



**CITY OF LONDON CORPORATION
CITY FUND**

AUDIT COMPLETION REPORT
Audit for the year ended 31 March 2018

31 July 2018

CONTENTS

| | | | |
|--|----|--|----|
| WELCOME..... | 2 | APPENDIX I: AUDIT DIFFERENCES | 27 |
| OVERVIEW | 3 | APPENDIX II: RECOMMENDATIONS AND ACTION PLAN | 30 |
| KEY AUDIT AND ACCOUNTING MATTERS | 5 | APPENDIX III: MATERIALITY | 33 |
| OTHER REPORTING MATTERS..... | 20 | APPENDIX IV: INDEPENDENCE | 34 |
| CONTROL ENVIRONMENT | 21 | APPENDIX V: FEES SCHEDULE | 35 |
| WHOLE OF GOVERNMENT ACCOUNTS..... | 22 | APPENDIX VI: DRAFT LETTER OF REPRESENTATION..... | 36 |
| USE OF RESOURCES | 23 | APPENDIX VII: DRAFT AUDIT REPORT | 39 |
| | | APPENDIX VIII: AUDIT QUALITY | 40 |

WELCOME

We have pleasure in presenting our Audit Completion Report to the Audit and Risk Management Committee. This report is an integral part of our communication strategy with you, a strategy which is designed to ensure effective two way communication throughout the audit process with those charged with governance.

It summarises the results of completing the planned audit approach for the year ended 31 March 2018, specific audit findings and areas requiring further discussion and/or the attention of the Audit and Risk Management Committee. At the completion stage of the audit it is essential that we engage with the Audit and Risk Management Committee on the results of audit work on key risk areas, including significant estimates and judgements made by management, critical accounting policies, any significant deficiencies in internal controls, and the presentation and disclosure in the financial statements.

We discussed these matters with you at the Audit and Risk Management Committee meeting on 17 July 2018.

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

We would also like to take this opportunity to thank the management and staff of the Corporation for the co-operation and assistance provided during the audit.

OVERVIEW

This summary provides an overview of the audit matters that we believe are important to the Audit and Risk Management Committee in reviewing the results of the audit of the financial statements and use of resources of the Corporation's City Fund for the year ended 31 March 2018. It is also intended to promote effective communication and discussion and to ensure that the results of the audit appropriately incorporate input from those charged with governance.

| AUDIT SCOPE AND OBJECTIVES | |
|----------------------------------|--|
| Audit status | We have completed our audit procedures in accordance with the planned scope and our objectives have been achieved. |
| Audit risks update | No additional significant audit risks were identified during the course of our audit procedures subsequent to our Audit Plan to you dated 15 February 2018. |
| Materiality | Our final materiality is £24.4 million with specific materiality for items which impact on the Comprehensive Income and Expenditure statement of £6.3 million. We have increased our materiality from £23.4 million to £24.4 million as a result of an increase in the valuation of assets and increased our specific materiality from £5.8 million to £6.3 million as a result of an increase in gross expenditure. |
| Changes to audit approach | There were no significant changes to our planned audit approach nor were any restrictions placed on our audit. |
| KEY AUDIT AND ACCOUNTING MATTERS | |
| Material misstatements | Our audit identified no material misstatements. |
| Unadjusted audit differences | <p>We are required to bring to your attention audit differences that we have identified, but you are not proposing to adjust. These include:</p> <ul style="list-style-type: none"> Two errors in the calculation of the provision for NDR appeals including an error in the formula that reduces the provision by £4.1 million and re-categorisation of appeal type for a number of appeals that increases the provision by £1.4 million. The net error is an overstatement of the appeals provision and understatement of the surplus for the year of £2.7 million in the collection fund and the City Fund's share included in the CIES of £0.81 million based on the 30% share of business rates. We believe that management has been overly prudent in providing for 100% of 2017 rating list appeals and that the provision amount, while not material, may be overstated by a non-trivial amount. We estimate that the potential impact on the Corporation's CIES where the amount provided is beyond a reasonable range could be up to £0.35 million. Error in the depreciation rate used resulting in £0.16 million overstatement of depreciation cost (and understatement of assets). Errors found where accrued expenditure for open purchase orders had been recorded as receipted but not invoiced (GRNIs) but where the orders had only been partly fulfilled. Our testing of 14 items with a value of £2.69 million identified 6 items totalling £0.84 million should not have been included as accrued expenditure. We have projected potential additional errors across the total of GRNIs at £2.47 million. <p>If corrected, these errors would increase the surplus on the provision of services for the year by £2.16 million (or £4.63 million including the projected error across all GRNIs). The depreciation error and NDR appeals provision errors would not impact on the General Fund balance this year as these are reversed to other reserves.</p> |
| Control environment | We identified a significant weakness in internal controls relating to strategic financial management for the City of London Police Force. |

OVERVIEW

KEY MATTERS FROM OUR AUDIT OF USE OF RESOURCES

| | |
|------------------------------------|--|
| Sustainable finances (City Police) | <p>City Police has produced an MTFS showing a surplus for 2018/19 and then moving into deficit over the following three years. Our review of the processes around the production of the MTFS and budget monitoring by the police finance team has identified a number of weaknesses including overly optimistic financial estimates and assumptions, incorrect treatment of slippage of projects and high turnover of senior finance staff.</p> <p>We consider that there are deficiencies in the robustness and accuracy of the information being provided by the City Police Finance team to the Corporation of London's Chamberlain's department. The Chamberlain's Department is providing assistance to strengthen financial management arrangements in the City Police Finance team and to provide additional financial resources in the short term to address funding gaps.</p> |
| Sustainable finances (City Fund) | <p>The City Fund MTFS shows a surplus for 2018/19 but then forecasts a budgeted deficit over the following three years through planned withdrawal from reserves of £103 million to fund the Museum of London and Combined Courts Relocation projects. The City Fund may choose to make use of capital borrowing rather than revenue funding for some of these costs as they crystallise should the need arise. The City Fund currently holds reserves of £122 million. We consider that there are appropriate arrangements in place with regard to sustainable finances for City Fund.</p> |

AUDIT OPINION

| | |
|----------------------|---|
| Financial statements | We issued an unmodified opinion on the financial statements for the year ended 31 March 2018. |
| Governance Statement | We have no exceptions to report in relation to the consistency of the Annual Governance Statement with the financial statements or our knowledge. |
| Use of resources | We issued an unmodified opinion on the arrangements for securing economy, efficiency and effectiveness for the use of resources for the year ended 31 March 2018. |

OTHER MATTERS FOR THE ATTENTION OF THE AUDIT COMMITTEE

| | |
|-------------------------------------|---|
| Whole of Government Accounts (WGA) | We will complete our review of the WGA Data Collection Tool (DCT), after we have completed our audit of the financial statements. We plan to issue our opinion on the consistency of the DCT return with the audited financial statements before the 31 August 2018 deadline. |
| Audit independence | Our observations on our audit independence and objectivity and related matters are set out in Appendix IV. |
| Management letter of representation | The management letter of representation is set out in Appendix VI. |

KEY AUDIT AND ACCOUNTING MATTERS

AUDIT RISKS

We assessed the following matters as audit risks, as identified in our Audit Plan to the Audit and Risk Management Committee. We have set out below how these risks have been addressed and the outcomes of our procedures.

Key: ■ Significant risk ■ Normal risk ■ Other key issues

| | AUDIT AREA | RISK DESCRIPTION | HOW RISK WAS ADDRESSED BY OUR AUDIT | AUDIT FINDINGS AND CONCLUSION |
|---|--|--|---|--|
| 1 | Management override of controls | <p>Auditing standards presume that a risk of management override of controls is present in all entities and require us to 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.</p> <p>By its nature, there are no controls in place to mitigate the risk of management override.</p> | <p>We have:</p> <ul style="list-style-type: none"> Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements Reviewed accounting estimates for biases and evaluated whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud Obtained an understanding of the business rationale for significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual. | <p>Our work testing journal entries has not identified any issues.</p> <p>We have found no bias in accounting estimates. We have commented on the reasonableness of significant accounting estimates later in the report.</p> <p>We found no significant transactions that were outside the normal course of business or otherwise appear unusual.</p> |



KEY AUDIT AND ACCOUNTING MATTERS

| | AUDIT AREA | RISK DESCRIPTION | HOW RISK WAS ADDRESSED BY OUR AUDIT | AUDIT FINDINGS AND CONCLUSION |
|---|----------------------|---|--|--|
| 2 | Revenue recognitions | <p>Under Auditing Standards there is a presumption that income recognition presents a fraud risk.</p> <p>In particular, we consider there to be a significant risk in respect of the existence (recognition) 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).</p> <p>We also consider there to be a significant risk in relation to the existence of fees and charges and investment rental income recorded in the CIES with a particular focus on year-end cut off.</p> | <p>We 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.</p> <p>We tested a sample of fees and charges to ensure income has been recorded in the correct period and that all income that has been recorded should have been recorded.</p> | <p>Our work testing a sample of grants and performance conditions is complete and no issues have been identified.</p> <p>Our testing confirmed that income has been recorded in the correct period and that income that should have been recorded has been recorded.</p> |

KEY AUDIT AND ACCOUNTING MATTERS

| AUDIT AREA | RISK DESCRIPTION | HOW RISK WAS ADDRESSED BY OUR AUDIT | AUDIT FINDINGS AND CONCLUSION |
|---|--|---|---|
| <p>3 Land, buildings, dwellings and investment property valuations</p> | <p>Management use external valuation data to assess whether there has been a material change in the value of classes of assets. Investment properties are revalued annually according to market conditions at year-end. Higher value operational properties (other land and buildings and dwellings) are revalued annually to provide assurance that carrying values are materially stated, with the remainder of non-material value assets revalued periodically (minimum of every five years). Operational asset valuations are undertaken by both external and internal valuers.</p> <p>We consider there to be a significant risk over the valuation of land buildings, dwellings and investment properties where valuations are based on market assumptions or where updated valuations have not be provided for a class of assets at the year-end.</p> <p>This is a significant risk due to the higher estimation uncertainty arising from the range of assumptions available to value land and property assets.</p> | <p>We reviewed the instructions and the detailed information provided by the City Fund to the valuers and performed procedures to confirm the accuracy and completeness of the information.</p> <p>We confirmed that the basis of valuation for assets valued in year is appropriate based on their usage.</p> <p>We reviewed valuation movements against indices of price movements for similar classes of assets and followed up valuation movements that appear unusual against indices.</p> | <p>From our review of the instructions provided to the valuers and assessment of the expertise of the valuers, we are satisfied that we can rely on this work. Our audit work to agree the accuracy and completeness of information provided to the valuers to support the underlying asset data (such as floor areas and rent agreements) did not identify any issues.</p> <p>Our audit work on valuation basis applied for the use of the asset for a sample of assets did not identify any issues.</p> <p>Overall the valuation movements were in line with our expectations based on indices for similar classes of transactions. Our review of the reasonableness of valuation assumptions applied is noted on the following page.</p> |


KEY AUDIT AND ACCOUNTING MATTERS

| SIGNIFICANT ACCOUNTING ESTIMATES | | |
|---|--|--|
| Land, buildings, dwellings and investment property valuations | | |
| ESTIMATE | HOW RISK WAS ADDRESSED BY OUR AUDIT | IMPACT |
| <p>Land and buildings are valued by reference to existing use market values</p> <p>Dwellings are valued by reference to open market value less a social housing discount</p> <p>Investment properties are valued by reference to highest and best use market value</p> <p>Some specialist buildings are valued at depreciated replacement cost by reference to building indices</p> | <p>We have benchmarked the valuation movements to land and building price indices for the year produced by Gerald Eve LLP and reviewed the information and assumptions used by the valuers.</p> <p>Dwellings</p> <p>Council dwellings decreased in value by £10.9 million (-3.17%) in 2017/18.</p> <p>Dwellings were subject to valuation based on allocation of properties into relevant Beacons (for similar types of properties) and valued by reference to recent sales data for similar properties. Our benchmark report for house prices suggests an overall reduction in value of London properties 0.7% and the City Surveyor has provided City of London price data suggesting an overall market reduction for house sales of 0.45% based on the Nationwide Index London Regional House Sales.</p> <p>The commentary provided in relation to the HRA valuation provides details of the sales data used to support the HRA valuation. Where possible the City Surveyor has used other sales on City Fund Estates to support their valuations. Where there haven't been appropriate sales in the year the City Surveyor have used other similar properties in the area or other City of London Estates. Based on our work, we are satisfied that the valuations of dwellings are reasonable.</p> <p>We note that the useful economic lives (UEL) of council dwellings has been set at 125 years based on the usual term for leases granted and is significantly longer than the UELs used by other local authorities. The Corporation's City Surveyor has stated that this is due to the robust structure and ongoing repairs, maintenance and cyclical replacement works programmes in place for these properties. We are satisfied that the remaining UELs, used to calculate council dwelling depreciation, are reasonable.</p> <p>Other land and buildings</p> <p>Other land and buildings increased in value by £34.8 million (+7.98%) in 2017/18.</p> <p>Land and buildings have been valued using an appropriate basis of valuation (such as existing use, depreciated replacement cost or market value) depending on the use of the asset.</p> <p>Our benchmark report for rebuild costs from the national BCIS Tender Price Index suggests an increase in value for depreciated replacement cost (DRC) valuations of +6.7%, although this is subject to a higher degree of volatility and estimation from regional costs and other factors.</p> <p>Based on our work, we are satisfied that the valuations of other land and buildings are reasonable.</p> | <p style="text-align: center;">↓</p>  <p style="text-align: center;">< lower higher ></p> <p style="text-align: center;">↓</p>  <p style="text-align: center;">< lower higher ></p> |

KEY AUDIT AND ACCOUNTING MATTERS

SIGNIFICANT ACCOUNTING ESTIMATES

Land, buildings, dwellings and investment property valuations

| ESTIMATE | HOW RISK WAS ADDRESSED BY OUR AUDIT | IMPACT |
|---|--|---|
| <p>Land and buildings are valued by reference to existing use market values</p> <p>Dwellings are valued by reference to open market value less a social housing discount</p> <p>Investment properties are valued by reference to highest and best use market value</p> <p>Some specialist buildings are valued at depreciated replacement cost by reference to building indices</p> | <p>Investment properties</p> <p>Investment properties increased in value by £69.2 million (+4.79%) in 2017/18. Our benchmark report for City office space suggests an increase in value of 4.0% (MSCI capital index) and +4.3% for City / Mid Town retail space. We agreed a sample of investment properties to rent agreements and reviewed the data for a sample of properties where the movement in value appeared unusual compared to the general index movement. Based on our work to date, we are satisfied that the valuations of investment properties are reasonable.</p> <p>We note that this year, following a change of valuer for investment properties, the basis of valuation disclosure is now a mixture of Level 2 (based on recent sales for similar properties with significant observable inputs) and Level 3 (using modelling techniques) depending on the type of property. All investment properties were classified as Level 2 last year. We noted that in prior year the European Public Real Estate Association (EPRA) 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.</p> <p>Assets not revalued in year</p> <p>The majority of land and property assets are subject to annual valuation although some lower value other land and buildings are subject to a rolling five-year, with a desktop review of the assets not revalued undertaken to assess whether, as a class of assets, these should be subject to valuation adjustment if the current value is materially different to their carrying value. No adjustments have been made for these assets not subject to revaluation in year. Based on our review, we are satisfied that classes of assets that have not been revalued are not materially different to their current value.</p> | <p style="text-align: center;">↓</p>  <p style="text-align: center;">< lower higher ></p> |

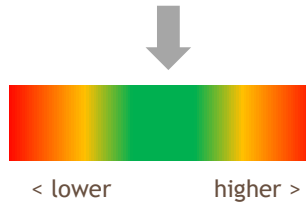
KEY AUDIT AND ACCOUNTING MATTERS

| AUDIT AREA | RISK DESCRIPTION | HOW RISK WAS ADDRESSED BY OUR AUDIT | AUDIT FINDINGS AND CONCLUSION |
|--|---|--|---|
| <p>4 LGPS pension and police pension liabilities assumptions</p> | <p>The LGPS pension liability comprises the City Fund's share of the market value of assets held in the City of London Pension Fund and the estimated future liability to pay pensions. The unfunded police pension liability includes the future liability to pay police pensions. An actuarial estimate of the pension funds' liabilities is calculated by an independent firm of actuaries with specialist knowledge and experience.</p> <p>The estimate is based on a roll-forward of membership data from the most recent full valuation (2016 for LGPS and 2017 for police), updated where necessary, and has regard to local factors such as mortality rates and expected pay rises along with other assumptions around inflation when calculating the liability at 31 March 2018.</p> <p>There is a risk the membership data and cash flows provided to the actuary at 31 March may not be correct, or the valuation uses inappropriate assumptions to value the liability.</p> | <p>We compared the assumptions used by the scheme actuary with assumptions used by other local government actuaries (provided by PwC consulting actuaries) to assess the reasonableness of the assumptions and impact on the calculation of the present value of estimated future pension payments.</p> <p>We checked that the disclosure in the financial statements were consistent with the information provided by the actuary.</p> <p>We reviewed the data provided to the actuary to ensure that is complete and accurate.</p> | <p>We are satisfied that the assumptions used to calculate the present value of future pension obligations are reasonable. Further information on the assumptions used is included in the following page.</p> <p>All disclosures were agreed to the actuary's report. We note that the allocation of the overall LGPS net liability is allocated across the Corporation's funds based on the proportion of pensionable payroll for each fund, and City Fund's share is 51% in the current and previous year.</p> <p>We have obtained assurance over the membership data, data provided at the last full valuations and the cash flows used by the actuary to update liabilities and share of assets for the year.</p> |

KEY AUDIT AND ACCOUNTING MATTERS

SIGNIFICANT ACCOUNTING ESTIMATES

Pension liability assumptions - LGPS

| ESTIMATE | HOW RISK WAS ADDRESSED BY OUR AUDIT | IMPACT | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
|---|---|---|------------|---|------------------------------------|---------|--------------|------|------------|------------|--------------|------|------------|------------|-----------------|------|---|------------------------------------|------------------|------|------------|------------|---------------|-------|------------|------------|-------------------|--|--|--|----------------|------------|-----------|------------|------------------|------------|-----------|------------|----------------|------------|-----------|------------|------------------|------------|------------|------------|-------------|-----|-----|------------|
| The key assumptions include estimating future expected cash flows to pay pensions including inflation, salary increases and mortality of members; and the discount rate to calculate the present value of these cash outflows | <p>The City Fund's share of the LGPS net pension liability reduced by £2.7 million to £302.2 million in the year. This includes an increase in scheme assets of £11.1 million from interest and gains on investments and an increase in liabilities £8.4 million where current service costs and interest on liabilities exceeds contributions.</p> <p>We have compared the assumptions used to an acceptable range and those used across the local government actuaries. The PwC consulting actuary review of the relative strength of the main assumptions on the liability assumptions suggests that Barnett Waddingham tends to place a higher value on the LGPS liabilities than other actuaries where standard assumptions are applied and that the overall assumptions are reasonable.</p> |  <p>< lower higher ></p> | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | <table border="1"> <thead> <tr> <th></th> <th>Actual</th> <th>Acceptable range</th> <th>Comment</th> </tr> </thead> <tbody> <tr> <td>RPI increase</td> <td>3.3%</td> <td>3.30-3.35%</td> <td>Reasonable</td> </tr> <tr> <td>CPI increase</td> <td>2.3%</td> <td>2.30-2.35%</td> <td>Reasonable</td> </tr> <tr> <td>Salary increase</td> <td>3.8%</td> <td>CPI +1.5% to 2.2% (based on 2016 valuation)</td> <td>Reasonable in context of CPI / RPI</td> </tr> <tr> <td>Pension increase</td> <td>2.3%</td> <td>2.30-2.35%</td> <td>Reasonable</td> </tr> <tr> <td>Discount rate</td> <td>2.55%</td> <td>2.50-2.60%</td> <td>Reasonable</td> </tr> <tr> <td colspan="4">Mortality - LGPS:</td> </tr> <tr> <td>- Male current</td> <td>25.3 years</td> <td>23.7-26.8</td> <td>Reasonable</td> </tr> <tr> <td>- Female current</td> <td>26.7 years</td> <td>26.6-28.4</td> <td>Reasonable</td> </tr> <tr> <td>- Male retired</td> <td>23.9 years</td> <td>21.5-24.5</td> <td>Reasonable</td> </tr> <tr> <td>- Female retired</td> <td>25.2 years</td> <td>24.3-26.10</td> <td>Reasonable</td> </tr> <tr> <td>Commutation</td> <td>50%</td> <td>50%</td> <td>Reasonable</td> </tr> </tbody> </table> | | | Actual | Acceptable range | Comment | RPI increase | 3.3% | 3.30-3.35% | Reasonable | CPI increase | 2.3% | 2.30-2.35% | Reasonable | Salary increase | 3.8% | CPI +1.5% to 2.2% (based on 2016 valuation) | Reasonable in context of CPI / RPI | Pension increase | 2.3% | 2.30-2.35% | Reasonable | Discount rate | 2.55% | 2.50-2.60% | Reasonable | Mortality - LGPS: | | | | - Male current | 25.3 years | 23.7-26.8 | Reasonable | - Female current | 26.7 years | 26.6-28.4 | Reasonable | - Male retired | 23.9 years | 21.5-24.5 | Reasonable | - Female retired | 25.2 years | 24.3-26.10 | Reasonable | Commutation | 50% | 50% | Reasonable |
| | | | Actual | Acceptable range | Comment | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | RPI increase | | 3.3% | 3.30-3.35% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | CPI increase | | 2.3% | 2.30-2.35% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Salary increase | | 3.8% | CPI +1.5% to 2.2% (based on 2016 valuation) | Reasonable in context of CPI / RPI | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Pension increase | | 2.3% | 2.30-2.35% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Discount rate | | 2.55% | 2.50-2.60% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Mortality - LGPS: | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | - Male current | | 25.3 years | 23.7-26.8 | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | - Female current | | 26.7 years | 26.6-28.4 | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | - Male retired | | 23.9 years | 21.5-24.5 | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | - Female retired | | 25.2 years | 24.3-26.10 | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Commutation | | 50% | 50% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| The assumptions used fall within the reasonable range. | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |

KEY AUDIT AND ACCOUNTING MATTERS

| SIGNIFICANT ACCOUNTING ESTIMATES | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
|--|--|---|---|-------------------|--|------------------|----------|--------------|------|------------|------------|--------------|------|------------|------------|-----------------|------|-------------------|--|------------------|------|------------|------------|---------------|-------|------------|------------|-------------------|--|--|--|----------------|------------|---|--|------------------|------------|---|--|----------------|------------|---|--|------------------|------------|---|--|
| Pension liability assumptions - Police | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| ESTIMATE | HOW RISK WAS ADDRESSED BY OUR AUDIT | | IMPACT | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| <p>The key assumptions include estimating future expected cash flows to pay pensions including inflation, salary increases and mortality of members; and the discount rate to calculate the present value of these cash outflows</p> | <p>The police pension liability increased by £42.9 million to £955.9 million in the year. A full valuation update was undertaken using membership data at 31 March 2017 and, along with other changes in assumptions at 31 March 2018, has resulted in demographic and other experience losses in 2017/18 of £53 million and gains from changes to financial assumptions of £25 million.</p> <p>We have compared the assumptions used to an acceptable range and those used across the police actuaries. The PwC consulting actuary review of the relative strength of the main assumptions on the police liability assumptions suggests that Barnett Waddingham tends to place a medium strength value on the liability compared to other actuaries where standard assumptions are applied and that the overall assumptions are reasonable.</p> | | <p style="text-align: center;">↓</p> <p style="text-align: center;">< lower higher ></p> | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | | <table border="1"> <thead> <tr> <th></th> <th>Actual</th> <th>Acceptable range</th> <th>Comments</th> </tr> </thead> <tbody> <tr> <td>RPI increase</td> <td>3.3%</td> <td>3.30-3.35%</td> <td>Reasonable</td> </tr> <tr> <td>CPI increase</td> <td>2.3%</td> <td>2.30-2.35%</td> <td>Reasonable</td> </tr> <tr> <td>Salary increase</td> <td>3.8%</td> <td>CPI +1.5% to 2.2%</td> <td>(based on 2016 valuation) Reasonable in context of CPI / RPI</td> </tr> <tr> <td>Pension increase</td> <td>2.3%</td> <td>2.30-2.35%</td> <td>Reasonable</td> </tr> <tr> <td>Discount rate</td> <td>2.55%</td> <td>2.50-2.60%</td> <td>Reasonable</td> </tr> <tr> <td colspan="4">Mortality - LGPS:</td> </tr> <tr> <td>- Male current</td> <td>23.2 years</td> <td>-</td> <td>As per full valuation mortality assessment</td> </tr> <tr> <td>- Female current</td> <td>25.6 years</td> <td>-</td> <td>As per full valuation mortality assessment</td> </tr> <tr> <td>- Male retired</td> <td>21.7 years</td> <td>-</td> <td>As per full valuation mortality assessment</td> </tr> <tr> <td>- Female retired</td> <td>24.0 years</td> <td>-</td> <td>As per full valuation mortality assessment</td> </tr> </tbody> </table> | | | Actual | Acceptable range | Comments | RPI increase | 3.3% | 3.30-3.35% | Reasonable | CPI increase | 2.3% | 2.30-2.35% | Reasonable | Salary increase | 3.8% | CPI +1.5% to 2.2% | (based on 2016 valuation) Reasonable in context of CPI / RPI | Pension increase | 2.3% | 2.30-2.35% | Reasonable | Discount rate | 2.55% | 2.50-2.60% | Reasonable | Mortality - LGPS: | | | | - Male current | 23.2 years | - | As per full valuation mortality assessment | - Female current | 25.6 years | - | As per full valuation mortality assessment | - Male retired | 21.7 years | - | As per full valuation mortality assessment | - Female retired | 24.0 years | - | As per full valuation mortality assessment |
| | | Actual | | Acceptable range | Comments | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | RPI increase | 3.3% | | 3.30-3.35% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | CPI increase | 2.3% | | 2.30-2.35% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Salary increase | 3.8% | | CPI +1.5% to 2.2% | (based on 2016 valuation) Reasonable in context of CPI / RPI | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Pension increase | 2.3% | | 2.30-2.35% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Discount rate | 2.55% | | 2.50-2.60% | Reasonable | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | Mortality - LGPS: | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | - Male current | 23.2 years | | - | As per full valuation mortality assessment | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| - Female current | 25.6 years | - | As per full valuation mortality assessment | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| - Male retired | 21.7 years | - | As per full valuation mortality assessment | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| - Female retired | 24.0 years | - | As per full valuation mortality assessment | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | <p>Mortality ranges are not provided within the PwC report for police but has stated that the approach taken by the actuary to estimate mortality rates is reasonable</p> | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | <p>The assumptions used fall within the reasonable range.</p> | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |


KEY AUDIT AND ACCOUNTING MATTERS

| | AUDIT AREA | RISK DESCRIPTION | HOW RISK WAS ADDRESSED BY OUR AUDIT | AUDIT FINDINGS AND CONCLUSION |
|---|---|--|--|--|
| 5 | Lease premiums | <p>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.</p> <p>The apportionment between the land and building elements is a complex accounting estimate and there is a risk that the value of the split applied may not be appropriate.</p> | <p>We reviewed the process applied for apportioning lease premiums between land (deferred revenue) and buildings (capital disposal) including reviewing the work of external valuer to confirm if this is appropriate.</p> <p>We selected a sample of leases and confirm that the allocations have been accurately calculated.</p> | <p>Our audit work to test a sample lease premium allocations did not identify any issues.</p> |
| 6 | Consideration of related party transactions | <p>We consider if the disclosures in the financial statements concerning related party transactions are complete and accurate, and in line with the requirements of the accounting standards.</p> <p>There is a risk that related party transactions disclosures are omitted from the financial statements, or do not accurately reflect the underlying related party transaction.</p> | <p>We reviewed relevant information concerning any such identified transactions.</p> <p>We have discussed with management and review member's and Senior Management declarations to ensure there are no potential related party transactions which have not been disclosed.</p> | <p>We found a small number of errors in the disclosure provided for audit and these have been amended in the final accounts.</p> |

KEY AUDIT AND ACCOUNTING MATTERS

| | AUDIT AREA | RISK DESCRIPTION | HOW RISK WAS ADDRESSED BY OUR AUDIT | AUDIT FINDINGS AND CONCLUSION |
|---|--------------------------------------|---|---|--|
| 7 | Non-domestic rates appeals provision | <p>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.</p> <p>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.</p> <p>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.</p> | <p>We reviewed the accuracy of the appeals data to confirm that it is complete based on the VOA list, and that settled appeals are removed.</p> <p>We reviewed the assumptions used in the preparation of the estimate including the historic success rates to confirm that appeal success rates and amounts expected to be refunded are appropriate.</p> | <p>Our audit work found that the methodology for calculation of the appeals provision was satisfactory and was based on accurate information provided by the VOA.</p> <p>However, we found two errors in calculations. Firstly, an error in formula used to calculate the provision resulted in an overstatement of the appeals provision by £4.1 million. Secondly, the re-categorisation of appeal type for a number of appeals that increases the provision by £1.4 million.</p> <p>The net error is an overstatement of the appeals provision and understatement of the surplus for the year of £2.7 million in the collection fund and the City Fund's share included in the CIES of £0.81 million based on the 30% share of business rates.</p> <p>Our review of the reasonableness of assumptions used to estimate the likely success of appeals and expected refunds is noted on the following page.</p> |

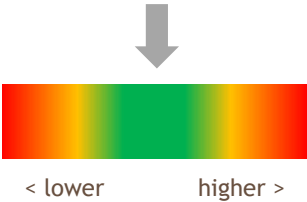
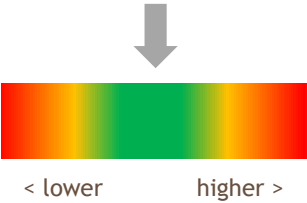
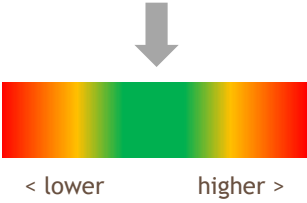
KEY AUDIT AND ACCOUNTING MATTERS

| ACCOUNTING ESTIMATES | | |
|--|--|---|
| Provision for NDR appeals | | |
| ESTIMATE | HOW RISK WAS ADDRESSED BY OUR AUDIT | IMPACT |
| <p>The key assumption is the future expected rate of successful appeals and amount to be refunded to rate payers</p> | <p>Management applied different success rates to different types of appeals based on the amounts repaid on appeal on recent years against the amount appealed. This takes into account both the success of a rateable value reduction appeal and for the number of years the appeal is backdated.</p> <p>2010 rating list</p> <p>Success rates for the 2010 valuations range from 0.2% for appeals with multiple assessments to 11% for appeals where there have been material changes in circumstances. Higher success rates have been used for properties that have been demolished or no longer exist (22.3%).</p> <p>These assumptions are reasonable based on historic settlements and refunds for the 2010 rating list appeals for estimating the provision for the future refunds from successful appeal.</p> <p>2017 rating list</p> <p>The Corporation has received appeals totalling £1.5 million on the 2017 rating list. As there are no settled appeals for the 2017 rating list for the Corporation, management has applied a success rate of 100% to the appeals received to date due to a lack of reliable data. The Corporation's share of this provision at 30% is £0.45 million. We are aware that MHCLG has informed local authorities that they may wish to apply a rate at 4.7% of appealed bills based on a national review of data.</p> <p>Our view is that management has been overly prudent in providing for 100% of appeals and that the provision amount, while not material, may be overstated by a non-trivial amount. We estimate that the potential impact on the Corporation's CIES where the amount provided is beyond a reasonable range could be up to £0.35 million.</p> | <p style="text-align: center;">↓</p>  <p style="text-align: center;">< lower higher ></p> |

KEY AUDIT AND ACCOUNTING MATTERS

| | AUDIT AREA | RISK DESCRIPTION | HOW RISK WAS ADDRESSED BY OUR AUDIT | AUDIT FINDINGS AND CONCLUSION |
|---|--|--|--|---|
| 8 | Allowances for non-collection of receivables | <p>The City Fund includes a material amount in respect of provisions for non-collection of NDR arrears, private residential rent arrears (current tenants) and arrears in relation to the Barbican Centre and City Police.</p> <p>There is a risk that the provisions may not accurately reflect collection rates based on age or debt recovery rates.</p> | <p>We reviewed the provision model for significant income streams and debtor balances to assess whether it appropriately reflects historical collection rates by age of debt or arrears.</p> | <p>Our audit work to agreed provision rates to aged debt based on collection rates in recent years did not identify any issues.</p> |

KEY AUDIT AND ACCOUNTING MATTERS

| ACCOUNTING ESTIMATES | | |
|---|---|--|
| Allowances for non-collection of receivables | | |
| ESTIMATE | HOW RISK WAS ADDRESSED BY OUR AUDIT | IMPACT |
| The key assumption is the estimate of future write off for uncollectable debt across material debtors | <p>Non-domestic rate arrears and cost provision</p> <p>The City Fund's share of debts and provision at the 31 March 2018 was £11 million and £3 million respectively. The majority of the provision has been calculated using the best information available at the year-end, for example, current collection rates.</p> <p>We note that £0.291 million of the provision has been calculated using generic CIPFA guidelines that 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.</p> <p>We are satisfied that the provision for non-collection of NDR arrears assumptions are reasonable.</p> |  |
| | <p>Rent arrears and cost provision</p> <p>Arrears and provision as at 31 March 2018 were £11.9 million and £0.7 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.</p> <p>We are satisfied that the provision for non-collection of rent arrears assumptions are reasonable.</p> |  |
| | <p>Sundry debt arrears and cost provision</p> <p>Arrears and provision as at 31 March 2018 were £28.4 million and £4.9 million respectively. The vast majority of the sundry arrears relate to the Barbican Centre and Police. All significant debts are now reviewed on a case-by-case basis rather than using standard provision percentages that cannot be supported but appropriate audit evidence, as reported by us in the prior year</p> <p>We are satisfied that the provision for non-collection of sundry debt assumptions are reasonable.</p> |  |

KEY AUDIT AND ACCOUNTING MATTERS

OTHER ISSUES

We comment below on other issues identified in the course of our audit, of which we believe you should be aware:

| | AUDIT AREA | AUDIT FINDINGS |
|----|------------------------------|--|
| 9 | Completeness of expenditure | Our testing of the completeness of HRA expenditure identified one invoice which related to a software license for 2018/19 but was incorrectly recorded as expenditure in 2017/18. We have extended our testing of expenditure cut-off to ascertain whether this is an isolate error or indicative of a wider potential misstatement. We did not find any further issues and therefore concluded that this was an isolated incident. |
| 10 | Presentation and disclosures | <p>Our initial review of the financial statements noted a number of presentational issues which are due to be amended in the revised set of accounts. In the course of our work we noted:</p> <ul style="list-style-type: none"> • Multiple errors within the senior office remuneration and banding note • Omissions in the exit packages note (7 employees) • Omissions in the related parties note (2 related parties) • LGPS current service cost incorrectly included in Net cost of service for Spitalfields as this is included as a traded service and should be included below the Net cost of services line • Collection fund disclosure omitted the total rateable value disclosure • Fixed asset register revaluation figure does not agree to the figure in the accounts • Capital commitments disclosure was understated • Finance lease disclosure not updated from the prior year • Additions to intangible assets incorrectly classified as Vehicles, Plant and Equipment. |
| 10 | Goods received not invoiced | Our testing of accrued expenditure for open purchase orders that had been recorded as receipted but not invoiced (GRNIs) found a number of instances where the order had only been partly fulfilled but the full amount of the order recorded as expenditure in the year. We extended our testing and found errors for 6 GRNI items totalling £0.84 million (total tested £2.69 million) that should not have been included as accrued expenditure. We have projected potential additional errors across total of GRNIs at £2.47m based on the error rate for the sample tested. |

KEY AUDIT AND ACCOUNTING MATTERS

MATTERS REQUIRING ADDITIONAL CONSIDERATION

We comment below on other matters requiring additional consideration:

| | AUDIT AREA | AUDIT FINDINGS |
|----|------------|--|
| 11 | Fraud | Whilst management has ultimate responsibility for prevention and detection of fraud, we are required to obtain reasonable assurance that the financial statements are free from material misstatement, including those arising as a result of fraud. Our audit procedures did not identify any fraud. We will seek confirmation from those charged with governance on whether you are aware of any known, suspected or alleged frauds. |

OTHER REPORTING MATTERS

We comment below on other reporting required to be considered in arriving at the final content of our audit report:

| MATTER | COMMENT |
|--------|---|
| 1 | <p>We are required to report on whether the financial and non-financial information in the Statement of Accounts is consistent with the financial statements and the knowledge acquired by us in the course of our audit.</p> <p>Our audit identified one inconsistency between the other information in the Statement of Accounts and the financial statements:</p> <ul style="list-style-type: none">Budgeted forecast surplus for police is shown as £0 in the narrative report and £4.2 million in the MTFS. The MTFS figure is the correct one. <p>This issue has been corrected in the revised Statement of Accounts.</p> |
| 2 | <p>We are required to report by exception if the Annual Governance Statement is misleading or inconsistent with other information that is forthcoming from the audit.</p> <p>Our work has not identified any issues.</p> |

CONTROL ENVIRONMENT

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 the Audit and Risk Management Committee.

As the purpose of the audit is for us to express an opinion on the Corporation's City Fund financial statements and use of resources, 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 note that the Corporation's internal audit function has issued a number of observations and recommendations on the control environment during 2017/18. We have not repeated these recommendations in this report unless we consider them to highlight significant deficiencies in control which we are required to report to you.

We have identified one significant weakness in internal controls relating to the budget setting and monitoring process for the City of London Police Force. Further details are provided within the Use of Resources section below.

We have also identified other deficiencies in controls which have been discussed with management and included in the action plan at Appendix II.

WHOLE OF GOVERNMENT ACCOUNTS

We comment below on other reporting required:

| | MATTER | COMMENT |
|---|---|---|
| 1 | For Whole of Government Accounts (WGA) component bodies that are over the prescribed threshold of £500 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 Corporation for use by 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. | Our review of the Corporation's WGA Data Collection Tool (DCT) is in progress. We will complete our review of the WGA Data Collection Tool (DCT), after we have completed our audit of the Corporation's City Fund financial statements. We will issue our opinion on the consistency of the DCT return with the audited financial statements before the 31 August 2018 statutory deadline. |

USE OF RESOURCES

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) and report to you on an 'except for' basis. 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.

AUDIT RISKS

We assessed the following matters as audit risks, as identified in our Audit Plan to the Audit and Risk Management Committee. We have set out below how these risks have been addressed and the outcomes of our work.

Key: ■ Significant risk ■ Normal risk

USE OF RESOURCES

| RISK AREA | RISK DESCRIPTION AND WORK PERFORMED | AUDIT FINDINGS AND CONCLUSION |
|---|--|--|
| <p>1 Financial planning and informed decision making (City Police)</p> | <p>City Police had forecast an overspend of £1.6 million at Month 6 and at Month 9 reforecast that it was on course to balance the budget. This favourable movement was due to the continued and widespread vacancies across the Force and eleven deleted Police Staff posts in December 2017 which has created significant underspending within pay budgets.</p> <p>The police budget for 2018/19 has been brought into balance, through a combination of efficiency savings, additional government grant in the provisional settlement and drawdown on reserves. This intends to provide time to implement Force transformation plans following the Deloitte Review. This should help to address the forecast budget deficit of £4 to 5 million per annum in subsequent years, when it is anticipated reserves will be exhausted, and pressures arising from increased demand and the changing nature of police services.</p> <p>Identifying the required level of savings in the medium term will be a challenge and is likely to require difficult decisions around service provision and possible increases in business rate premium.</p> <p>We reviewed the Medium Term Financial Strategy and assess the reasonableness of the assumptions used for cost pressures and the amount of grant reductions applied. We also reviewed the findings of the Internal Audit review of the MTFS process.</p> <p>We also reviewed the delivery of the budgeted savings in 2017/18 and the strategies to close the budget gap in the medium term.</p> | <p>City Police reported an outturn surplus of £3.5 million for 2017/18 and reported that this has been achieved through underspends and savings.</p> <p>We believe that this does not reflect underlying performance since the surplus is a result of slippage on costs that have been carried forward into future years that were funded from additional resources provided from the City Fund budget. Currently this is not reflected in their Budget for 2018/19 and City Police has submitted a balanced budget for 2018/19.</p> <p>We consider that there are deficiencies in the robustness and accuracy of the information being provided by the City Police Finance team to the Corporation of London's Chamberlain's department. As a result of the unbudgeted slippage the breakeven position in 2018/19, which was thought to be providing breathing space for the Force transformation plans to be progressed following the Deloitte review, is no longer available at the level first thought.</p> <p>In addition, the Chamberlain's Department and Internal Audit have raised a number of concerns regarding the development of the Police MTFS and subsequent budget monitoring which we concur with. Late and incomplete budget monitoring returns are regularly provided to the Chamberlain's Department from Police. This may be a result of high levels of staff turnover and lack of continuity at a senior level within the Police finance team due to staff illness and resignation.</p> <p>The Chamberlain's Department have raised concerns about the assumptions used in the Police MTFS and are planning to revisit the MTFS to address these issues and to ensure that the financial position is sustainable over the medium term.</p> <p>We consider that there are deficiencies in the robustness and accuracy of the information being provided by the City Police Finance team to the Corporation of London's Chamberlain's department.</p> <p>However, as the Chamberlain's Department is providing assistant to strengthen financial management arrangements in the City Police Finance team and the Corporation has allocated additional financial support from the City Fund in the short term to address funding gaps, we are content that this does not materially impact on the overall arrangements of the Corporation's City Fund to secure economy, efficiency and effectiveness in its use of resources.</p> |

USE OF RESOURCES

| RISK AREA | RISK DESCRIPTION AND WORK PERFORMED | AUDIT FINDINGS AND CONCLUSION |
|---|--|--|
| <p>2 Sustainable finances (City Fund)</p> | <p>The City Fund is currently forecasting a better than budget position of £1.5 million in 2017/18 which is mainly due to additional income from positive box office performances at the Barbican.</p> <p>Extra business rates income, combined with an increase in anticipated rents from the fund's investment properties and additional interest on cash balances, has allowed cost pressures to be accommodated and the inclusion of additional funding to meet Member priorities and initiatives, whilst still leaving the fund in surplus for 2017/18 and 2018/19.</p> <p>The fund moves into deficit from 2019/20 onwards due to the inclusion of costs for the Museum of London and the Combined Courts relocation projects. This assumes that the preference will be to utilise City Fund reserves prior to borrowing to fund these projects, though this is subject to the overall funding strategies for the projects, which are yet to be agreed.</p> <p>The MTFs is based on key income and expenditure assumptions as well as significant savings/ income generation proposals within service budgets. If key assumptions and savings plans have not been based on reliable data or have been overly optimistic the financial position could deteriorate over the medium term.</p> | <p>We have reviewed the assumptions used in preparing the MTFs for the City Fund and are content that cost pressures and income growth assumptions are reasonable.</p> <p>We note that Internal audit carried out a review of the MTFs in spring 2018 and gave a substantial assurance rating.</p> <p>The City Fund MTFs shows a surplus for 2018/19 but then forecasts a budgeted deficit over the following three years through planned withdrawal from reserves of £103 million to fund the Museum of London and Combined Courts Relocation projects. The City Fund may choose to make use of capital borrowing rather than revenue funding for some of these costs as they crystallise should the need arise. The City Fund currently holds reserves of £122 million.</p> <p>We consider that there are appropriate arrangements in place with regard to sustainable finances for City Fund.</p> |

APPENDICES

APPENDIX I: AUDIT DIFFERENCES

We are required to bring to your attention audit differences identified during the audit, except for those that are clearly trivial, that the Audit and Risk Committee is required to consider. This includes: audit differences that have been corrected by management; and those that remain uncorrected along with the effect that they have individually, and in aggregate, on the financial statements.

ADJUSTED AUDIT DIFFERENCES

Our audit has not identified any material misstatements.

UNADJUSTED AUDIT DIFFERENCES

We note below the unadjusted audit differences identified by our audit work which would increase the surplus on the provision of services for the year by £2.16 million (or £4.63 million including the projected error across all GRNIs). The depreciation error and NDR appeals provision errors would not impact on the General Fund balance this year as these are reversed to other reserves.

You consider these identified misstatements to be immaterial in the context of the financial statements taken as a whole. We concur with this judgement however we also request that you correct them even though not material.

- Two errors in the calculation of the provision for NDR appeals including an error in the formula that reduces the provision by £4.1 million and re-categorisation of appeal type for a number of appeals that increases the provision by £1.4 million. The net error is an overstatement of the appeals provision and understatement of the surplus for the year of £2.7 million in the collection fund and the City Fund's share included in the CIES of £0.81 million based on the 30% share of business rates.
- We believe that management has been overly prudent in providing for 100% of 2017 rating list appeals and that the provision amount, while not material, may be overstated by a non-trivial amount. We estimate that the potential impact on the Corporation's CIES where the amount provided is beyond a reasonable range could be up to £0.35 million.
- Error in the deprecation rate used resulting in £0.16 million overstatement of deprecation cost (and understatement of assets) and overstatement of the charge to the CIES for the year.
- Errors found where accrued expenditure for open purchase orders had been recorded as receipted but not invoiced (GRNIs) but where the orders had only been partly fulfilled. Our testing of 14 items with a value of £2.69 million identified 6 items totalling £0.84 million should not have been included as accrued expenditure. We have projected potential additional errors across total of GRNIs at £2.47 million.

APPENDIX I: AUDIT DIFFERENCES

| | £m | INCOME AND EXPENDITURE | | STATEMENT OF FINANCIAL POSITION | |
|--|------------|------------------------|----------|---------------------------------|----------|
| | | DR £m | CR £m | DR £m | CR £m |
| Surplus on the provision of services for the year before adjustments | 72.8 | | | | |
| DR NDR appeals provision | | | | 0.8 | |
| CR Taxation and non-specific Grant income | 0.8 | | 0.8 | | |
| <i>Impact of incorrect provision calculation</i> | | | | | |
| DR Property, plant and equipment (depreciation) | | | | 0.1 | |
| CR Depreciation charged to Net Cost of service | 0.1 | | 0.1 | | |
| <i>Impact of incorrect depreciation rate being used</i> | | | | | |
| DR NDR appeals provision | | | | 0.4 | |
| CR Taxation and non-specific Grant income | 0.4 | | 0.4 | | |
| <i>Impact of excessive NDR appeals provision on 2017 rating list</i> | | | | | |
| DR Payables (Accruals) factual error | | | 0.8 | | |
| DR Payables (Accruals) extrapolated error | | | 2.5 | | |
| CR Expenditure factual and extrapolated error | 3.3 | 3.3 | | | |
| <i>Impact of extrapolated errors found in Payables Accruals</i> | | | | | |
| TOTAL UNADJUSTED AUDIT DIFFERENCES | 4.6 | | | | |
| Surplus on the provision of services if adjustments accounted for | 77.4 | | | | |

APPENDIX I: AUDIT DIFFERENCES

| IMPACT ON GENERAL FUND AND HRA BALANCES | GENERAL FUND BALANCE £000s | HRA BALANCE £000s |
|---|-------------------------------|----------------------|
| Balances before adjustments | 122.3 | 4.5 |
| Adjustments to CIES above | 4.6 | 0 |
| Adjustments via movement in Reserves Statement: | | |
| - Collection Fund Adjustment Account | (1.2) | 0 |
| - Capital Financing Reserve | (0.1) | 0 |
| BALANCES AFTER ADJUSTMENTS | 125.6 | 4.5 |

UNADJUSTED DISCLOSURE MATTERS

No remaining uncorrected disclosures.

APPENDIX II: RECOMMENDATIONS AND ACTION PLAN

Key: ■ Significant risk ■ Other deficiency in internal control ■ Other observations

| AREA | OBSERVATION AND IMPLICATION | RECOMMENDATION | MANAGEMENT RESPONSE | RESPONSIBLE OFFICER | TIMING |
|--|--|--|---|--|------------------------------------|
| STATEMENT OF ACCOUNTS AND FINANCIAL STATEMENTS | | | | | |
| ■ NNDR Appeals provision 2017 valuation | The provision on the 2017 valuation appeals received to date has been made at 100% due to the Authority not having any settled claims on the 2017 valuation. | The Corporation should review any settlement data available to ensure that the provision is based on expected settlements rather than a worse-case scenario. | The Check, Challenge, Appeal process for NNDR appeals means appeals received are more likely to be settled than in previous years. This will be kept under review. | Head of Revenues | Mar 2019 |
| USE OF RESOURCES | | | | | |
| ■ City Police financial planning | Internal audit and the Chamberlain's Department have identified weaknesses in the Budget setting and monitoring process in relation to City of London Police | Management should ensure that they carry out the proposed review of the Police MTFS and budget setting and monitoring process as soon as possible so that a confirmed position is available to enable plans to be drawn up to assist the force in moving forward on a solid financial footing. | A review of the MTFS assumptions will be completed in Autumn 2018. The Deputy Chamberlain and Assistant Commissioner have discussed the expected timetable. Budget monitoring will be submitted on time. | Deputy Chamberlain Assistant Commissioner | Dec 2018 Throughout 2018/19 |

APPENDIX II: RECOMMENDATIONS AND ACTION PLAN

We have followed up on the recommendations that we raised in the prior year:

| AREA | OBSERVATION AND IMPLICATION | RECOMMENDATION | MANAGEMENT RESPONSE | RESPONSIBLE OFFICER | TIMING |
|---|--|--|--|---|---|
| Changes in presentation of the financial statements | <p>The financial statements includes an analysis of income by its nature (i.e fees & charges, grant income, interest and investment income, business rate income etc), in note 5.</p> <p>However, there is not an analysis of how this income is split between committees as required by the CIPFA Code.</p> | We recommend that this analysis is disclosed in the financial statements. | This note has been included in the 2017/18 financial statements as we are confident this is Code compliant in conjunction with the expenditure and funding analysis in note 4. | Deputy Director Financial Services | September 2017 |
| Creditors police seized funds | <p>The City fund has recognised £35 million (£3.1 million in 2015/16), of creditors in respect of police seized funds as it is considered that the City Fund has a right to the assets (cash seized), until instructed otherwise by the Court.</p> <p>We identified that there were 104 police seized funds (classified as creditors) balances amounting to £1.6 million relating to pre 1 April 2015 seizures and only three of these account balances had moved in the two years to 31 March 2017. During 2016/17 a further 46 seizures had occurred amounting to £13.1 million, the largest of which, £10.9 million was repaid after 31 March 2017.</p> | <p>We recommend that a review of police funds over two years old is carried out to determine if these funds are still held by the City Fund and/or whether the Police can apply to the Court to release these funds.</p> <p>We also recommend that given the value of the seized funds further details of why the City Fund has the right to the asset should be included in the management's judgements disclosure and further detail of the types of funds held should be disclosed within the creditors note.</p> | <p>This work is in progress and is subject to a further review by Internal Audit.</p> <p>Appropriate text has been included in the 2017/18 financial statements.</p> | <p>Commissioner</p> <p>Deputy Director Financial Services</p> | <p>January 2018</p> <p>January 2018</p> |

APPENDIX II: RECOMMENDATIONS AND ACTION PLAN

| AREA | OBSERVATION AND IMPLICATION | RECOMMENDATION | MANAGEMENT RESPONSE | RESPONSIBLE OFFICER | TIMING |
|-------------------|---|--|---------------------|---|--------------|
| Barbican journals | <p>Our testing identified the following:</p> <ul style="list-style-type: none"> • Posting of Barbican entries in to Oracle (main accounting system) seems to be overly complicated with multiple journal entries being created, reversed, recreated, re-reversed repeatedly many on the same day or within a few days of the entry being made. • We identified that income from events is often not posted to revenue codes for several months after the event has closed. • We also noted that the Barbican finance team have limited access to reporting functions on the ENTA & Revel systems, which meant there was difficulty running reports to support our sample testing. <p>We understand that the City are currently tendering for a new ticketing system which should address these issues.</p> | <p>We recommend that the process and timing of Barbican journal entries are reviewed to ensure that unnecessary journal posting are reduced and journals are posted on a timely basis.</p> <p>We also recommend that the reporting functions set up is reviewed for the Barbican finance team to ensure that they have the correct level of access in order to perform required day-to-day activities.</p> | Agreed | Head of Finance Barbican and Deputy Director Financial Services | January 2018 |

APPENDIX III: MATERIALITY

| MATERIALITY - FINAL AND PLANNING | | |
|---|------------|------------|
| | FINAL | PLANNING |
| City Fund overall Materiality | 24,400,000 | 23,400,000 |
| Specific materiality for other financial statement areas: | | |
| - Impact on revenue resources through the Comprehensive income and expenditure statement (CIES) and Movement in reserves statement (MiRS) | 6,375,000 | 5,800,000 |
| Clearly trivial threshold: | | |
| - Overall materiality | 488,000 | 468,000 |
| - Specific materiality | 127,500 | 116,000 |

Materiality for the City Fund overall materiality was based on 1% of the aggregate balance of property, plant and equipment and investment properties. This is because the City Fund has custody of significant public assets through its ownership of property assets and investments that are used to generate income to support the local authority services provided by the Corporation. These capital and investment balances form the largest part of the balance sheet. We consider that the balance sheet is of primary interest to the reader of the financial statements (Members of the City of London Corporation) and therefore we use the total value of property, plant and equipment, investment properties and investments as a suitable value for materiality.

Specific materiality was set using a lower level of materiality at 1.5% of gross expenditure to income and expenditure transactions in the Comprehensive income and expenditure statement (CIES) and Movement in reserves statement (MiRS) that impact on revenue resources to reduce the risk of material misstatements. While the balance sheet is of primary interest to the reader of the financial statements, we consider that a misstatement at a lower level through revenue expenditure would be material where this may impact on setting future council tax or HRA rent levels.

We had no reason to revise our final materiality percentage levels. We have, however, applied these levels to balances and transactions as at 31 March 2018 reported in the draft financial statements which has resulted in a change to the materiality amounts.

APPENDIX IV: INDEPENDENCE

Under ISAs (UK) and the FRC's Ethical Standard, we are required as auditors to confirm our independence.

We have embedded the requirements of the Standards in our methodologies, tools and internal training programmes. Our internal procedures require that audit engagement leads are made aware of any matters which may reasonably be thought to bear on the integrity, objectivity or independence of the firm, the members of the engagement team or others who are in a position to influence the outcome of the engagement. This document considers such matters in the context of our audit for the year ended 31 March 2018.

Details of services, other than audit, provided by us to the Corporation during the period and up to the date of this report were provided in our Audit Plan. These services have been approved by the Chamberlain.

Details of rotation arrangements for key members of the audit team and others involved in the engagement were provided in our Audit Plan.

We have not identified any other relationships or threats that may reasonably be thought to bear on our objectivity and independence.

We confirm that the firm, the engagement team and other partners, directors, senior managers and managers conducting the audit comply with relevant ethical requirements including the FRC's Ethical Standard and are independent of the Corporation.

Should you have any comments or queries regarding any independence matters we would welcome their discussion in more detail.

APPENDIX V: FEES SCHEDULE

| | 2017/18 FINAL £ | 2017/18 PLANNED £ | 2016//17 FINAL £ | EXPLANATION FOR VARIANCES |
|---|-----------------------|-------------------------|------------------------|------------------------------|
| Code audit fee | 86,383 ⁽¹⁾ | 86,383 | 86,383 | As per PSAA Scale Fee |
| Fee for reporting on the housing benefits subsidy claim | 11,396 | 11,396 | 11,205 | As per PSAA Scale Fee |
| TOTAL AUDIT AND CERTIFICATION FEES | 97,779 | 97,779 | 97,588 | |
| Fees for reporting on other government grants: | | | | |
| • Pooling of housing capital receipts return | 2,340 | 2,340 | 2,340 | |
| • Teachers' Pension (local education authority) | 4,500 | 4,500 | 4,500 | |
| • Teachers' Pension (Centre for Young Musicians -City's Cash) | 4,500 | 4,500 | 4,500 | |
| Fees for other non-audit services | Nil | Nil | Nil | |
| NON-AUDIT ASSURANCE SERVICES | 11,340 | 11,340 | 11,340 | |
| TOTAL ASSURANCE SERVICES | 109,119 | 109,119 | 108,928 | |

⁽¹⁾ Additional work has been required this year for investment property valuations, police pensions for the triennial valuation data submission, and extended testing where errors were found in the initial testing. We will agree with management the impact on this addition work on the final fees.

APPENDIX VI: DRAFT LETTER OF REPRESENTATION

TO BE TYPED ON CLIENT HEADED NOTEPAPER

BDO LLP
55 Baker Street
London
W1U 7EU

[XX] July 2018

Dear Sirs

Financial statements of City of London Corporation City Fund for the year ended 31 March 2018

We confirm that the following representations given to you in connection with your audit of the Corporation's City Fund financial statements for the year ended 31 March 2018 are made to the best of our knowledge and belief, and after having made appropriate enquiries of other officers and members of the Corporation.

The Chamberlain has fulfilled his responsibilities for the preparation and presentation of the financial statements as set out in the Accounts and Audit Regulations 2015 and Statement of Responsibilities of Auditors and Audited Bodies within Chapter 2 of the Code of Audit Practice published by the National Audit Office in April 2015, and in particular that the financial statements give a true and fair view of the financial position of the Corporation as of 31 March 2018 and of its income and expenditure and cash flows for the year then ended in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom (the Code).

We have fulfilled our responsibilities on behalf of the Corporation, as set out in the Accounts and Audit Regulations 2015, to make arrangements for the proper administration of the Corporation's financial affairs, to conduct a review at least once in a year of the effectiveness of the system of internal control and approve the Annual Governance Statement, to approve the Statement of Accounts (which include the financial statements), and for making accurate representations to you.

We have provided you with unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence. In addition, all the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the Corporation's City Fund have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all management and other meetings have been made available to you.

In relation to those laws and regulations which provide the legal framework within which the Corporation's business is conducted and which are central to our ability to conduct our business, we have disclosed to you all instances of possible non-compliance of which we are aware and all actual or contingent consequences arising from such instances of non-compliance.

There have been no events since the balance sheet date which either require changes to be made to the figures included in the financial statements or to be disclosed by way of a note. Should any material events of this type occur, we will advise you accordingly.

We are responsible for adopting sound accounting policies, designing, implementing and maintaining internal control, to, among other things, help assure the preparation of the financial statements in conformity with generally accepted accounting principles and preventing and detecting fraud and error.

We have considered the risk that the financial statements may be materially misstated due to fraud and have identified no significant risks.

To the best of our knowledge we are not aware of any fraud or suspected fraud involving management or employees. Additionally, we are not aware of any fraud or suspected fraud involving any other party that could materially affect the financial statements.

To the best of our knowledge we are not aware of any allegations of fraud or suspected fraud affecting the financial statements that have been communicated by employees, former employees, analysts, regulators or any other party.

We attach a schedule showing accounting adjustments that you have proposed, which we acknowledge that you request we correct, together with the reasons why we have not recorded these proposed adjustments in the financial statements. In our opinion, the effects of not recording such identified financial statement misstatements are, both individually and in the aggregate, immaterial to the financial statements.

We have disclosed to you the identity of all related parties and all the related party relationships and transactions of which we are aware. We have appropriately accounted for and disclosed such relationships and transactions in accordance with the applicable financial reporting framework.

We have no plans or intentions that may materially affect the carrying value and where relevant, the fair value measurement, or classification of assets or liabilities reflected in the financial statements.

a) Pension fund assumptions

We confirm that the actuarial assumptions underlying the valuation of the Local Government Pension Scheme (LGPS) and Police pension scheme liabilities, as applied by the scheme actuary, are reasonable and consistent with our knowledge of the business. These assumptions include:

- Rate of inflation (CPI): 2.3%
- Rate of increase in salaries: 3.8%
- Rate of increase in pensions: 2.3%
- Rate of discounting scheme liabilities: 2.55%
- LGPS commutation take up option: 50%

We also confirm that the actuary has applied up-to-date mortality tables for life expectancy of scheme members in calculating scheme liabilities.

b) Valuation of housing stock, other land and buildings and investment properties

We are satisfied that the useful economic lives of the housing stock and other land and buildings, and their constituent components, used in the valuation of the housing stock and other land and buildings, and the calculation of the depreciation charge for the year, are reasonable.

We confirm that the valuations applied to corporation dwellings and other land and buildings revalued in the year, as provided by the valuer and accounted for in the financial statements, are reasonable and consistent with our knowledge of the business and current market prices.

We are satisfied that investment properties have been appropriately assessed as Level 2 or Level 3 on the fair value hierarchy for valuation purposes and valued at fair value, based on highest and best use.

c) Allowance for non-collection of receivables

We are satisfied that the impairment allowances for non-domestic rates, housing rent and sundry debt arrears are reasonable, based on collection rate data.

d) Non domestic rates appeals provision

We are satisfied that the provision recognised for non-domestic rates appeals is materially correct, and the calculation of historical appeals are consistent with those advised to me by the Valuation Office Agency. We confirm that the successful rates applied to outstanding appeals as at 31 March 2018 are consistent with our knowledge of the business.

We have disclosed all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements and these have been disclosed in accordance with the requirements of accounting standards.

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

We confirm that the financial statements are free of material misstatements, including omissions.

We acknowledge our legal responsibilities regarding disclosure of information to you as auditors and confirm that so far as we are aware, there is no relevant audit information needed by you in connection with preparing your audit report of which you are unaware. The Chamberlain and each member has taken all the steps that they ought to have taken as a director or member to make themselves aware of any relevant audit information and to establish that you are aware of that information.

Yours faithfully

Dr Peter Kane

Chamberlain of London

APPENDIX VII: DRAFT AUDIT REPORT

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE CITY OF LONDON CORPORATION CITY FUND

UNMODIFIED STANDARD FINANCIAL STATEMENTS OPINION AND USE OF RESOURCES CONCLUSION

APPENDIX VIII: 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 welcomes feedback from external bodies and is committed to implementing all 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 companies), the firm undertakes a thorough annual internal Audit Quality Assurance Review and as a 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.

More details can be found in our Transparency Report at www.bdo.co.uk



FOR MORE INFORMATION:

LEIGH LLOYD-THOMAS
Engagement lead

T: 020 7893 2616
E: leigh.lloyd-thomas@bdo.co.uk

FRANCESCA PALMER
Manager

T: 01473 320739
E: francesca.palmer@bdo.co.uk

The matters raised in our report prepared in connection with the audit are those we believe should be brought to the attention of the organisation. They do not purport to be a complete record of all matters arising. No responsibility to any third party is accepted.

BDO LLP is a corporate establishment under the Limited Liability Partnership Act 2000 and a UK Member Firm of BDO International. BDO Northern Ireland, a separate partnership, operates under a licence agreement. BDO LLP and BDO Northern Ireland are both separately authorised and regulated by the Financial Conduct Authority to conduct investment business.

Copyright ©2018 BDO LLP. All rights reserved.

www.bdo.co.uk

