Annex 2

Deloitte.

City of London Corporation – City Fund

Progress report to the Audit and Risk Management Committee on the audit for the year ended 31 March 2015

the Distinctive audit

14 July 2015

Contents

"I am pleased to present this progress report on the findings from our 2014/15 external audit."

Heather Bygrave, Engagement Lead Partner

A reminder of our Audit Plan and subsequent changes made:

- Materiality: £5.1m (revised from estimate of £4.5m in our audit planning report to reflect higher than assumed gross spend on services).
- Threshold for reporting misstatements: £250k.
- Significant risks over valuation of investment properties, fraud in recognition of grant income and management override of controls.
- A further significant risk in relation to the valuation of the pension liability has been identified in view of the amount of the increase in this account balance compared to prior year.
- We have removed a risk in relation to the Oracle upgrade as in the event this did not involve the transfer of data.
- We have taken a fully substantive audit approach.

The big picture

The Big Picture

Our work is in progress at the time of issue of this report and some key matters have not yet been concluded on. As in previous years, we will provide an oral update at the meeting

Statement of accounts

- The key judgement areas are in relation to the valuation of properties, the valuation of pension liabilities and the estimation of provisions for business rates appeals.
- We also provide comments on the Crossrail commitment. The position is unchanged from that anticipated in our planning report to the Committee, but we comment on additional disclosures and commentary which the City of London Corporation ("the City") has included in the draft financial statements this year.
- During the year the City entered into an agreement for the development and lease of its existing property at 2 Fann Street. We provide a commentary on the accounting treatment for this transaction. There are four further property transactions which have similarities with this and we are discussing the accounting treatment for these with officers. These issues need to be resolved before we are able to conclude on the financial statements.

Audit work on the financial statements

- Valuation of investment properties - We focused on the key assumptions made, and the reasonableness of the valuations arrived at, by the City's valuers. We concluded satisfactorily on their reasonableness.
- Grant income recognition - We focused on the judgements made by officers in determining the basis of recognition for individual grants. Information was outstanding or received too late in respect of grants administered by City Police to enable us to conclude our work in this area prior to the issue of this report.
- We identified a risk in our planning report in relation to the upgrade to the Oracle R12 version. In the event, the process did not involve the transfer of data as the database was not replaced or changed. Our risk assessment work did not identify any other risks around the upgrade. We therefore removed this risk.
- Management override of controls - Auditing standards presume that there is always a risk of management override of controls. We did not identify any areas of concern from our work, but there are a small number of journals where further information is needed.
- We reported in our planning report that the valuation of the pension liability was a key source of estimation uncertainty. In view of the significant increase in this account balance during the year, we have identified the valuation of the pension liability as an additional significant risk. We completed our work and identified a material adjustment as the actuary used asset valuations estimated using data at February which was £19.7m lower than the actual year end position. The impact on the City Fund net pension liability is approximately £9 million and officers have agreed to update the financial statements for this.
- We have not identified any material control deficiencies from our work to date.

Officers have again faced the challenge of finalising the financial statements at the same time as responding to audit queries.

We received the full draft financial statements on 30 June 2015. This is in line with the statutory timetable, but the timing does not enable finalisation of our work in advance of the more demanding committee reporting timetable which the City sets itself.

Our work is therefore in progress, including internal review processes. Whilst we comment on a number of open areas of work through this report, this is not intended to, and does not provide, a comprehensive list.

In particular open issues on provision for business rates appeal refunds, property transactions and recognition of police grant income need to be resolved.

In accordance with our practice in previous years, we will provide an oral update at the meeting on the progress of the audit and any significant issues which have arisen since the issue of this report. Subsequent to the meeting, we will provide an updated version of this report once our procedures are complete for circulation to members.

We will provide a schedule of any misstatements which remain uncorrected in the updated version of this report.

Other work

- We expect to issue an unmodified value for money conclusion.
- We have not yet commenced our work on the City's Whole of Government Accounts return. We will do this once we have received a finalised version of the financial statements.

Significant audit risks

This section explains the nature of significant risks, how these risks have been addressed by our audit work and our conclusions. We also explain related presentational and disclosure matters within the financial statements.

Valuation of investment properties

The valuations arrived at by the City's valuers were reasonable in material respects

Nature of risk

The City has a substantial portfolio of investment properties which are subject to annual revaluation. The carrying value at 31 March 2015 was £1,088m (£130m gain in year). Some of the properties require the application of specialist valuation assumptions. The current and recent economic volatility has affected property values, generally, and the City has recorded significant gains and losses over the last few years.

All properties are valued in accordance with the Royal Institution of Chartered Surveyors Valuation and Appraisal Standards. The portfolio has been substantially valued by one external firm of valuers at 31 March 2015, with a second valuer valuing a further two properties where the principal valuer had declared a conflict of interest.

The key judgement area(s), its impact on the financial statements and our audit challenge

We involve real estate specialists from Deloitte as part of the engagement team to assist us. Our work included:

- assessing the overall performance of the City Fund investment and strategic property portfolios against published data on overall property market movements, for the period from March 2014 to March 2015 and sought and challenged reasons for over- or under-performance against the wider market for individual properties;
- undertaking a desktop analysis to assess a selection of properties, comparing the key assumptions adopted against publicly available benchmarks and information;
- considering the approach and methodology of the valuers, together with the instructions from the City.

We noted that the process followed in preparation of the valuations appears to be reasonable.

The Investment Property Databank ("IPD") index reports changes in capital values of various property types. Reported movements in Central London in the year to 31 March 2015 are summarised in the table below:

Property Type	Change in Capital Value
City Offices	+15.9%
Midtown Offices	+22.8%
West End Offices	+17.4%
City & Midtown Retail	+17.5%
West End Retail	+24.2%

With a like-for-like portfolio movement of +13.2%, the core investment portfolio has increased in value by slightly less than the wider London property market. However, the value of the strategic property estate has increased well ahead of the wider market (+36.7%). The valuer has explained that these assets, which are typically in fringe locations and let off lower rents than the prime City, have seen exceptional growth in this period. This has been caused by significantly increasing rents, as potential City occupiers move to more fringe locations, given rising rental levels in the core City. In addition, as rental growth occurs and other sectors appear well priced, investors have been attracted to such assets in the past year. These assets generally offer the potential for active management, which is attractive in the current market.

We believe the internal and external valuations produced for the City Fund as at 31 March 2015 are a reasonable reflection of their market value. However, going forwards, the City should monitor the valuations of:

- The valuations of the developments in progress (London Wall Place, International House, 100 Cheapside and 12 – 14 New Fetter Lane) are monitored in the coming year, since these valuations are likely to see the greatest degree of value change going forward; and
- The intentions of Ciena to vacate or remain in occupation at 43-51 Worship Street, as this could affect the value of the property going forward.

Work in other areas relating to investment properties is ongoing, in particular our testing of the treatment of transactions accounted for as disposals which we comment on in the other issues section, below.

Valuation of pension liability

We identified this as an audit risk because of the significant increase in the liability

Nature of risk

The pension liability is substantial so that its calculation is sensitive to comparatively small changes in assumptions made about future changes in salaries, price and pensions, mortality and other key variables. Some of these assumptions which draw on market prices and other economic indices can be volatile.

We did not identify pension accounting as an area of significant audit risk in our planning report as there is no impact on the general City Fund reserve from the accounting entries made under IFRS. However, as a result of the significant increase in the account balance, we have subsequently reclassified this risk from normal to significant.

The key judgement area(s), its impact on the financial statements and our audit challenge

We considered the qualifications, relevant expertise and independence of the actuary. We included a specialist from our team of actuaries in our engagement.

The key driver of the increase in the provision is a reduction in the discount rate assumption from 4.4% to 3.3%.

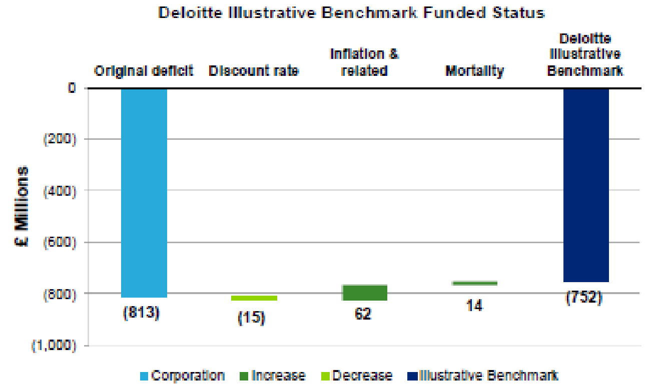
The City's proposed discount rate has been set by reference to the annualised yield at the 18 year point on the Merrill Lynch AA rated corporate bond curve.

This is consistent with the methodology used at last year end. Although the methodology used by the City is based on the respective schemes' durations, it is not our preferred approach which is to take into account future projected cashflows. However, the discount rate could be derived by using an appropriate methodology. The proposed assumption is therefore reasonable. The City's actuaries' sensitivity analysis implies that setting the discount rate assumption to be in line with our illustrative benchmark could increase the assessed liability value by £15m.

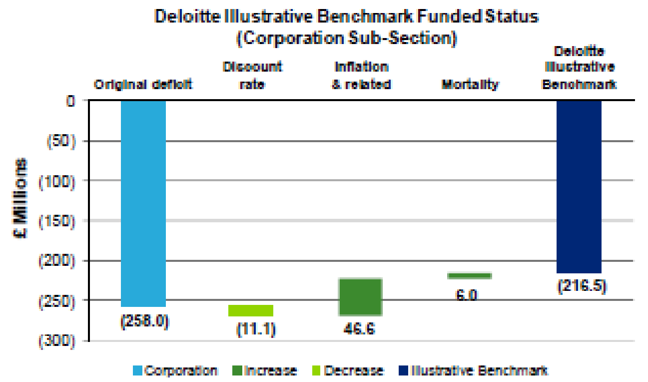
The other main area where there was a difference between the practice adopted by the actuary and our preferred approach is in determining inflation related assumptions. It is common actuarial practice to apply a deduction to the market implied RPI inflation to allow for an inflation risk premium ("IRP"). An IRP makes allowance for the additional premium investors are assumed to pay for protection against inflation and for any other distortions due to such factors as an under supply of index linked gilts. In this case, no deduction has been made to allow for an IRP. This is consistent with the approach at the previous year end, but typical actuarial practice is to make a deduction of around 0.25%. As a whole, the resulting inflation related assumptions are reasonable, albeit relatively prudent due to the absence of an IRP deduction.

When considering the suitability of assumptions it is important to consider the assumptions in aggregate to determine the strength of the set of assumptions as a whole. In particular, the results are very sensitive to the difference between various assumptions. An optimistic proposal to one assumption may be balanced by an offsetting prudent assumption or vice versa. The charts below give an indication of the broad impact on the liability value of setting the main assumptions to be in line with our illustrative benchmark assumptions. This is not intended to imply that the value calculated by the actuary is inappropriate.

Police pension



City of London Pension Scheme



Valuation of pension liability (continued)

We identified this as an audit risk because of the significant increase in the liability

The pension assets are estimated by the actuary based on information provided in February. The value estimated by the actuary for the City of London Pension Scheme as a whole was £19.7m less than the outturn position as shown in the pension scheme accounts in the draft financial statements. As a consequence, the net pension liability in the City Fund accounts is overstated by approximately £9 million. Officers have indicated their intention to correct this in the final version of the financial statements.

Fraud in grant income recognition

We focused on the judgements made by officers in determining the basis of recognition for individual grants. Our work is ongoing, in particular we have not received information to complete the majority of police grants in our sample

Nature of risk

The City received grants and contributions totalling £183m.

Auditing Standards include a presumption that there is a significant risk of fraud in revenue recognition. We have pinpointed this risk to the recognition of grant income. Accounting for grant income can be complex as the timing for recognising income in the accounts will depend on the scheme rules for each grant. Under the Code, income from grants is recognised as soon as all conditions have been met.

We have retained this as a risk in view of the size of this income stream and some of the complexities around recognition of individual grants.

The significant risk in relation to management override, its impact on the financial statements and our audit challenge

We noted that the Corporate Accountancy Unit had sent out instructions to staff involved in the preparation of the accounts highlighting the accounting requirements for grants. Last year we noted that although no errors were identified in the recognition of grant income from sample testing, the City may wish to consider the application of central controls to the accounting for such income given the significant sums involved and the complexity of treatment. The arrangements this year remain the same as last year.

We also carried out extended testing to check that recognition of income in 2014/15 properly reflects any conditions within the grant offer letter and accompanying documentation.

Our work on this risk is in progress. In particular, information was outstanding in respect of grants administered by City Police to enable us to conclude our work in this area prior to the issue of this report.

Management override of controls

We have not identified any issues from our work to date. Testing of some journal selections is outstanding

Nature of risk

Standards on auditing include a presumption of a risk of management override of key controls which cannot be rebutted by the auditor. This recognises that management may be able to override controls that are in place to prevent inaccurate or even fraudulent financial reporting.

The significant risk in relation to management override, its impact on the financial statements and our audit challenge

Our audit work is designed to test management override of controls and key estimates.

We have summarised our findings above on the key estimates around grant income recognition, investment property valuation and the value at which properties were transferred to the City Fund.

Other audit work completed to address the significant risk

Specific areas of work are:

Journals

In testing journals, we analysed the whole population of journals to identify those which had features which could be indicators of possible fraud and to focus our testing on these. The sample we selected included items from the following categories of interest:

- Journals which were backdated more than 60 days
- Journals posted around period end with poor descriptions that impact in a manner that is of interest.
- Journals which include key words of interest
- Largest journal lines
- Journals with a line item whose value is a round sum amount.
- Journals posted on specific non-business days including weekends, bank holidays and user defined dates
- Journals to seldom used accounts

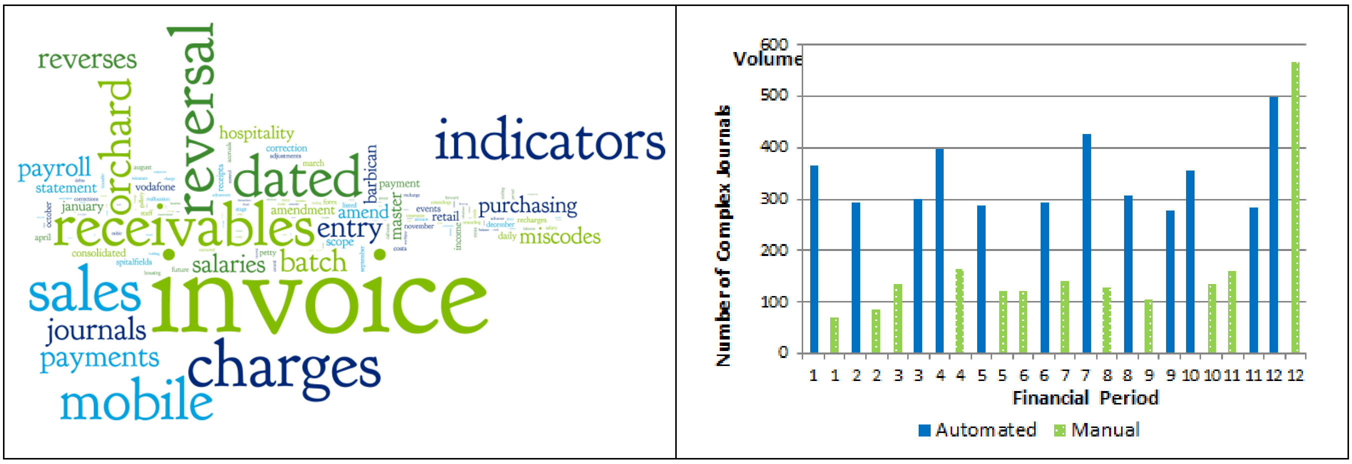
There are a small number of journals where we require further information to complete our work. There are no issues identified to date.

Accounting estimates

In addition to the key estimates discussed above, we have tested the basis for other estimates used in the financial statements and have not identified any evidence of management bias from our work to date. We discuss other areas of significant judgement, which we do not consider give rise to a significant risk of material misstatement, in the next section.

Significant transactions

We did not identify any significant transactions outside the normal course of business or transactions where the business rationale was not clear.



Illustrative output from our Spotlight tool – most common words used in journals and number of complex journals by period for City Fund

Other matters in your financial statements

Other matters in your financial statements

We comment on other key areas of judgement and other matters which do not represent significant audit risks

The Crossrail commitment

- The notes to the financial statements since 2008/9 have disclosed a commitment made by the City to contribute £200 million towards the cost of Crossrail. The wording in the 2015 draft financial statements (which is repeated in the explanatory foreword) is as follows:

  "The City of London Corporation has agreed with Government that £200m will be provided from City Fund towards the costs of constructing Crossrail. The payment of this amount is dependent on the achievement of a number of conditions, primarily the completion of certain works in relation to Crossrail stations. Therefore a liability has not been recognised in the financial statements pending performance of the conditions but will be recognised when it becomes payable. At this stage it is anticipated that the contribution will be made in March 2016. The financing strategy for the contribution is based on the accumulation of annual rental income from specific investment properties and capital receipts from the sale of assets".
- The City has also included a cross reference on the balance sheet to this: *"This is before a £200m commitment towards Crossrail, anticipated to be paid in March 2016 (see explanatory foreword)".*
- During our audit of the 2008/9 financial statements we discussed with officers their assessment of the accounting treatment for this item. We concurred with officers that the agreement with the Government, contained within an exchange of letters between the Corporation and the Secretary of State, is an "executory contract" (contracts under which both parties are still to perform to an equal degree the actions promised by and required of them under the contract). As such it falls outside the scope of International Accounting Standard 37 Provisions, Contingent Liabilities and Contingent Assets (unless onerous).
- As a result, in past financial statements, whilst the transaction has been disclosed as a commitment, a liability has not yet been recognised on the balance sheet pending performance of the undertakings made by the Secretary of State, which include completion of certain works in relation to Crossrail stations.
- The relevant works at 31 March 2015were incomplete at that date and are not expected to be complete until around March 2016. We therefore agree there should be no change to the past treatment in the 2014/15 accounts with disclosure only as a significant revenue commitment.

Other matters in your financial statements (continued)

We comment on other key areas of judgement and other matters which do not represent significant audit risks

Valuation of operational properties

- In our planning report, we identified a significant risk in relation to the valuation of investment properties, but not for operational properties. This is principally because we believe there is more user focus on investment properties as their value and the rental stream they generate our important to an assessment of the financial position and performance of the City Fund. We believe there is less user focus on the value of operational properties as they are generally required for ongoing use in the delivery of services and their valuation is less relevant when properties are held for this purpose. We also consider that the valuations of the City's operational properties are not complex and, due to provisions within local government accounting arrangements, do not impact on the level of revenue and capital resources available to meet future spend.
- Nevertheless, the valuation of operational properties remains key source of estimation uncertainty in the financial statements and we have therefore provided comments here.
- For all categories of operational properties we have evaluated the qualifications and experience of the valuers and decisions taken on which properties will be subject to full or desktop valuations.
- The City continues to perform a full revaluation of Housing Revenue Account dwellings on an annual basis. On a like-for –like basis, the valuation has increased by 13.9%. This is broadly consistent with the average of a basket of residential house prices indices which we used to benchmark the reasonableness of the outcome of the valuation (13.6%).
- We similarly benchmarked the change in value of other operational properties subject to revaluation in the year against published indicators to assess reasonableness. We looked in more detail at the increase in valuation of St Andrews House of £43m (80% uplift) which related not just to market changes, but also changes to the valuation methodology to analyse unsold properties in greater detail by type to enable a closer match to relevant archetypes. As a whole, the valuations of non-dwelling operational properties increased by 7% in comparison to building cost indices which increased by 4.5% (relevant to specialised assets valued at depreciated replacement cost) and 9-17% for properties valued on the basis of market information. We are currently following up on movements which are significantly outside these benchmarks.
- Revaluations for other assets which are carried out on a rolling basis and which were not selected for valuation in 2014/15 totalled £31m. The Code of Practice on Local Authority Accounting allows for valuations to be carried out on a rolling basis but also requires properties to be recorded at their fair value at each balance sheet date in material respects. Taking into account the comparatively small value not subject to formal valuation, the modest general price change over the period and the existing officer processes for bringing forward in the valuation programme any individual properties with unusual factors impacting on their valuation, we conclude that the design of the valuation programme was adequate to meet its objective.

Other matters in your financial statements (continued)

We comment on other key areas of judgement and other matters which do not represent significant audit risks

Accounting treatment for 2 Fann Street and other property transactions in the year

- The property, 2 Fann Street, was previously held in Property, Plant and Equipment as used it was for the delivery of services (YMCA hostel provided in relation to the City's homelessness functions). During 2013/14 the hostel was closed, but continued to be carried in PPE pending a decision on its future.
- In 2014/15, a deal was agreed with a developer for the lease of the property under which the property would be converted into residential units by the developer and, on practical completion of the development, let to the developer on a 150 year lease. £28m is to be paid upfront and annual rent of £1,000. £8m of the consideration was paid before the year end (this is split between £1m on entering the agreement which is refundable if planning permission not obtained and £7m following grant of planning permission. These amounts became non-refundable at that point. The balance of £20m is payable on practical completion of the development. There are also overage provisions.
- The agreement with the developer is terminated if certain conditions are not met, including development notice not being issued within 1 year of grant of planning permission and practical completion not reached within 4 years of the signing of the agreement. In the event of termination, the developer is required to transfer the property back to the City. There is no further payment or repayment of amounts. However, the developer is proceeding with the development and is currently expected to complete well before the long stop date.
- The developer will let individual units on subleases with lease period of 150 years. The City has also signed a deed of surrender that will oblige it to take back the lease 30 months after practical completion. The City will then hold the leases within individual unit holders direct. The lease term of150 years is estimated to be approximate to the remaining useful economic life of the building.
- In the initial version of the financial statements authorised for issue, the property was included in investment properties pending further consideration of its treatment.
- A series of transactions should be considered as linked and accounted for as one transaction when the overall economic effect cannot be understood without reference to the series of transactions as a whole. The agreement with the developer to develop the property and to subsequently lease the property to the developer and then take on the individual subleases with unit holders are linked in this way.
- The consideration of £28m is in respect of the right of the developer (and subsequently the individual leaseholders) to use the asset (i.e. to covert to residential units and subsequently sublet the properties/occupy) therefore forms part of the lease payments (notwithstanding that the formal lease does not commence until practical completion is reached). The developer is proceeding with the development and it is probable that the transaction will run its course. It is therefore appropriate to recognise the assets relating to the lease at this point.
- We have also raised questions on four other property transactions with total proceeds of £101m where the principles are similar. These are currently treated as capital receipts.
- The land and building components of the lease should be analysed separately as to their classification. Leases of land are assessed in the same way as all other leases. Land normally has an indefinite economic life, so it is unlikely that the lease term will be for the major part of the economic life of the asset. Nevertheless, some of the other characteristics of a finance lease may be met, in which case a lease of land may be a finance lease. We are currently working through the lease classifications with officers.
- We do not anticipate being able to conclude positively overall on the financial statements until these issues have been resolved.
- We understand that some of potential accounting treatments being discussed would have an impact on the recognition of resources which was not anticipated at the time of entering into the initial transactions. We recommend, going forwards, an accounting treatment note is prepared at the time of the transaction and in good time for the preparation of the draft financial statements.

Other matters in your financial statements (continued)

We comment on other key areas of judgement and other matters which do not represent significant audit risks

Provision for refunds of business rates granted on appeal

- The accounting and estimation processes for calculating the financial impact of appeals against rateable values requires the exercise of judgement, but the impact on the City is in part mitigated by the operation of floors and ceilings within the calculation of the amount of business rates to be retained locally.
- The volume of open cases means that the City have needed to make a general provision using the “expected value” method, in this case based on the City’s recent historical experience in settling appeals. In particular, the provision has been calculated on the assumption that the appeals will be settled with the same success rate and average percentage financial effect per successful appeal as in 2014/15. The approach is reasonable, but is dependent on the cases settled in 2014/15 being representative of the open cases at 31 March 2015.
- The City’s share of the provision has increased from £35.1m to £56.5m. This is consistent with what we understand to be the trend nationally and is caused by a spike in the number of new appeals caused by ratepayers submitting claims to meet a deadline of 31 March 2015 which represents the closure of the period in which new appeals can be made against the 2010 List. In addition to new appeals received in 2014/15, approximately half the claims which were outstanding at 31 March 2014 also remained outstanding at the current year end. It is possible that the quality of some of these new appeals submitted at the end of 2014/15 to meet the deadline may not as high as those determined during 2014/15. However, there is limited information available to the City to assess this until the Valuation Officer starts to determine these new appeals.
- There is also, more specifically, an enhanced risk this year end that appeals have been duplicated, although in some cases multiple appeals on the same hereditament may be genuine separate appeals which would need to be included in the estimate for the provision for refunds. We have asked officers to consider this risk further as this was not covered in their original assessment.
- The effect on the calculation of the provision of the increase in the value of outstanding appeals at 31 March 2015 compared to 31 March 2014 has been partly offset by a reduction in the assumed value at which appeals are settled from 4.2% to 3.4% between these two year ends. The assumption at each year end is derived directly from experience in the preceding financial year. Officers took the decision last year to restrict the period it looked back in setting the provision to one year as the nature of appeals changes over time as the issues which drive those appeals change. This view is reasonable, but there is nevertheless a risk that the cases determined in the period may not be representative of the appeals which were open at the year end if, for example, the Valuation Officer has not worked evenly across all categories of appeal during 2014/15.
- Officers have further analysed the available data to inform their assessment of this risk. Officers are currently investigating a category of appeal where the rateable value under appeal at 31 March 2015 at £1.1 billion (a third of the total under appeal) is substantially higher than the total amount determined by the Valuation Officer over the last four years of £98 million. Whilst an ongoing legal case which impacts on this category may have driven part of this increase, officers also believe that there is significant duplication of cases within this category. It is also likely that a different settlement rate will be appropriate to that suggested by the historical record.
- Officers have reanalysed and propose to reduce the total provision by £19m (City Fund share approximately £6m). We will conclude once we have tested this new analysis.
- Our testing of payments made after the year end identified instances where the Valuation Officer had determined an appeal before the year end, resulting in the need for the City to make a refund, but where this had not been processed on the City’s business rates system until after the year end. As a result, there was neither a creditor at the year end (as it had not been processed by the year end on the City’s systems) nor allowance for the refund in the appeals provision (as the Valuation Officer did not consider it to be an open appeal and was therefore not within the information provided to the City. We have asked officers to assess the financial value of any similar cases and understand that the impact on the total provision is £6m. of which the City Fund share is approximately £2m.

Value for Money conclusion

Value for money conclusion

We have not identified any significant risks and expect to issue an unqualified conclusion

Work performed

Under the Code of Audit Practice 2010 we are required to include in our audit report a conclusion on whether the City of London Corporation has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources in respect of the City Fund - this conclusion is known as "the VFM conclusion".

Our conclusion is based on the following two reporting criteria:

- **The organisation has proper arrangements in place for securing financial resilience. The focus of this criterion is on whether the organisation has robust systems and processes to manage financial risks and opportunities effectively, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.**
- **The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness. The focus of this criterion is on whether the organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.**

Risk assessment

Our preliminary assessment was that there were no significant risks in relation to our VFM responsibilities which required additional local work to be carried out and we therefore did not identify any risks or additional local work in our audit plan.

We have subsequently carried out a detailed risk assessment which also takes account of the latest refresh of the Medium Term Financial Strategy ("MTFS"), as well as the outturn financial and performance information for 2014/15. The risk assessment has involved consideration of common risk factors identified by the Audit Commission, concluding on whether they represent actual risks for the purpose of our VFM conclusion on the City Fund. We undertook this work through review of relevant documentation, including committee papers and discussion with officers. We also considered whether there were other risks which might be specific to the City Fund. We did this principally through our consideration of what has been reported in the Annual Governance Statement, any concerns reported by regulators and other matters which have come to our attention from our work carried out in relation to our other Code responsibilities.

As anticipated in our audit planning report, a key focus in our risk assessment work was progress on closing the spending gap.

In carrying out our risk assessment of financial resilience, we considered the following key points:

- Following work as part of the service based review programme in 2014, the City forecast a balanced MTFS as part of its annual refresh in respect of its local authority functions. The City carried out a programme of service based reviews during 2014 and 2015 which have been reflected in the balanced MTFS for the local authority functions. The position at the time of setting the 2015/16 Budget was as follows:

Budget/MTFS £m	2015/16	2016/17	2017/18	2018/19
Non Police (surplus)/deficit	(0.2)	(0.9)	(0.2)	(0.5)
Non Police unallocated reserve	(47.1)	(48.0)	(48.2)	(48.7)

- As a result of a positive budget variance in 2014/15, the starting position on the unallocated reserve at 1 April 2015 is £8.6m higher than assumed in the February 2015 MTFS and is therefore not included in the table above, providing further headroom.

Value for money conclusion (continued)

We expect to issue an unmodified value for money conclusion

- The impact of reductions in central government funding for local government has been less marked on the City Fund compared to London Boroughs. As a result, the programme has not required the same level of member choices over priorities or transformational change in the way in which services are delivered or in the infrastructure to support their delivery. Officers assess that the changes are predominantly “managerial” in nature and do to this extent do not give rise to the same level of risk of non delivery.
- The City also has significant uncommitted revenue reserves in the event of unexpected variations in forecast spend - £48.7m forecast at the end of the period covered by the MTFS.
- The position in relation to the City’s policing functions is more difficult. The latest HMIC report on the City Police’s response to budget reductions concludes positively on the work which has been carried out to date, but nevertheless, there is further work still required at that time to balance the spend with resources in the medium term. The position at the time of setting the 2015/16 Budget was as follows:

Budget/MTFS £m	2015/16	2016/17	2017/18	2018/19
Police (surplus)/deficit	1.7	3.9	7.6	NA
Police unallocated reserve	(4.2)	(0.3)	7.2	NA

- Again, as a result of a positive budget variance in 2014/15, the starting position on the police reserve at 1 April 2015 is £3.1m higher than assumed/reflected in the table above, delaying the point at which the police reserve is exhausted.
- The City Police have a savings programme which is aimed to meet this shortfall which will be formally considered by members in September 2015. We examined the savings plan developed during 2014/15 and how this has been subsequently reflected into a revised draft Medium Term Financial Strategy for the City Police.
- The latest plan for City Police, assuming no change to funding and that savings proposals are formally accepted by members means that the earmarked police reserve is positive over the period of the current budget + 2 year forecast, albeit with utilisation of £4.3m of this balance. A number of the current savings proposals are rated as higher or medium risk, albeit there are further proposals which are currently being worked on but not yet incorporated into the draft financial plans.
- The City Police have further work to do to create a sustainable financial and operating plan with spend balanced with resources if it is to continue to operate without cross funding from non-police functions. In reaching our overall conclusion, however, we have considered the financial position and plans of the police and non-police functions taken together and also noted: the positive assessment of HMIC on the City Police’s response to date; their assessment of the scope for additional savings on spend; and the availability of reserves set aside to manage further reductions over the period to 31 March 2018, together with variations against its financial plans in this period.
- The City has a track record of responding to challenges posed by reductions in government funding and, before that, reductions in key sources of rental and investment income and has added to its reserves in successive years through to 2013 and in 2015. In 2014, revenue reserves have drawn on to finance the reinvestment of funds previously held in deposits into property investments in order to achieve higher returns. Excluding this, the underlying trend has been maintained
- The City has also not needed to make significant adverse changes to forecast surplus/deficit position for the non-Police expenditure during the period covered by the preceding period medium term financial strategy in each of the last 3 years.
- The City has also continued its track record of spending within the City Fund revenue budget, recording an underspend of £12.0 million in 2014/15. The City will need to continue to make sure going forwards that it strikes an appropriate balance between prudent budgeting and forecasting which maintain continued financial resilience on the one hand and providing accurate information for decision making purposes on spending plans on the other.

Value for money conclusion (continued)

We expect to issue an unmodified value for money conclusion

	Unallocated reserve £m	Earmarked reserves £m £m	Total £m £m	Change over year £m £m	Underspend £m
2015	56.4	74.9	131.3	+9.3	12.0
2014	43.5	78.5	122.0	-54.2	4.9
2013	70.9	105.3	176.2	+18.5	6.5
2012	63.7	94.0	157.7	+17.6	13.7
2011	52.9	87.2	140.1	+9.9	4.4
2010	48.5	81.7	130.2	+4.4	7.9

- The reserves position at 31 March 2015, together with the surplus the City has budgeted to make in the current financial year, and the ongoing service based review programme, provides some cover in the event of slippage in the savings programme or unexpected charges or drops in income.

Conclusion

We have concluded that there are no significant risks identified which require an additional response. We expect to issue an unmodified value for money conclusion.

Responsibility Statement

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our report is designed to help the Audit and Risk Management Committee and the Chamberlain and Finance Committee discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA 260 to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes:

- Results of our work on key audit judgements;
- Other insights we have identified from our audit.

What we don't report

- As you will be aware, our audit was not designed to identify all matters that may be relevant to the board.
- Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.
- Finally, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our Plan.

The scope of our work

- Our observations are developed in the context of our audit of the financial statements.
- We described the scope of our work in our audit plan and the supplementary "Briefing on audit matters".

We welcome the opportunity to discuss our report with you and receive your feedback.

Deloitte LLP.

Deloitte LLP

Chartered Accountants

St Albans

14 July 2015

This report has been prepared for the members of the City of London Corporation, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

Appendices

Appendix 1: Fraud: responsibilities and representations

Required representations	We have asked the Corporation to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the financial statements may be materially misstated as a result of fraud and that you have disclosed to us all information in relation to fraud or suspected fraud that you are aware of and that affects the entity or group.
Concerns	We have no concerns to report in relation to fraud from the work noted above or our audit procedures.
Audit work performed	In our planning we identified the risk of fraud in management override of controls and fraud in recognition of grant income as key audit risk for your organisation. During course of our audit, we have had discussions with internal audit, management and those charged governance. We discussed knowledge of actual or suspected cases of fraud, the assessment of fraud risk and arrangements for responding to the risk of fraud. There were no material issues raised in relation to fraud and no adjustments were required to our audit plan.

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.

Appendix 2: Independence and fees

We confirm our independence

As part of our obligations under International Standards on Auditing (UK and Ireland), and the standing guidance issued by Public Sector Audit Appointments Limited (previously the Audit Commission), we are required to report to you on the matters listed below:

Independence confirmation	We confirm that we comply with APB Ethical Standards for Auditors and that, in our professional judgement, we are independent and our objectivity is not compromised.
Fees	Details of the fees charged by Deloitte for the period from 1 April 2014 to 31 March 2015 are summarised on the next page.
Non-audit services	Details of fees earned from non audit services in the year ended 31 March 2015 is provided on the next page. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary. We provided an assessment of the impact of services provided or proposed from 1 April 2014 on our independence and relevant safeguards in our planning report. There is one further service in relation to lease advisory work at New Spitalfields which has been agreed since that time. The work is expected to be carried out in 2015/16 and 2016/17. Members received a report prepared by officers at the last meeting. We obtained approval from Public Sector Audit Appointments Limited before agreeing to perform this work. Our assessment of the threats to our independence and safeguards is as follows: Self-interest – estimated non-audit fees are not at a level relative to past audit fees which gives rise to an unacceptable threat to independence. Self review – the services will be performed during 2015/16 and 2016/17 and the results of the service will be reported on after the expected date for the issue of our final audit certificate, expected to be in September 2015. The services are therefore not relevant to our audit of the financial statements or our VFM conclusion. We also note that the leased units form only a small part of the City's investment property portfolio Management – Management are responsible for taking decisions on the basis of the report prepared by the expert. The City Surveyors department are responsible for the management of an investment property portfolio which for the City Fund is in excess of £1 billion and have the experience and expertise to evaluate the report and take decisions. Advocacy – the role of expert witness requires the witness to act independently. The overriding duty of an expert witness is to provide a complete and honest opinion to the court. He must not act as an advocate. Safeguards: Our work on the 2014/15 accounts is subject to an independent engagement quality control review by a member of our professional standards team. The work will be led and carried out by a team which is from a different office and service line. We have concluded that these safeguards are adequate to reduce the residual threat to our independence to an acceptable level. In addition, we expect to carry out to report on returns on teachers' pensions and capital receipts. These returns fall outside the Public Sector Audit Appointment Limited's grants and returns certification regime. Fees for this work have not yet been agreed.

Relationships	There are no other relationships we have with the City, its members and senior officers and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence.

Appendix 2: Independence and fees (continued)

We summarise audit and non audit fees for the year

The professional fees earned or proposed by Deloitte for the period from 1 April 2014 to 31 March 2015 are as follows:

	Current year £000	Prior year £000
Audit of the City Fund	*117	117
Audit related assurance services		
Certification of grants and returns on behalf of the Audit Commission	15	17
Certification of grants outside the regime	8	-
Other non-audit services		
Lease advisory services	20	14
Tax advisory services - Research paper on financial transaction tax	-	18
Total fees	156	169
Audit of the City of London pension scheme	21	21

*In our audit planning report we noted that we had requested approval from the Audit Commission for an additional fee of £1,515 to match the level of fee in the prior year. This has now been received and we have updated the table to include this amount.

The table does not include fees in respect of work we expect to carry out on two returns which fall outside the Public Sector Audit Appointment Limited’s grants and returns certification regime as fees for these have not yet been agreed.

Appendix 3: Draft management representation letter

We set out in draft the representations we request

Deloitte LLP
3 Victoria Square
Victoria Street
St Albans
AL1 3TF

Dear Sirs

This representation letter is provided in connection with your audit of the financial statements of the City of London Corporation (City Fund) for the year ended 31 March 2015 for the purpose of expressing an opinion as to whether the financial statements present fairly the financial position of City of London Corporation (City Fund) at 31 March 2015 and of the results of its operations, other comprehensive income and expenditure and its cash flows for the year then ended in accordance with applicable accounting framework and Accounts and Audit Regulations 2010.

We acknowledge our responsibilities for preparing financial statements for the City of London Corporation (City Fund) ("the local authority") which present fairly and for making accurate representations to you. For the avoidance of doubt, references to the local authority should be taken as applying equally to the City of London Pension Scheme and references to the financial statements of the local authority, includes information in those financial statements dealing with the City of London Pension Scheme.

We confirm, to the best of our knowledge and belief, the following representations.

Financial statements

1. We understand and have fulfilled our responsibilities for the preparation of the financial statements in accordance with the applicable financial reporting framework and the Accounts and Audit Regulations 2003 (as amended) which give a true and fair view.

2. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

3. The measurement processes, including related assumptions and models used to determine accounting estimates in the context of the applicable financial reporting framework are appropriate and have been applied consistently.

4. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of IAS24 "Related party disclosures".

5. All events subsequent to the date of the financial statements and for which the applicable financial reporting framework requires adjustment of or disclosure have been adjusted or disclosed.

6. We confirm that the financial statements have been prepared on the going concern basis. We do not intend to liquidate the Corporation or cease trading as we consider we have realistic alternatives to doing so. We are not aware of any material uncertainties related to events or conditions that may cast significant doubt upon the Corporation's ability to continue as a going concern. We confirm the completeness of the information provided regarding events and conditions relating to going concern at the date of approval of the financial statements, including our plans for future actions.

7. [The effects of uncorrected misstatements are immaterial, both individually and in aggregate, to the financial statements as a whole – to be updated in the letter depending on whether there are any uncorrected misstatements remaining].

Appendix 3: Draft management representation letter (continued)

We set out in draft the representations we request

8. We are not aware of events or changes in circumstances occurring during the period which indicate that the carrying amount of fixed assets may not be recoverable.

9. The Corporation has satisfactory title to all assets.

10. We have reconsidered the remaining useful lives of the fixed assets and confirm that the present rates of depreciation are appropriate to amortise the cost or revalued amount less residual value over the remaining useful lives.

Information provided

11. We have provided you with all relevant information and access.

12. All minutes of member and management meetings during and since the financial year have been made available to you.

13. All transactions have been recorded and are reflected in the financial statements and the underlying accounting records.

14. We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

15. We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.

16. We are not aware of any fraud or suspected fraud that affects the entity and involves:
    (i). management;
    (ii). employees who have significant roles in internal control; or
    (iii). others where the fraud could have a material effect on the financial statements.

17. We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

18. We are not aware of any instances of non-compliance, or suspected non-compliance, with laws, regulations, and contractual agreements whose effects should be considered when preparing financial statements.

19. We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware.

20. No claims in connection with litigation have been or are expected to be received.

21. We have recorded or disclosed, as appropriate, all liabilities, both actual and contingent.

22. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities reflected in the financial statements.

23. We are not aware of any events or changes in circumstances occurring during the period which indicate that the carrying value of fixed assets may not be recoverable.

Appendix 3: Draft management representation letter (continued)

We set out in draft the representations we request

24. We have evaluated whether the restrictions, terms or conditions on grants have been fulfilled with, and deferred income to the extent that conditions have not been fulfilled.

25. We confirm that:

    - all retirement benefits and schemes, including UK, foreign, funded or unfunded, approved or unapproved, contractual or implicit have been identified and properly accounted for;
    - all settlements and curtailments have been identified and properly accounted for;
    - all events which relate to the determination of pension liabilities have been brought to the actuary's attention;
    - the actuarial assumptions underlying the valuation of the scheme liabilities (including the discount rate used) accord with the City's best estimates of the future events that will affect the cost of retirement benefits and are consistent with our knowledge of the business.
    - the actuary's calculations have been based on complete and up to date member data as far as appropriate regarding the adopted methodology; and
    - the amounts included in the financial statements derived from the work of the actuary are appropriate.

We confirm that the above representations are made on the basis of adequate enquiries of management and staff (and where appropriate, inspection of evidence) sufficient to satisfy ourselves that we can properly make each of the above representations to you.

Yours faithfully