of their role in ensuring only appropriate transactions are undertaken, and that all are approved and reported on.</p> |
| <p>4. What controls are in place to authorise and approve significant transactions outside of the normal course of business?</p> | <p>All transactions have to follow standard Council procurement guidelines, which include a number of key controls at each step in the transaction. Related party transactions are captured, and reported on in full. The controls above are in place for all related party transactions, regardless of whether they are inside, or outside the normal course of business.</p> |

Accounting estimates

Issue

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 |
|---|---|
| <p>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?</p> | <p>Material transactions / events etc: most significant is impact of Covid-19 on value of assets, additional grants (including classification between agent and principal) and impact on outstanding debts and NNDR appeals. Valuation for Rating (Coronavirus)(England) Regulations 2021 replaces the impact of NNDR appeals on the grounds of material change of circumstances going forwards.</p> |
| <p>2. How does the Council's risk management process identify and addresses risks relating to accounting estimates?</p> | <p>For 2020/21 officers have updated a risk assessment process which considers:</p> <ul style="list-style-type: none"> • Value • Impact on operating costs • Criticality to operational delivery • Past experience • External scrutiny (area of political / public sensitivity) • Judgement: where specific expertise is required <p>Risks are graded low (green), medium (amber) and high (red). This reflects the methodology set out in the CIPFA Balance Sheet management in the public services – a framework for good practice. Where risks are identified as high the key issues will be summarised and reported to Corporate Management Team.</p> |
| <p>3. How do management identify the methods, assumptions or source data, and the need for changes in them, in relation to key accounting estimates?</p> | <p>Methods: based on changes in regulation and external guidance (accounting standards, ACOP and ACOP Guidance Notes). Assumptions: based on past experience, consideration of best practice and professional knowledge. External advisors and valuers are used for land and property (LSH), pensions (Mercers) and financial instruments (Link) Source data: comes from a number of sources depending on the nature of the estimate but includes balances and transactions on Integra (where relevant) and records of ownership of land and buildings. Need for changes: based on in-year review of changes in standards / guidance / good practice and changes in ownership / values.</p> |

Accounting Estimates - General Enquiries of Management

| Question | Management response |
|---|--|
| 4. How do management review the outcomes of previous accounting estimates? | <p>For land & buildings, investment properties and pensions valuations the values at 1 April 2020 are compared to changes and values at 31 April 2021 as provided by external advisors. Estimated useful lives are compared to repair and maintenance costs and projections.</p> <p>For provisions for bad debts and provisions for appeals, the estimates are reviewed against actual write-offs or actual appeals settled.</p> <p>For material accruals, the estimate is compared to the actual settled value.</p> <p>Any material changes are reported as identified: for example it was identified that there was an error in the value of the accrual for housing benefit subsidy was identified as part of the audit for 2018/19 and reported to managers and councillors as part of the Corporate Financial Update process.</p> |
| 5. Were any changes made to the estimation processes in 2020/21 and, if so, what was the reason for these? | <p>Calculation of provision for NNDR appeals: the methodology for the 2005/2010 list is being applied to the 2017 list, until now a simpler model using an average success rate for all grounds for appeal had been used for the 2017 list as there were only a small number of claims. The number and value of challenges has increased significantly during 2020/21 so it is now appropriate to split the reasons and apply a success rate for each ground for appeal (deletions, material change of circumstances etc).</p> |
| 6. How do management identify the need for and apply specialised skills or knowledge related to accounting estimates? | <p>Identified through the professional and organisational expertise of the finance specialists: material areas of spend are reviewed regularly through the corporate budgeting and monitoring process. Some balance sheet management is also carried out. Also from internal and external audit advice and reviews.</p> <p>The major areas of accounting estimates relate to the valuation of non-current assets where external advice and valuations are prepared: land and property, financial instruments and pensions.</p> <p>Allocations of staff time, and therefore allocation of management overheads, are based on information provided by each Operational or Specialist Lead.</p> |

Accounting Estimates - General Enquiries of Management

| Question | Management response |
|--|--|
| <p>7. How does the Council determine what control activities are needed for significant accounting estimates, including the controls at any service providers or management experts?</p> | <p>It is judgement based primarily on materiality but will also take into account changes in the regulatory/accounting environment and best practice.</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>Regular monitoring reports are provided to Cabinet, Overview and Scrutiny Committee and Council, and are subject to further review as necessary. Reports on specific areas, such Customer Connect are considered directly by the Audit Committee.</p> <p>We are reliant on assurance from the Pensions Team at Cumbria County Council as the Administering Authority and the valuers at LSH, the Council's property services contractor.</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>Notes 4 and 5 of the Statement of Accounts is allocated to these accounting estimates together with the impact of different assumptions.</p> <p>We have a tiered approach to review and management oversight of accounting estimates. Detailed work is carried out in the finance team. Where there are significant estimates, these are discussed with the s151 officer, who oversees the subsequent work to calculate and disclose outcomes. The Audit committee is briefed on all such matters and the presentation and publication of the financial statements.</p> |

Accounting Estimates - General Enquiries of Management

| Question | Management response |
|--|--|
| <p>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)?</p> | <p>Calculation of provision for NNDR appeals: the methodology for the 2005/2010 list is being applied to the 2017 list Interpretation of agent / principal status around accountable body schemes (Kendal Flood Alleviation ERDF Scheme) and Covid-19 grant schemes.</p> |
| <p>11. Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?</p> | <p>Yes- Accounting estimates are made by members of the finance team with sufficient skill and knowledge. The finance team at SLDC is experienced and there have been no issues in prior year audits surrounding estimates. Accounting treatment used by the Council is in line with IFRS and the Code of Practice.</p> |
| <p>12. How is the Audit Committee provided with assurance that the arrangements for accounting estimates are adequate ?</p> | <p>Professionally qualified finance team, undergo regular training to ensure skills and knowledge are up-to-date. Use of external support where required. Internal and External audit reports: including monitoring of recommendations Receipt of Accounting Policies and Statement of Accounts: opportunity to review and question officers. From April 2021 consideration of General Queries of Management will be reported to Audit Committee.</p> |

Appendix A Accounting Estimates

| Estimate | Method / model used to make the estimate | Controls used to identify estimates | Whether Management have used an expert | Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates | Has there been a change in accounting method in year? |
|-------------------------------|---|---|---|--|---|
| Land and buildings valuations | The Council re-values its assets every four years as part of a rolling programme. Valuations are carried out in accordance with the methodologies and bases for estimation set out in the professional standards of the Royal Institute of Chartered Surveyors ("RICS") Valuation Standards (6th Edition) and guidance provided by CIPFA. Also review for material change either through enhancement or impairment and review of significant assets outside the rolling programme. | Asset valuations provided by LSH for land and buildings, museum collection valuation provided by expert. Asset life estimates provided by LSH or asset owner (for VPE). SLDC staff use own knowledge and experience to review values and asset lives. | Use RICS qualified valuer employed by LSH – the Council's property services contractor. | 2019/20 valuations were reported on the basis of 'material valuation uncertainty' by the Council's valuers. By the 2020/21 valuation date the property markets were deemed to be operating with sufficient volume and relevant evidence on which to base valuation judgements. Accordingly valuations are not reported as being subject to 'material valuation uncertainty' in 2020/21. To mitigate the risk of material error arising from PPE valuations, the Council operates a 4 year rolling programme of asset valuations. In addition, where the professional valuers identify evidence that an asset may need reviewing, this will also be done outside of the main programme. As a matter of course all assets with a value of more than 10% of the total assets value are valued every two years. In addition there is a potential impact of up to £3.765m from the (surplus) or deficit on revaluation of non-current assets, not charged to the revaluation reserve. Although the value of assets on the balance sheet would reduce, this would have no overall impact of the financial viability of the Council. | No |
| Depreciation | Covers all assets with a finite useful life, other than freehold land. Higher value assets such as office buildings and leisure centres are split into components where doing this would have a material impact on the depreciation charged in year. Charge calculated on opening balance sheet | | | The impact of a 10% change in valuation of significant assets would result in £54k of extra depreciation in the CIES, though this is reversed out of the general fund in the MIRS. | 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? |
|---|--|---|---|---|---|
| Investment property valuations | Annual valuation at fair value in existing use. | Asset valuations provided by LSH for land and buildings | Use RICS qualified valuer employed by LSH – the Council's property services contractor. | Based on valuer developing estimates and assumptions consistent about how market participants would price the property. The valuers base their assumptions on observable data as far as possible, but this is not always available. In that case, the valuers use the best information available. These valuations have been impacted by the Covid-19 pandemic in the same way as Property Plant and Equipment above. | No |
| Valuation of defined benefit net pension fund liabilities | Based on discount rates, salary increases, changes in retirement ages, mortality rates and expected returns on pension fund assets. Included within the assets of the pension fund are investments in direct and indirect property totalling £11.1m which is impacted in the same way as Property Plant and Equipment above. | | Use actuary employed by Mercers appointed by Cumbria County Council as pensions administrator | The effects on the net pension liability of changes in individual assumptions can be measured, however, there are statutory overrides in place to ensure that the impact on the Council's usable reserves is limited to the amounts actually payable in year. Note 35 includes sensitivity analysis of the impact of changes in actuarial assumptions on plan assets and liabilities. | No |



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