



**CITY OF LONDON CORPORATION -
CITY FUND AND PENSION FUND**

ANNUAL AUDIT LETTER

Audit for the year ended 31 March 2018

14 August 2018

EXECUTIVE SUMMARY

PURPOSE OF THE LETTER

This annual audit letter summarises the key issues arising from the work that we have carried out at the City of London Corporation for the year ended 31 March 2018.

It is addressed to the Corporation but is also intended to communicate the key findings we have identified to key external stakeholders and members of the public.

RESPONSIBILITIES OF AUDITORS AND THE CORPORATION

It is the responsibility of the Corporation to ensure that proper arrangements are in place for the conduct of its business and that public money is safeguarded and properly accounted for.

Our responsibility is to plan and carry out an audit that meets the requirements of the National Audit Office's (NAO's) Code of Audit Practice (the Code). Under the Code, we are required to report on:

- Our opinion on the City Fund's financial statements
- Our opinion on the Pension Fund's financial statements
- Whether the Corporation, in respect of the City Fund and Pension Fund, has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

We recognise the value of your co-operation and support and would like to take this opportunity to express our appreciation for the assistance and co-operation provided during the audit.

BDO LLP

AUDIT CONCLUSIONS

FINANCIAL STATEMENTS

We issued our unmodified opinions on the City Fund and Pension Fund's financial statements on 31 July 2018.

We identified errors above our reporting threshold for the City Fund that would increase the surplus on the provision of services for the year by £4.63 million. These errors related to NDR appeals provisions, depreciation charge for the year and accruals for expenditure where the goods had not been received by the Corporation at the year end. We extrapolated the potential error across all Goods Received Not Invoiced amounts and were satisfied that the potential error would not be material.

For the Pension Fund we identified errors that would increase the value of investments by £0.49 million following revised valuations received from the fund managers.

These were not corrected by management as the amounts were not material.

USE OF RESOURCES

We issued our unmodified conclusion on the arrangements for securing economy, efficiency and effectiveness in the use of resources on 31 July 2018 in respect of the City Fund and Pension Fund.

The City Fund financial plans 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 currently holds reserves of £122 million. However, we noted weaknesses in the City Police's strategic financial planning arrangements and significant funding gaps in the medium terms to be addressed.

Overall, we consider that there are appropriate arrangements in place with regard to sustainable finances.

FINANCIAL STATEMENTS

OPINIONS

We issued our unmodified opinions on the City Fund and Pension Fund's financial statements on 31 July 2018.

This means we consider:

- The financial statements give a true and fair view of the financial position and its income and expenditure for the year
- Have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting 2017/18.

SCOPE OF THE AUDIT

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error.

This includes an assessment of whether the accounting policies are appropriate to the City Fund and Pension Fund's circumstances and have been consistently applied and adequately disclosed the reasonableness of significant accounting estimates, and the overall presentation of the financial statements.

OUR APPLICATION OF MATERIALITY

We apply the concept of materiality both in planning and performing our audit and in evaluating the effect of misstatements. We consider materiality to be the magnitude by which misstatements, including omissions, could influence the economic decisions of reasonably knowledgeable users that are taken on the basis of the financial statements.

The materiality for the City Fund's financial statements was set at £24.4 million. This was determined with reference to a benchmark 1% of the aggregate balance of property, plant and equipment and investment properties. We set a lower materiality level £6.375 million for the transactions included in the Income and Expenditure Account that impact on revenue reserves.

The materiality for the Pension Fund's financial statements was set at £9.88 million. This was determined with reference to a benchmark of net assets (of which it represents 1 per cent) which we consider to be one of the principal considerations for the pension fund in assessing financial performance. We set a lower materiality level £1.95 million for the transactions included in the Fund Account of the Pension Fund.

OUR ASSESSMENT OF RISKS OF MATERIAL MISSTATEMENT

Our audit was scoped by obtaining an understanding of the Corporation, in relation to the City Fund and Pension Fund, and its environment, including the system of internal control, and assessing the risks of material misstatement in the financial statements. We set out below the risks that had the greatest effect on our audit strategy, the allocation of resources in the audit, and the direction of the efforts of the audit team.

FINANCIAL STATEMENTS

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT	CONCLUSION
Management override of controls	<p>Under auditing standards, there is a presumed risk of management override of controls as management is in a unique position to manipulate accounting records to prepare fraudulent financial statements.</p> <p>We responded to this risk by testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements.</p> <p>We reviewed the accounting estimates for bias and evaluated whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud.</p> <p>We obtained an understanding of the business rationale for significant transactions that were outside the normal course of business for the Trust or appeared to be unusual.</p>	<p>No issues were identified by our audit work from our review of journals and review accounting estimates for management bias. We found no significant transactions that were outside the normal course of business or otherwise appear unusual.</p>

FINANCIAL STATEMENTS

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT	CONCLUSION
Revenue recognition	<p>Under auditing standards there is a presumption that income recognition presents a fraud risk.</p> <p>We responded to this risk by testing an increased sample of fees, charges and investment property rental income to underlying documentation to confirm the existence and accuracy of transactions throughout the year.</p> <p>We tested a sample of grants subject to performance conditions to confirm that conditions of the grant had been met before the income is recognised.</p> <p>We also tested a sample receipts either side of year end, to confirm that income has been recorded in the correct period and that all income that should have been recorded at year end has been.</p>	<p>Our testing confirmed that income was valid and agreed to underlying documentation, that grants were recognised only when performance conditions had been met, and income had been recorded in the correct period.</p>

FINANCIAL STATEMENTS

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT	CONCLUSION
Valuation of land, buildings and investment property	<p>Due to the significant value of the City Fund's property assets, and the high degree of estimation uncertainty, there is a significant risk over the valuation of land, buildings and investment properties where valuations are based on assumptions or where updated valuations have not been provided for a class of assets at the year-end.</p> <p>We responded to this risk by:</p> <ul style="list-style-type: none"> • Reviewing the instructions provided to the valuers and assessing their expertise. • Checking the accuracy and completeness of the source data used by the valuers. • Checking the basis of valuation for assets valued in year as appropriate. • Reviewed the reasonableness of assumptions used in the valuations against indices and price movements for classes of assets, and followed up valuation movements that appeared unusual against indices. • Estimated the potential movement on classes of assets that were not revalued in year to assess whether there is the potential for material movements since the last valuation. 	<p>The Corporation engaged external valuers to value the majority of property assets at 31 March 2018. This included valuation falls for dwellings of £10.9 million (-3.2%), land and buildings increases of £24.8 million (+8%) and investment property increases of £69.2 million (+4.8%).</p> <p>From our review of the instructions provided to the valuers and the valuers' reports we are satisfied that we can rely on their work.</p> <p>We confirmed that the basis of valuation for assets valued in year is appropriate based on the nature and use of the assets.</p> <p>No issues have been identified from our review of the source data provided to the valuer.</p> <p>Assumptions used and valuation movements were found to be reasonable.</p> <p>Our review confirmed that assets not subject to revaluation in year were not materially different to their carrying value.</p>

FINANCIAL STATEMENTS

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT	CONCLUSION
Valuation of pension liability (LGPS scheme and police scheme)	<p>There is a risk that membership data and cash flows provided to the actuary may not be correct, or the valuation uses inappropriate assumptions to value the liability.</p> <p>This is a significant risk due to the higher estimation uncertainty arising from the range of assumptions available to value the pension liability.</p> <p>We responded to this risk by:</p> <ul style="list-style-type: none"> • Agreeing the information provided to the actuary for contributions and investment returns for the year. • Agreeing data provided to the actuary for the triennial update for the police pension scheme. • Reviewing the reasonableness of the assumptions used in the calculation against other local government actuaries and other observable data. • Checking whether any significant changes in membership data have been communicated to the actuary. 	<p>The LGPS pension fund liability to pay future pensions increased by £21 million to £1,627 million. This increase was due to a marginal increase in life expectancy and a reduced discount rate, offset by lower future pay and pension increases. The overall LGPS net liability fell by £3.7 million following increased investment returns and the City Fund share decreased by £2.7 million to £302.2 million.</p> <p>The Police pension scheme liability increased by £42.9 million to £955.8 million. This key movements include reductions for financial assumptions (lower future pay and pension increases) and increases for life expectancy and experience losses arising from refreshed membership data used in the triennial valuation for 2017.</p> <p>We agreed the information provided to the actuary for the LGPS contributions paid and investment returns for the year.</p> <p>We also agreed the triennial dataset for police scheme members used for the 2017 triennial update of the police pension liability.</p> <p>Our review of assumptions used to estimate the value the pension liability were found to be reasonable. We used the PwC consulting actuary report for the review of the methodology of the actuary and reasonableness of the assumptions.</p> <p>There were no significant changes to staff numbers that would require additional communication with the actuary and potential amendment to the roll-forward data to the 2016 LGPS triennial valuation.</p>

USE OF RESOURCES

CONCLUSION	We issued our unmodified conclusion on the arrangements for securing economy, efficiency and effectiveness in its use of resources on 31 July 2018 in respect of the City Fund and Pension Fund.
	This means we consider that the Corporation, in respect of the City Fund and Pension Fund, has proper arrangements to: <ul style="list-style-type: none">• Ensure it took properly informed decisions• Deploy resources to achieve planned and sustainable outcomes for taxpayers and local people.

SCOPE OF THE AUDIT

We are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources.

As part of reaching our overall conclusion we consider the following sub criteria in our work: informed decision making, sustainable resource deployment, and working with partners and other third parties.

OUR ASSESSMENT OF SIGNIFICANT RISKS

Our audit was scoped by our cumulative knowledge brought forward from previous audits, relevant findings from work undertaken in support of the opinion on financial statements, reports from the Corporation including internal audit, information disclosed or available to support the annual governance statement, and information available from the risk registers and supporting arrangements.

We set out below the risks that had the greatest effect on our audit strategy, the allocation of resources in the audit, and the direction of the efforts of the audit team.

USE OF RESOURCES

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT	CONCLUSION
Financial sustainability	<p>The City Fund's Medium Term Financial Strategy (MTFS) is balanced in the medium term and includes savings and income generation proposals within service budgets. It does include significant drawdown from revenue reserves to support capital projects such as the relocation of the Museum of London and Combined Courts.</p> <p>The Police MTFS requires the use of its remaining revenue reserves to balance the budget and funding gaps in the coming years to be addressed through efficiencies and savings.</p> <p>For the Police budget, 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 MTFS for both City Fund and Police to assess the reasonableness of the assumptions and the delivery of the budgeted savings in the medium term.</p>	<p>The City Fund's 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 currently holds reserves of £122 million to support this capital investment.</p> <p>The assumptions used in preparing the City Fund's MTFS for cost pressures and income growth are reasonable.</p> <p>The Police budget for 2018/19 has been brought into balance through a combination of efficiency savings, slippage on schemes in 2017/18 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>We noted weaknesses in the Police's strategic financial planning arrangements and have some concerns that the significant funding gaps in the medium term will not be addressed by the efficiencies programme.</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>

APPENDIX

REPORTS ISSUED

We issued the following reports since our previous annual audit letter.

REPORT	DATE
Grant claims and certification 2016/17	17 January 2018
Audit plan Pension Fund 2017/18	12 February 2018
Audit plan City Fund 2017/18	15 February 2018
Audit completion report Pension Fund 2017/18	10 July 2018
Audit completion report City Fund 2017/18	31 July 2018

FEES

We are currently in discussion with management regarding final fees.

AUDIT AREA	FINAL FEES £	PLANNED FEES £
City Fund audit - PSAA scale fee	⁽¹⁾ TBC	86,383
Pension Fund audit - PSAA scale fee	21,000	21,000
Housing benefits subsidy certification fee	11,396	11,396
Total audit fees	TBC	118,779
Pooled housing receipts certification	2,340	2,340
Teachers pension return certification (LEA)	4,500	4,500
Teachers pension return certification (Sir John Cass)	4,500	4,500
Total audit related services fees	11,340	11,340
Other non-audit services	-	-
Total assurance services fees	TBC	130,119

⁽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.

FOR MORE INFORMATION:

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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.

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