

Councillor John Worrow
Chair, Governance & Audit Committee
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Dear Councillor Worrow,

The purpose of this letter is to contribute towards the effective two-way communication between auditors and the Council's Governance & Audit Committee 'those charged with governance'. The report covers some important areas of the auditor risk assessment where we are required to make inquiries of the Governance & Audit Committee ("Committee") under auditing standards.

Background

Under International Standards on Auditing (UK and Ireland) (ISA(UK&I)) auditors have specific responsibilities to communicate with the Committee. ISA(UK&I) emphasise the importance of two-way communication between the auditor and the Committee and also specify matters that should be communicated.

This two-way communication assists both the auditor and the Committee in understanding matters relating to the audit and developing a constructive working relationship. It also enables the auditor to obtain information relevant to the audit from the Committee and supports the Committee in fulfilling its responsibilities in relation to the financial reporting process.

Communication

As part of our risk assessment procedures we are required to obtain an understanding of management processes over the following areas:

- fraud (Appendix I)
- laws and regulations (Appendix II)
- going concern (Appendix III) and

how the Governance & Audit Committee oversees management's processes (Appendix IV).

This letter includes a series of questions on each of these areas and the response we have received from the Council's management. The Committee should consider whether these responses are consistent with its understanding and whether there are any further comments it wishes to make.

Please could you provide a response by 26 April 2013 and do contact me if you wish to discuss anything in relation to this request.

Yours sincerely

Lisa Robertson
Audit Manager
For Grant Thornton UK LLP

Matters in relation to fraud

ISA(UK&I)240 covers auditors responsibilities relating to fraud in an audit of financial statements. The primary responsibility to prevent and detect fraud rests with both the Governance & Audit Committee and management. Management, with the oversight of the Governance & Audit Committee, needs to ensure a strong emphasis on fraud prevention and deterrence and encourage a culture of honest and ethical behaviour.

As part of its oversight, the Governance & Audit Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error. We are required to maintain professional scepticism throughout the audit, considering the potential for management override of controls.

As part of our audit risk assessment procedures we are required to consider risks of fraud. This includes considering the arrangements management has put in place with regard to fraud risks including:

- assessment that the financial statements could be materially misstated due to fraud
- process for identifying and responding to risks of fraud, including any identified specific risks
- communication with the Governance & Audit Committee regarding its processes for identifying and responding to risks of fraud
- communication to employees regarding business practices and ethical behaviour.

We need to understand how the Governance & Audit Committee oversees the above processes. We are also required to make inquiries of both management and the Governance & Audit Committee as to their knowledge of any actual, suspected or alleged fraud. These areas have been set out in the fraud risk assessment questions below together with responses from the Council's management.

Question	Management response
<p>Has the Council assessed the risk of material misstatement in the financial statements due to fraud?</p> <p>What are the results of this process?</p>	<p>Yes the Council has assessed this risk and considers the risk to be negligible</p>
<p>What processes does the Council have in place to identify and respond to risks of fraud?</p>	<p>The Council operates a robust key control framework within the financial procedures that has met with favourable internal audit reports. This includes ensuring that the finance team are adequately skilled and alert to anomalies that could indicate a misstatement due to fraud; a devolved budget management system which means that managers have sight of financial transactions and can therefore identify any rogue payments; senior management reviews of the financial statements are also undertaken to aid the identification of material inconsistencies.</p>

<p>Have any specific fraud risks, or areas with a high risk of fraud, been identified and what has been done to mitigate these risks?</p>	<p>We are aware that the possibility of fraud occurring could be higher in the current economic climate. This is particularly so within the benefits area and therefore specialised staff are employed in this area to deal with fraud.</p>
<p>Are internal controls, including segregation of duties, in place and operating effectively? If not, where are the risk areas and what mitigating actions have been taken?</p>	<p>Managers are aware of the need for segregation of duties and these are in place wherever resources allow. The Internal Audit Plan looks at the key internal controls on a regular basis and the results of these audits show that the Council has good control measures in place. The authorised signatory forms limit access to systems and certain processes dependent on the nature of an individual's role, thus preventing someone from having inappropriate access to the financial systems. Staff receive regular briefings on being alert to fraud.</p>
<p>Are there any areas where there is a potential for override of controls or inappropriate influence over the financial reporting process (for example because of undue pressure to achieve financial targets)?</p>	<p>No</p>
<p>Are there any areas where there is a potential for misreporting override of controls or inappropriate influence over the financial reporting process?</p>	<p>No</p>
<p>How does the Governance & Audit Committee exercise oversight over management's processes for identifying and responding to risks of fraud? What arrangements are in place to report fraud issues and risks to the Governance & Audit Committee?</p>	<p>The Governance and Audit Committee receives regular updates from Internal Audit on the results of their audit reviews on the Council's key internal controls. Any instances of fraud are reported to the Governance and Audit Committee. Members of this committee receive regular training on anti-fraud measures and regularly reviews the Council's anti-fraud and corruption policy.</p>
<p>How does the Council communicate and encourage ethical behaviour of its staff and contractors?</p>	<p>The Council's commitment to good governance and anti-fraud principles are communicated using the Council's intranet site, Managers' development sessions, staff and member development sessions</p>
<p>How do you encourage staff to report their concerns about fraud? Have any significant issues been reported?</p>	<p>The Council's whistleblowing policy is widely publicised and officers feel comfortable at raising concerns where appropriate. Staff are exoected to raise</p>

	concerns whenever they suspect something untoward is going on. The whistleblowing policy has been used by staff to identify suspected fraud and all such instances have been fully investigated.
Are you aware of any related party relationships or transactions that could give rise to risks of fraud?	Members are expected to disclose any transactions they have entered into of a related party nature. I am not aware of any such relationships or transactions that have given rise to risks of fraud.
Are you aware of any instances of actual, suspected or alleged, fraud, either within the Council as a whole or within specific departments since 1 April 2012?	No

Matters in relation to laws and regulations

ISA(UK&I)250 requires us to consider the impact of laws and regulations in an audit of the financial statements.

Management, with the oversight of the Governance & Audit Committee, is responsible for ensuring that the Council's operations are conducted in accordance with laws and regulations including those that determine amounts in the financial statements.

As auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error, taking into account the appropriate legal and regulatory framework. As part of our risk assessment procedures we are required to make inquiries of management and the Governance & Audit Committee as to whether the entity is in compliance with laws and regulations. Where we become aware of information of non-compliance or suspected non-compliance we need to gain an understanding of the non-compliance and the possible effect on the financial statements.

Risk assessment questions have been set out below together with responses from management.

Question	Management response
<p>What arrangements does the Council have in place to prevent and detect non-compliance with laws and regulations?</p>	<p><u>Appointment of Monitoring Officer</u></p> <p>The Council has appointed a qualified solicitor as its Monitoring Officer whose statutory duties included reporting to Council or Cabinet (as appropriate) if he considers that any proposal decision or omission would give rise to unlawfulness or maladministration. The Monitoring Officer is also a member of the Council's Senior Management Team and is therefore able to advise on the legal implications of key operational and strategic decisions</p> <p><u>Complementary Role of the Chief Financial Officer</u></p> <p>The Monitoring Officer is supported in the discharge of his role by the Chief Executive in her statutory role as the Council's Chief Financial Officer (CFO). The duties of the CFO include ensuring the lawfulness of financial decisions as well as the maintenance of financial prudence and propriety. The CFO, Deputy CFO and Monitoring Officer are</p>

	<p>all members of Senior Management Team and support the work of the Governance & Audit Committee.</p> <p><u>Legal Service</u></p> <p>The Council's In House Legal Service consist of three solicitors and two legal executives who provide a range of regulatory and transactional services and whose roles includes ensuring that the Council's actions are lawful.</p> <p><u>CPD Training</u></p> <p>The Council' Monitoring Officer, Legal Services Manager, Litigation Solicitor, Assistant Litigation Solicitor and Senior Legal Executive are all required to undertake a minimum of 18 hours Continual Professional Development training per annum to ensure they retain the ability to advise competently on legal risk and compliance.</p> <p><u>Member Decision Making</u></p> <p>The Standard template report to Cabinet and Council includes 'Legal Implications' which are completed or approved by a member of the Council's s in-house Legal Team in order that legal risk and compliance is considered as a normal part of the member decision making process. In addition the Monitoring Officer attends Council and Cabinet Meetings and other qualified solicitors attend meetings of the Council's Regulatory Committees - the Planning Committee, Licensing Panel and the Licensing Sub Committee.</p>
How is the Governance & Audit Committee provided with assurance that all relevant laws and regulations have been complied with?	As set out above.
Have there been any instances of non-compliance or suspected non-compliance with law and regulation since 1 April 2012, or earlier with an on-going impact on the 2012/13 financial statements?	No.

<p>What arrangements does the Council have in place to identify, evaluate and account for litigation or claims?</p>	<p>All claims against the Council which are not covered by insurance are managed by the Legal Service. The advice and/or representation of Counsel is sought as necessary and other experts appointed where needed to defend or settle claims. Where Legal consider that a claim against the Council is likely to succeed, they will advise on an appropriate financial settlement including the making Part 36 Offers in order to protect the public purse and minimise the Council's financial exposure.</p>
<p>Is there any actual or potential litigation or claims that would affect the financial statements?</p>	<p>The decision of the Council to place a temporary suspension on the movement of live animal resulted in judicial review proceedings and an injunction and damages application against the Council. The judicial review proceedings and injunction claim have since been settled by consent order but the damages claim has been referred to the Chancery Division of the High Court. The Claimants have stated the damages claim at £1.4 million but given that leading Counsel has advised that the Council has a number of strongly arguable technical defences which, if successful, would entirely defeat the claim, it is not intended to make any provision for this claims in the accounts.</p>
<p>Have there been any reports from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?</p>	<p>No</p>

Matters in relation to going concern

ISA(UK&I)570 covers auditor responsibilities in the audit of financial statements relating to management's use of the going concern assumption in the financial statements.

The going concern assumption is a fundamental principle in the preparation of financial statements. Under this assumption entities are viewed as continuing in business for the foreseeable future. Assets and liabilities are recorded on the basis that the entity will be able to realise its assets and discharge its liabilities in the normal course of business.

The code of practice on local authority accounting requires an authority's financial statements to be prepared on a going concern basis. Although the Council is not subject to the same future trading uncertainties as private sector entities, consideration of the key features of the going concern provides an indication of the Council's financial resilience.

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

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

Question	Management response
Does the Council have procedures in place to assess the Council's ability to continue as a going concern?	<p>The Council reviews its financial position on a monthly basis as part of its budget monitoring processes. If an overall budget overspend is highlighted as part of this process, then every effort is made by managers to bring spend back within a balanced budget position.</p> <p>The Medium Term Financial Plan reviews the Council's financial position over a four year period and presents a balanced budget position over this time frame.</p> <p>A comparison of assets to liabilities is considered as part of the balance sheet review and this shows that the Council is able to discharge its liabilities over the normal course of business.</p>
Is management aware of the existence of other events or conditions that may cast doubt on the Council's ability to continue as a going concern?	No

<p>Are arrangements in place to report the going concern assessment to the Governance & Audit Committee?</p>	<p>This is considered as part of the committee's scrutiny of the Statement of Accounts</p>
<p>Are the financial assumptions in that report (eg future levels of income and expenditure) consistent with the Council's Business Plan and the financial information provided to the Council throughout the year?</p>	<p>The Medium Term Financial Plan assumptions are updated as and when financial circumstances change over the course of the year</p>
<p>Are the implications of statutory or policy changes appropriately reflected in the Business Plan, financial forecasts and report on going concern?</p>	<p>The Medium Term Financial Plan reflects the financial impact of any statutory or policy changes</p>
<p>Have there been any significant issues raised with the Governance & Audit Committee during the year which could cast doubts on the assumptions made? (Examples include adverse comments raised by internal and external audit regarding financial performance or significant weaknesses in systems of financial control).</p>	<p>No</p>
<p>Does a review of available financial information identify any adverse financial indicators including negative cash flow? If so, what action is being taken to improve financial performance?</p>	<p>No</p>
<p>Does the Council have sufficient staff in post, with the appropriate skills and experience, particularly at senior manager level, to ensure the delivery of the Council's objectives? If not, what action is being taken to obtain those skills?</p>	<p>Staffing levels and skills are reviewed on a regular basis as part of the Council's ongoing financial planning</p>

How the Governance & Audit Committee oversees management's processes

- To comply with International Auditing Standards, each year we need to refresh our understanding of how the Governance & Audit Committee gains assurance over management processes and arrangements.

Question	Governance & Audit Committee response
<p>How does the Governance & Audit Committee oversee management's processes in relation to:</p> <ul style="list-style-type: none"> • carrying out an assessment of the risk the financial statements may be materially misstated due to fraud or error • identifying and responding to the risk of breaches of internal control • identifying and responding to risks of fraud in the organisation (including any specific risks of fraud which management have identified or that have been brought to its attention, or classes of transactions, account balances, or disclosure for which a risk of fraud is likely to exist) • communicating to employees its views on appropriate business practice and ethical behaviour (for example by updating, communicating and monitoring against the codes of conduct)? 	
<p>Do you have knowledge of any actual, suspected or alleged frauds? If so, please provide details.</p>	
<p>How does the Governance & Audit Committee gain assurance that all relevant laws and regulations have been complied with?</p>	

<p>Are you aware of any actual or potential litigation or claims that would affect the financial statements?</p>	
<p>Are you aware of any whistleblower tips or complaints received?</p>	
<p>How has the Governance & Audit Committee satisfied itself that it is appropriate to adopt the going concern basis in preparing the financial statements?</p>	