ANNEX 2

CITY OF LONDON – CITY FUND

AUDIT FINDINGS REPORT

Audit for the year ended 31 March 2016 - Issued to the Audit and Risk Management Committee - 07 September 2016

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PURPOSE AND USE OF THIS REPORT

We present our updated Audit and Risk Management Committee Report which details the key findings to date arising from the audit for the attention of those charged with governance. It forms a key part of our communication strategy with you, a strategy which is designed to promote effective two way communication throughout the audit process.

We have updated the report and highlighted changes in green compared to the report we issued to the Audit and Risk Management Committee on 18 July 2016.

As auditors we are responsible for performing our audit in accordance with International Standards on Auditing (UK & Ireland) which provide us with a framework which enables us to form and express an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management nor those charged with governance of their responsibilities for the preparation of the financial statements.

The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements and our value for money conclusion. As the purpose of the audit is for us to express an opinion on the financial statements and value for money, you will appreciate that our audit cannot necessarily be expected to disclose all matters that may be of interest to you and, as a result, the matters reported may not be the only ones which exist. As part of our work, we considered internal control relevant to the preparation of the financial statements such that we were able to design appropriate audit procedures. This work was not for the purpose of expressing an opinion on the effectiveness of internal control.

This report has been prepared solely for the use of the Audit and Risk Management Committee. In preparing this report we do not accept or assume responsibility for any other purpose or to any other person.

We would like to thank staff for their co-operation and assistance during the audit to date and throughout the period.

CONTENTS

SUMMARY 4

KEY AUDIT AND ACCOUNTING MATTERS 5

OUTSTANDING MATTERS 18

CONTROL ENVIRONMENT 19

WHOLE GOVERNMENT ACCOUNTS 20

USE OF RESOURCES 21

APPENDICES

I. MATERIALITY 24

II. INDEPENDENCE 25

III. FEES SCHEDULE 27

IV. AUDIT QUALITY 28

SUMMARY

AUDIT SCOPE AND OBJECTIVES

- We have completed our audit procedures in accordance with the planned scope and our objectives have been achieved, subject to the completion of work set out within the outstanding matters section of this report.
- There were no significant changes to our planned audit approach nor were any restrictions placed on our work.
- No additional significant audit risks were identified during the course of our audit procedures subsequent to our audit planning report to you dated February 2016
- Our materiality levels have not required reassessment since our audit planning referred to above.

AUDIT OPINION

- Subject to the successful completion of the work set out within the outstanding matters section of this report we anticipate issuing an unqualified opinion on the financial statements for the year ended 31 March 2016 by 23 September.
- We have no matters to report in relation to the arrangements in place to secure economy, efficiency and effectiveness.

OTHER MATTERS FOR THE ATTENTION OF COMMITTEE

- We will carry out our audit in relation to the whole government accounts return when we have completed our testing on the financial statements. We will provide our audit opinion before the 21 October 2016 deadline.

KEY AUDIT AND ACCOUNTING MATTERS

The key matters that have arisen in the course of our audit are summarised below:

Impacting on Core Financial Statements

i. £312,462 in relation to rental income has been recorded as 2015/16 income but should have been recorded as 2016/17 income.

ii. Cash & bank and creditors understated by £600,327 due to unrecorded rent deposit received directly via an internet payment into a newly created bank account.

iii. Barbican Estate asset valuation overstated by £4.56 million due to incorrect rents used in valuation.

iv. No.1 Alie Street investment land value understated by £6.2 million due to incorrect accounting of the lease premium received for this asset.

v. The actuary double counted the computation lump sum resulting in a net increase of £1.8m to police pension liabilities.

vi. The treatment of the Museum of London finance lease principal agreed with the previous auditors is inconsistent with how other finance leases have been accounted for.

Impacting on Disclosure Notes Only

vii. A number of issues in relation to the operating and finance lease disclosures.

viii. Some of the Related Party Transactions notes require adjustment to allow for accruals.

ix. We have identified a small number of changes to other disclosures, particularly in relation to compulsory redundancies, financial instruments and capital commitments.

Management has confirmed that the accounts will be amended to correct all of the above. Please see the key audit and accounting matters section for details of the items identified and the adjustments that will be made to correct these.

We have also suggested that management consider including a post balance sheet event disclosure to highlight the potential impact of Brexit. Management has concluded that it is still too early to report any potential impact and if disclosures were included this would require significant amounts of work for little added value. The FRC has however recommended that financial statements should include a non-adjusting subsequent event note where there has been a significant change in balance sheet items, such as pension fund liabilities, since the year end.

KEY AUDIT AND ACCOUNTING MATTERS

SIGNIFICANT AUDIT RISKS

We reported our risk assessment, which brought to your attention areas that require additional or special audit consideration and are considered significant audit risks, in the 2015/16 audit planning report dated February 2016. These significant risks have been highlighted in red and findings have been reported in the following table.

We have since undertaken a more detailed assessment of risk following the completion of our review of the authority's internal control environment and draft financial statements, and we have not identified any additional significant risks.

NATURE OF RISK	RELATED CONTROLS / RESPONSE TO RISK	HOW THE RISK WAS ADDRESSED BY OUR AUDIT	CONCLUSION AND RECOMMENDATION
MANAGEMENT OVERRIDE OF CONTROLS	Auditing standards presume that a risk of management override of controls is present in all entities. By its nature, there are no controls in place to mitigate the risk of management override	We respond to this risk by testing the appropriateness of accounting journals and other adjustments to the financial statements, reviewing accounting estimates for possible bias and obtaining an understanding of the business rationale of significant transactions that appear to be unusual.	Our audit work in relation to journals and estimates is in progress (see below for more detail on estimates). Work to date has not identified any significant issues. We will update the Audit and Risk Management Committee at the meeting on 13 September with the result of our testing.
REVENUE RECOGNITION	Auditing standards presume there is a risk of fraud in relation to revenue recognition.	We have carried out audit procedures to gain an understanding of the authority's internal control environment for significant income streams, including how this operates to prevent loss of income and ensure that income is recognised in the correct accounting period.	We have documented our understanding and key controls in respect of the City Fund's internal control environment for significant income streams and no significant weaknesses were identified.
	In particular, we consider there to be a significant risk in respect of the existence (recognition) and accuracy of revenue and capital grants that are subject to performance and / or conditions before these may be recognised as revenue in the comprehensive income and expenditure statement (CIES). (Continued)	We have tested a sample of grants subject to performance and / or conditions to confirm that conditions of the grant have been met before the income is recognised in the CIES.	We have not identified any issues as part of our revenue grant income testing.

KEY AUDIT AND ACCOUNTING MATTERS
Continued

NATURE OF RISK	RELATED CONTROLS / RESPONSE TO RISK	HOW THE RISK WAS ADDRESSED BY OUR AUDIT	CONCLUSION AND RECOMMENDATION
REVENUE RECOGNITION (continued)	We also consider there to be a significant risk in relation to the completeness and existence of fees and charges and property rental income recorded in the CIES.	We have tested a sample of fees and charges and property rental income to ensure income has been recorded in the correct period and that all income that should have been recorded has been recorded.	Testing of fees and charges and property rental income identified one error amounting to £312,462 in relation to rental income that has been recorded as 2015/16 income but which should have been recorded as 2016/17 income. Management has confirmed that this will be adjusted in the amended version of the financial statements.

KEY AUDIT AND ACCOUNTING MATTERS
Continued

OTHER AUDIT RISKS AND ACCOUNTING ISSUES

We report below our findings of the work designed to address all other risks identified in our 2015/16 audit planning report and any other relevant audit and accounting issues identified as a result of our audit: **Normal risk** **Other issue**

NATURE OF RISK	WORK PERFORMED AND FINDINGS	CONCLUSION
CROSSRAIL COMMITMENT	The City Fund has committed to contribute £200 million towards the costs of constructing Crossrail. The payment is dependent on achievement of a number of conditions, primarily completion of certain works in relation to Crossrail stations. Management has reported that the commitment conditions are crystallised only upon completion of these works and continue to report this as a commitment rather than a liability in the financial statements. The original project plan had assumed that the required works would be completed by March 2016, but there appears to be slippage with completion forecast in March 2017.	We have reviewed the progress of the Crossrail works against the agreement required to crystallise the payment and are satisfied that this remains a commitment rather than a liability at 31 March 2016. There has not been any recent formal correspondence with Transport for London (TfL) and no confirmation has been received to suggest that commitment conditions have crystallised. Management has stated that discussions with TfL indicate a forecast completion date of March 2017.
LEASE PREMIUMS	The City Fund is party to a significant number of lease arrangements as lessor. The premiums and rents are apportioned between the land element, which will ordinarily be an operating lease recognised as revenue, and the building element which is likely to be a finance lease and recorded as a capital disposal. The element of the premium relating to the land is treated as deferred income and released to revenue over the term of the lease. We have met with management and the City Surveyors to discuss the process applied for apportioning the significant lease premiums received in 2015/16 between land and buildings.	We are satisfied with land and building apportionments for leases and recognition of the associated lease premium between deferred income and capital receipts. Our testing of the accounting treatment for the lease premium received in 2015/16 in relation to No.1 Alie Street investment land has identified that £6.2 million of the total lease premium received (£16.5 million), had not be added to the carrying value of the asset. This has resulted in an understatements to investment properties disclosed in the balance sheet and to the gain on revaluation of investment properties as part of the surplus on the provision of services in the comprehensive income and expenditure statement by £6.2 million. Management has confirmed that this will be adjusted in the amended version of the financial statements. The adjustment does not impact on the City Fund unallocated reserve because asset revaluations are statutory adjustments reversed to the capital adjustment account (unusable reserve).
	As part of this meeting, we agreed that management would restate the value of the Bernard Morgan House asset held for sale as at 31 March 2015 (£7.2 million) from assets held for sale to surplus assets as a lease was issued rather than a sale/disposal. The value of the asset would then be revalued to £30.4 million to reflect the lease premium received and then this would be transferred to investment properties within 2015/16.	The restatement of Bernard Morgan House has been correctly adjusted in the draft accounts.

KEY AUDIT AND ACCOUNTING MATTERS
Continued

NATURE OF RISK	WORK PERFORMED AND FINDINGS	CONCLUSION
CONSIDERATION OF RELATED PARTY TRANSACTIONS	We consider if the disclosures in the financial statements concerning related party transactions are complete and adequate and in line with the requirements of the accounting standards. Our audit work identified that some related party transaction notes require adjustment for accruals.	Management has confirmed that the related party transactions disclosure amounts will be amended.
FINANCE AND OPERATING LEASES - 21 GARLICK HILL	In order to verify the completeness of leases disclosed in the financial statements we reviewed evidence such as non current asset valuation certificates to determine if all significant leases had been identified and disclosed. Our audit work identified that one investment property, 21 Garlick Hill, had been leased to the City on a long term basis a number of years ago but had not been included in the disclosures as finance lease (City as a lessee), but had rather been included as an operating lease (City as a lessee).	Management has confirmed that the finance and operating lease disclosures will be adjusted in the amended version of the financial statements as follows: • Reduce minimum lease payments for operating leases (City as a lessee) by £6.27 million • Increase the carrying amount of investment properties for finance leases (City as a lessee) by £15.7 million in the current year and £11.75 million as a prior year comparative. These corrections do not impact on the surplus on the provision of services for the year.
OPERATING LEASES - CITY AS A LESSOR DISCLOSURE	This disclosure estimates the total rents receivable over the lives of the various operating leases. We reviewed the disclosure to ensure it complied with requirements set out in the CIPFA code and the following was identified: • Incorrect rent amount used when calculating minimum lease payments in relation to the No.1 Alie Street lease for the new lease arrangement. Impact reduction of operating lease payments by £15.3 million over the life of the lease. • Incorrect rent amount used when calculating minimum lease payments in relation to the 20 St. Dunston's Hill. • Incorrect lease term used to calculate minimum lease payments in relation to the 21 Garlick Hill lease where City sublets to outside parties • Long term lease premiums for deferred income should have been included and spread over the length of the leases.	The overall impact of the adjustments will be to increase estimated future rents receivable from £2.9 billion to £3.1 billion in the 2015/16 disclosure. This takes account of the following amendments that management has confirmed will be included in the final version of the financial statements. • No.1 Alie Street - minimum lease payments reduced by £15.3 million • 20 St Dunston's Hill- minimum lease payments increased by £9.5 million • 21 Garlick Hill - minimum lease payments increased by £0.8 million • Lease premium deferred income - future minimum lease payments increased by £152.5 million in the disclosure for 31 March 2016 and reduced by £28 million when calculating the comparator. These corrections impact operating lease disclosures only and there is no impact on the surplus on the provision of services for the year.

KEY AUDIT AND ACCOUNTING MATTERS
Continued

NATURE OF RISK	WORK PERFORMED AND FINDINGS	CONCLUSION
MUSEUM OF LONDON FINANCE LEASE	The City Fund leases out the Museum of London (MoL) on a long term operating lease basis meaning the residual value of the land is accounted for as investment land in the accounts. A number of years ago the City Fund granted a loan of £18.1 million to the MoL in order for internal capital works to be carried out on the building and accounted for this as a loan in the accounts. In 2008/09 it was concluded in conjunction with the then auditor that it would be more appropriate to account for the transaction as a finance lease (City as a lessor) rather than a loan therefore the accounts were changed to reflect this. On the basis that the amount of annual principal receivable is relatively immaterial it was agreed with the then auditor that the principal could continue to be accounted for as income to the City Fund unallocated reserve rather than be treated as a capital receipt. However, to be consistent with the treatment of other finance leases, the accounting would need to change. This will require reductions to the capital adjustment account and to the City Fund unallocated reserve and increases to the deferred capital receipts reserve and to the capital receipts reserve.	Management has confirmed this will be adjusted in the amended version of the financial statements as follows: • Transfer £8.5 million from the opening balance (01/04/15) of capital adjustment account to restate the opening deferred capital receipts reserve balance as this is total principal outstanding • Transfer £3.6 million from the opening balance of the unallocated city fund reserve to restate the capital receipts reserve as this is the amount of principal recognised since accounting for the transaction as a finance lease • Transfer £0.6 million from the City Fund unallocated reserve to the capital receipts reserve as at 31/03/16 as this is the amount of principal received in 2015/16.
BARBICAN ESTATE ASSET VALUATION	Our review of the valuation in relation to Barbican Estate residential properties found that the rents used to inform the valuations were incorrect and as a result valuations for these properties are overstated by £4.56 million as is the revaluation reserve.	Management has confirmed the error will be adjusted in the amended version of the financial statements by reducing the value of the asset and the revaluation reserve by £4.56 million.

KEY AUDIT AND ACCOUNTING MATTERS
Continued

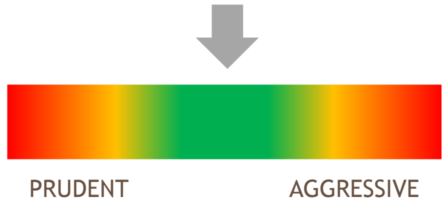
NATURE OF RISK	WORK PERFORMED AND FINDINGS	CONCLUSION
POLICE PENSIONS	The actuary report used to prepare the financial statements double counted the computation lump sums of £2.41 million. The actuary has since provided revised calculations (August 2016) to correct this error.	Management has confirmed this will be corrected in the amended version of the financial statements based on the revised actuary report by reducing benefits paid by £2.4 million and increasing actuarial gains arising from financial assumptions by £0.6 million. The net impact increases pension liabilities by £1.8 million.
RENT DEPOSIT RECEIVED	Our review of the general ledger cash and bank figures has identified an amount of £600,327 rent deposit received in 2015 directly into a new bank account via an internet payment but which had not been included in the cash and bank figures in the accounts.	Management has confirmed this will be corrected in the amended financial statements by increasing cash and cash equivalents and rent deposit creditors by £600,327.
NARRATIVE REPORTING	The Corporation City Fund will be required to produce a 'Narrative Report' replacing the Explanatory Foreword in the financial statements.	We are satisfied that the narrative report meets the new requirements of the CIPFA Code and that financial information is consistent with the financial statements.

KEY AUDIT AND ACCOUNTING MATTERS
Continued

ACCOUNTING ESTIMATES

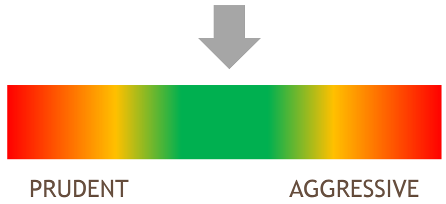
Our views on significant estimates, including any valuations of material assets and liabilities, arrived at the preparation of your financial statements are set out below:

ESTIMATES	AUDIT FINDINGS AND CONCLUSIONS
INVESTMENT PROPERTY VALUATIONS The Code has introduced a change in the basis of valuation of investment properties (IFRS 13), from a market value to a 'highest and best use' valuation. There is a possibility that valuations may be significantly different in certain circumstances particularly where an investment property could be developed for use with alternative consents, such as residential conversion, or where a current lease term is coming to an end and the property could be developed to enhance rental amounts. The Council will instruct JLL to carry out the annual valuation of the City Fund investment property portfolio having regard to the possibility of significant change in valuations under the highest and best use approach. This is not considered to be a change in accounting policy but a change in estimation technique that should be applied prospectively from 1 April 2015. Due to the significant carrying value of investment properties and inherent uncertainty that this new valuation basis could introduce, there is a risk that investment properties may not be appropriately valued as at 01 April 2015 and 31 March 2016.	Our meeting with management and JLL in February 2016 suggested that investment property valuations were unlikely to move significantly as a result of IFRS 13 because the majority of properties were already valued at 'highest and best use' and that there were sufficient observable inputs to support the assumptions used in valuing the properties. Whilst the City Fund's capital value of investment properties has increased by £180 million this mainly relates to a general increase in the market (using the IPD capital index for City office space). There were however several outliers where the market value had significantly increased/decreased due to changes in rental amounts, change in property use and receipt of lease premiums. After discussing the valuation methodology with the valuer, we are satisfied that the observable inputs used to value the assets have been disclosed as 'level 2' in the financial statements. We note that the European Public Real Estate Association (EPRA), a leading trade association, has suggested that in the majority of cases investments property valuations are likely to be level 3 valuations due to the extent that unobservable inputs or individual assumptions for each property. We will keep this under review as generally accepted practice develops.



KEY AUDIT AND ACCOUNTING MATTERS
Continued

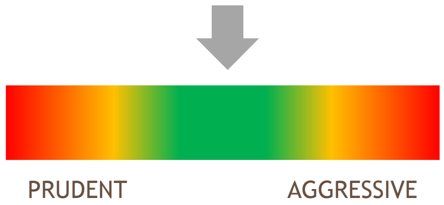
ESTIMATES	AUDIT FINDINGS AND CONCLUSIONS
PROPERTY, PLANT & EQUIPMENT VALUATIONS Local authorities are required to ensure that the value of property, plant and equipment (PPE) is not materially different to the current value (or fair value for surplus assets) at the balance sheet date. The fair value for housing dwellings, land and buildings included in PPE is a management estimate based on existing use values or depreciated replacement cost (DRC). Management use external valuation data to assess whether there has been a material change in the value of classes of assets and periodically (minimum of every five years) employs an external expert (valuer) to undertake a full valuation. The indices available to management to assess valuation changes are produced independently and are based on observable data (asset sales and building contract prices). The valuation expert is independent of management and will use its sector knowledge of local sales to estimate the fair values and remaining useful economic lives of assets. We consider there to be a risk over the valuation of housing dwellings, land and buildings where valuations are based on assumptions or where updated valuations have not been provided for a class of asset at year-end.	As at 31 March 2016 PPE had increased by approximately £81.9 million due to revaluations (the majority being attributable to council dwellings). We reviewed the valuations provided and the valuation methodology applied, and confirmed that the basis of valuation for assets valued in year is appropriate based on Code requirements. We compared the valuations to expected movements using available market information and concluded that the movements are within expectations. We note that the useful economic life for dwellings has been set at 125 years based on the usual term for leases granted. This is significantly longer than used by other local authorities and we are currently discussing with management and the valuers whether this is consistent with the RICS red code guidance. The additional depreciation that may result from applying asset lives of between 60 to 80 years (commonly used) would not be material.



KEY AUDIT AND ACCOUNTING MATTERS

Continued

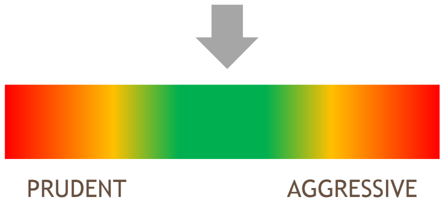
ESTIMATES	AUDIT FINDINGS AND CONCLUSIONS
PENSION LIABILITY ASSUMPTIONS The net pension liability relates to the Police pension fund and City Fund's share of the City of London Corporation pension fund. Actuarial estimates are calculated by an independent firm of actuaries with specialist knowledge and experience. The estimates are based on the most up to date membership data held by the pension fund and have regard to local factors such as mortality rates and expected pay rises along with other assumptions around inflation when calculating the liability.	As at 31 March 2016 net pension liabilities disclosed in the Balance Sheet decreased by £45.4 million compared to the balance at 31 March 2015. It should be noted that these retirement benefits (liabilities) will not actually be payable until employees retire but because the City has a commitment to make the payments (for those benefits) there is a requirement to disclose the information in the accounts at the time employees earn their future entitlement. The last formal valuation of both funds was carried out as at 31 March 2013. In order to assess the value of liabilities as at 31 March 2016 the actuary has rolled forward the value of the liabilities calculated at the latest formal valuation, allowing for up to date financial assumptions. The key changes to the financial assumptions relate to: City of London Corporation: • Reduction in the pension increase rate from 2.8% to 2.3% • Reduction in the salary increase rate from 4.3% to 3.8% • Reduction in the discount rate from 4.4% to 3.6% City Police: • Reduction in the pension increase rate from 2.4% to 2.3% • Reduction in the salary increase rate from 4.2% to 4.1% • Increase in the discount rate from 3.3% to 3.6% These changes have resulted in the significant decrease in the present value of the scheme liabilities at 31 March 2016. We have compared the assumptions used by the actuary to calculate the present value of future pension liabilities with the expected ranges provided by the independent consulting actuary. We are satisfied that the assumptions used are not unreasonable or outside of the expected ranges. Please refer to the findings table above for details of the error identified in relation to police pension computation lump sums.



KEY AUDIT AND ACCOUNTING MATTERS

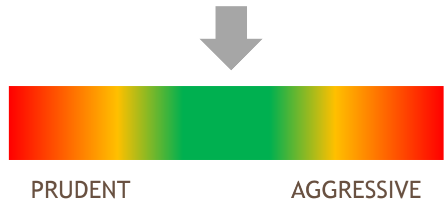
Continued

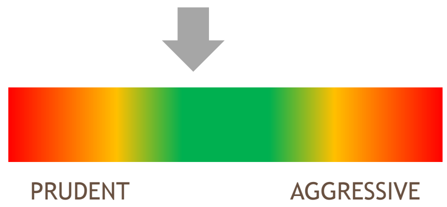
ESTIMATES	AUDIT FINDINGS AND CONCLUSIONS
NON DOMESTIC RATES APPEALS PROVISION Billing authorities are required to estimate the value of potential refund of business rates arising from rate appeals, including backdated appeals. The Valuation Office Agency (VOA) provides information regarding the appeals currently being assessed and settled. Management use this information to calculate a success rate for specific business types for settled appeals, and applies an appropriate rate to each type of business appeal still outstanding at year end. We consider there to be a risk in relation to the estimation of the provision due to potential incomplete data and assumptions used in calculating the likely success rate of appeals. We are aware that some NHS organisations are also appealing their business rate charge and are seeking to obtain charitable status to claim mandatory rate relief.	We have reviewed the current list of appeals provided by the VOA and how this information is used to calculate a success rate for each category of appeal. No issues have been identified. We have tested the accuracy of the information used to calculate the success rate, for example, settled appeals and no issues have been identified. We are not aware of any appeals made by NHS organisations.



KEY AUDIT AND ACCOUNTING MATTERS
Continued

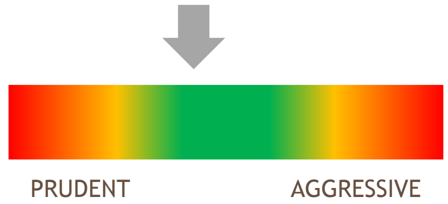
ESTIMATES	AUDIT FINDINGS AND CONCLUSIONS
ALLOWANCE FOR NON-COLLECTION OF RECEIVABLES The City Fund includes a material amount in respect of provision for non-collection of NDR, rents and sundry debt arrears. The provision is based on management assumptions in relation to the collection of the debt. There is a risk that the provisions may not accurately reflect collection rates based on age or debt recovery rates. (continued)	**Non-domestic rate arrears and cost provision** The City Fund's share of debts and provision at the 31 March 2016 was £6.8 million and £3.2 million respectively. The majority of the provision has been calculated using the best information available at the year-end, for example, current collection rates. Around £0.410 million of the provision has been calculated using CIPFA guidelines which are not considered to be up-to-date and may not accurately reflect the aging profile or current collection of debt within the City. Management has explained that costs are likely to outweigh the benefits of collating current collection rates for these debts. We are satisfied that the provision is not materially misstated. **Rent arrears and cost provision** Arrears and provision as at 31 March 2016 were £13.8 million and £1 million respectively. The majority of arrears relate to current tenants and the management surveyor reviews all individual arrears over £15,000 to determine the likely rent to be recovered. The provision relating to approximately £2 million of rent arrears (relating to rent attached to Barbican property and HRA), appears to be based on a standard percentage (3-6 mths 25%, 6-12mth 50% and >1year 100%). The standard percentages do not appear to correlate to the aging profile of debt and corresponding collection rates. Given that the total value of debt is immaterial the provision is not materially misstated. However, we would recommend that current assumptions around standard percentages are regularly reviewed to ensure that any potential material misstatements do not arise.





KEY AUDIT AND ACCOUNTING MATTERS
Continued

ESTIMATES	AUDIT FINDINGS AND CONCLUSIONS
ALLOWANCE FOR NON-COLLECTION OF RECEIVABLES	**Sundry debt arrears and cost provision** Arrears and provision as at 31 March 2016 were £9.4 million and £2.1 million respectively. Barbican centre • 3-5 month arrears (£0.443 million) are reviewed on a case-by case basis and provided for based on historical collection of similar debt • All arrears over 6 months (£0.367 million) are fully provided for however this does not appear to be based on current collection history. Police • Arrears totalling £1.4 million are calculated using management percentages of 0%, 5%, 25%, 50%, and 100% at <3mths, 3-6mths, 6-12mths, 12-24mths, 24+mths. However, no workings to support these assumptions have been provided. Given that the total value of debt is immaterial the provision is not materially misstated. However, we would recommend that current assumptions around standard percentages are regularly reviewed to ensure that any potential material misstatements do not arise.



KEY AUDIT AND ACCOUNTING MATTERS
Continued

FINANCIAL STATEMENT DISCLOSURES

Our views on the sufficiency and content of your financial statements' disclosures are set out below:

DISCLOSURE AREA	AUDIT FINDINGS AND CONCLUSIONS
POST BALANCE SHEET EVENTS - BREXIT	In light of the referendum vote for the UK to leave the EU and the consequential uncertainties in the political and economic environment, the Financial Reporting Council (FRC) has recommended that financial statements should include a non-adjusting subsequent event note where there has been a significant change in balance sheet items, such as pension fund liabilities, since the year end. We have suggested that the Council should consider disclosing a post balance sheet event to recognise this issue and the consequential potential impact on the pension fund liabilities arising on lower bond yields and investment property valuations. Management has informed us that the disclosure will not be included in the accounts because the view of the City is that it is still too early to assess whether there will be any medium/long term impact, which is the basis on which asset allocation and wider investment strategy decisions are made. Also, investment values change from day to day due to any number of factors of which Brexit is only one. Therefore, management believe that the disclosure would require significant amounts of work for little value added.
OTHER DISCLOSURES	We have identified a small number of changes to other disclosures, particularly in relation to compulsory redundancies, financial instruments and capital commitments. Management will amend the disclosures in the final version of the financial statements.

OUTSTANDING MATTERS

We have substantially completed our audit work in respect of the risk areas identified for financial statements for the year ended 31 March 2016, and anticipate issuing an unqualified opinion on the financial statements if no significant issues are identified in the work that remains to be completed.

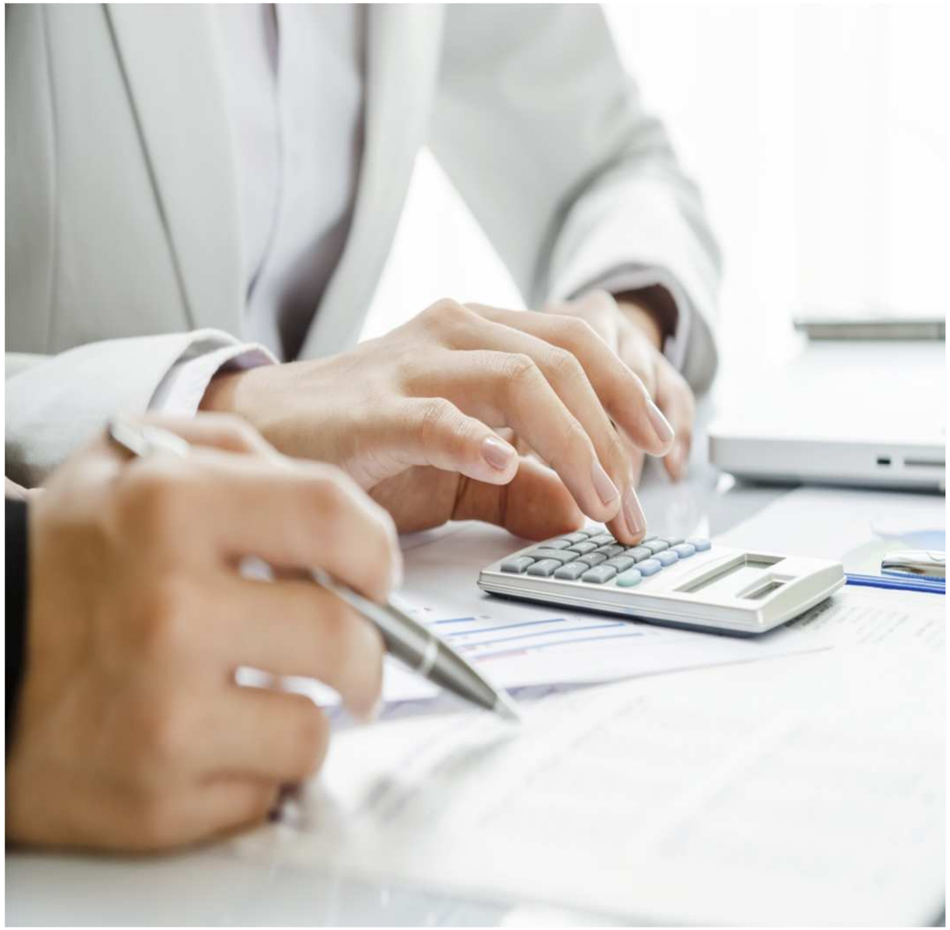
The following matters are outstanding at the date of this report. We will provide a verbal update on these matters to the Audit and Risk Management Committee as part of September 2016 meeting:

1 Completion of work in relation to:
- Completion of the review of journals
- Review of the annual governance statement.

2 Review and agreement of the final WGA data collection tool against the final set of financial statements.

3 Subsequent events review.

4 Management representation letter to be approved and signed.



CONTROL ENVIRONMENT
Significant deficiencies

We are required to report to you, in writing, significant deficiencies in internal control that we have identified during the audit. These matters are limited to those which we have concluded are of sufficient importance to merit being reported to you.

As the purpose of the audit is for us to express an opinion on the authority's financial statements, you will appreciate that our audit cannot necessarily be expected to disclose all matters that may be of interest to you and, as a result, the matters reported may not be the only ones which exist. As part of our work, we considered internal control relevant to the preparation of the financial statements such that we were able to design appropriate audit procedures. This work was not for the purpose of expressing an opinion on the effectiveness of internal control.

We have not identified any significant deficiencies in internal control.

WHOLE OF GOVERNMENT ACCOUNTS

We comment below on other reporting required:

MATTER	COMMENT
For Whole of Government Account (WGA) component bodies that are over the prescribed threshold of £350 million in any of: assets (excluding property, plant and equipment); liabilities (excluding pension liabilities); income or expenditure we are required to perform tests with regard to the Data Collection Tool (DCT) return prepared by the authority for use by the Department of Communities and Local Government for the consolidation of the local government accounts, and by HM Treasury at Whole of Government Accounts level. This work requires checking the consistency of the DCT return with the audited financial statements, and reviewing the consistency of income and expenditure transactions and receivables and payable balances with other government bodies.	HM Treasury's Whole of Government Accounts team issued a newsletter at the end of June to explain the delay in issuing the DCT which was released on Monday 4 July. This means that local authorities' deadline to submit the unaudited DCT to HM Treasury has been extended to 12 August and similarly our deadline to issue our audit opinion on the DCT has been extended to 21 October 2016. We will carry out our audit on the DCT when we have completed our testing on the financial statements. We will provide our audit opinion on the DCT before the 21 October 2016 deadline.

USE OF RESOURCES

Key informed decisions, deployed resources and sustainable outcomes

We are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources (value for money). This is based on the following reporting criterion:

- **In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.**

There are three sub criteria that we consider as part of our overall risk assessment:

- Informed decision making
- Sustainable resource deployment
- Working with partners and other third parties

We reported our risk assessment, which included use of resources significant risks, in the 2015/16 Audit Plan issued in February 2016. We have since undertaken a more detailed assessment of risk following our completion of the interim review of financial controls and review of the draft financial statements, and we have not included any additional significant risks.

We report below our findings of the work designed to address these significant risks and any other relevant use of resources work undertaken.

RISK	WORK PERFORMED	AUDIT ISSUES AND IMPACT ON CONCLUSION
FINANCIAL SUSTAINABILITY (POLICE)	We have reviewed the financial performance of City Police to date and its financial sustainability through review of the medium term financial and strategic plans. As at 31 March 2016 City Police's net expenditure (to be met from government grants, local taxation and transfers to/from reserves), was £67.4 million against a budget of £66 million. The overspend of £1.4 million was met from a transfer from the Police reserve. The update to the Medium Term Financial Strategy (MTFS) to 2018/19 has forecast current budget gaps for City Police in 2017/18 (£2.9 million) and 2018/19 (£4.8 million) which includes current earmarked reserves being exhausted during 2018. Management are currently reviewing the financial strategy to balance the budget over the medium term. The strategy includes maximising opportunities to increase income, exploring potential additional funding streams and further efficiencies and controls on expenditure.	It is essential that City Police ensure that cost models supporting service delivery are accurate and up-to-date in order to clearly represent resources required in the medium term. The current MTFS requires significant savings that are currently not supported by robust plans. City of London Corporation, as a whole organisation, are in a position to fund current forecast deficits in respect of City Police and on that basis we have concluded that City Police remain financially sustainable over the period of the MTFS.

USE OF RESOURCES
Continued

RISK	WORK PERFORMED	AUDIT ISSUES AND IMPACT ON CONCLUSION
FINANCIAL SUSTAINABILITY (CITY FUND)	We have reviewed the financial performance of the City Fund to date and its financial sustainability through review of the medium term financial and strategic plans. There was a net surplus for the year of £0.8m which compared to a budget deficit of £14.5m. This was mainly due to slippage/re-phasing of major revenue repairs, maintenance, improvement projects, increased interest from interest earnings and central contingencies and provision not being required, as well as increased rent income from City Fund Property Investment Estate including a backdated rent review together with reduced operational costs. As at 31 March 2016 usable reserves amounted to £258.2 million and, of this, £200 million is committed to the Crossrail capital project and also includes sums earmarked for purposes such as Highways, HRA and the Police. In our audit plan we reported that the City Fund's medium term financial forecast (MTFF) was currently indicating a surplus position over the next four years, including a surplus of £5.9 million in 2016/17 reducing to £1 million by 2019/20. The MTFF projections have been based on conservative income growth from business rates, council tax, rental income and other income streams as well as budgeting for increased expenditure in relation to pay rises, heightened security measures, delayed cyclical repairs and provisions for service transformation. The MTFF was updated in June and indicated an improved position with annual surpluses of £5m-£6m across the forecast period. However, these surpluses are likely to be reduced due to the recent decrease in interest rates and there may be other potential impacts arising from Brexit. Nevertheless, City Fund finances appear to be relatively robust over the medium term.	There are healthy levels of reserves available to support City Fund's services in the medium term therefore we are satisfied that there are appropriate arrangements in place to continue to remain financially sustainable over the period of the MTFS.

APPENDICES

APPENDIX I: MATERIALITY

MATERIALITY - FINAL AND PLANNING

	FINAL	PLANNING
Materiality	£5,300,000	£5,300,000
Clearly trivial threshold	£100,000	£100,000

Planning materiality for the authority has been based on 1.5% of the prior year gross expenditure. The clearly trivial amount is based on 2% of the materiality level.
We had no reason to revise our final materiality level.

APPENDIX II: INDEPENDENCE

INDEPENDENCE - ENGAGEMENT TEAM ROTATION		
SENIOR TEAM MEMBERS	NUMBER OF YEARS INVOLVED	ROTATION TO TAKE PLACE IN YEAR ENDED
LEIGH LLOYD-THOMAS – Audit engagement partner	1st year	31 March 2021
Engagement quality control reviewer	1st year	31 March 2021
KERRY BARNES – Audit manager	1st year	31 March 2026

APPENDIX II: INDEPENDENCE
Continued

INDEPENDENCE - THREATS TO INDEPENDENCE AND APPROPRIATE SAFEGUARDS
We have provided non audit services in respect of certain grant claims and returns that do not form part of the Code audit or mandated certification work as directed by Public Sector Audit Appointments Limited. These are recorded on the following page and their fees are not considered significant in relation to the audit fees. We are not aware of any financial, business, employment or personal relationships between the audit team, BDO and the authority. We confirm that the firm complies with the FRC's Ethical Standards and, in our professional judgement, is independent and objective within the meaning of those Standards. In our professional judgement the policies and safeguards in place ensure that we are independent within the meaning of all regulatory and professional requirements and that the objectivity of the audit engagement partner and audit staff is not impaired. Should you have any comments or queries regarding this confirmation we would welcome their discussion in more detail.

APPENDIX III: FEES SCHEDULE

	CURRENT YEAR £	THREATS TO INDEPENDENCE ARISING	SAFEGUARDS APPLIED AND WHY THEY ARE EFFECTIVE
Audit fee	86,383	N/A	
Certification fee (housing benefit subsidy)	11,396	N/A	
TOTAL AUDIT FEE	**97,779**		
Reporting on government grants (see below table for breakdown)	11,340	The threat to auditor independence from Audit Related Services is clearly insignificant. (ES5:54)	No safeguards required
TOTAL ASSURANCE SERVICES	**109,119**		

	CURRENT YEAR £
Teachers' Pension (local education authority)	4,500
Teachers' Pension (Centre for Young Musicians (City's Cash))	4,500
Pooling of Housing Capital Receipts	2,340
TOTAL AUDIT FEE	**11,340**

APPENDIX IV: AUDIT QUALITY

BDO is totally committed to audit quality. It is a standing item on the agenda of BDO's Leadership Team who, in conjunction with the Audit Stream Executive (which works to implement strategy and deliver on the audit stream's objectives), monitor the actions required to maintain a high level of audit quality within the audit stream and address findings from external and internal inspections. BDO welcome feedback from external bodies and is committed to implementing a necessary actions to address their findings.

We recognise the importance of continually seeking to improve audit quality and enhancing certain areas. Alongside reviews from a number of external reviewers, the AQR (the Financial Reporting Council's Audit Quality Review team), QAD (the ICAEW Quality Assurance Department) and the PCAOB (Public Company Accounting Oversight Board who oversee the audits of US firms), the firm undertake a thorough annual internal Audit Quality Assurance Review and as member firm of the BDO International network we are also subject to a quality review visit every three years. We have also implemented additional quality control review processes for all listed and public interest audits.

We seek to make improvements and address weaknesses identified from both external and internal quality reviews. Where issues have been identified an action plan is put in place. These plans may relate to individual assignments, individual offices to be firm-wide and in each instance the outcome of these actions is subject to monitoring and have been the subject of our analysis of root causes. The actions may include, but are not necessarily limited to, one or more of the following:

- The implementation, where appropriate, of relevant training for the engagement team where the issue is team specific;
- The revision and production of additional guidance in connection with the firm's audit approach where we identify that an issue is more wide-spread;
- The development and delivery of firm-wide training;
- Amendments and/or enhancements to stream policies and procedures.

FOR MORE INFORMATION:

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