



# Grant Thornton

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30 January 2013

Dear Councillor Clokie

**Ashford Borough Council Financial Statements for the year end 31 March 2013 - Understanding how the Audit Committee gains assurance from management**

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

I would be grateful, therefore, if you could write to me with your responses to the following questions.

- 1 How does the Audit Committee oversee management's processes in relation to:
  - 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 behavior (for example by updating, communicating and monitoring against the codes of conduct)?
- 2 Do you have knowledge of any actual, suspected or alleged frauds? If so, please provide details.
- 3 How does the Audit Committee gain assurance that all relevant laws and regulations have been complied with?
- 4 Are you aware of any actual or potential litigation or claims that would affect the financial statements?

**Chartered Accountants**

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In order to facilitate your response please find attached at Appendix 1 a copy of information provided by management relating to the matters set out above. Please could you provide a response by 31 March 2013 and please contact me if you wish to discuss anything in relation to this request.

Yours sincerely

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# Appendix 1 - Informing the audit risk assessment for Ashford Borough Council

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## Year end

31 March 2013

### Andy Mack

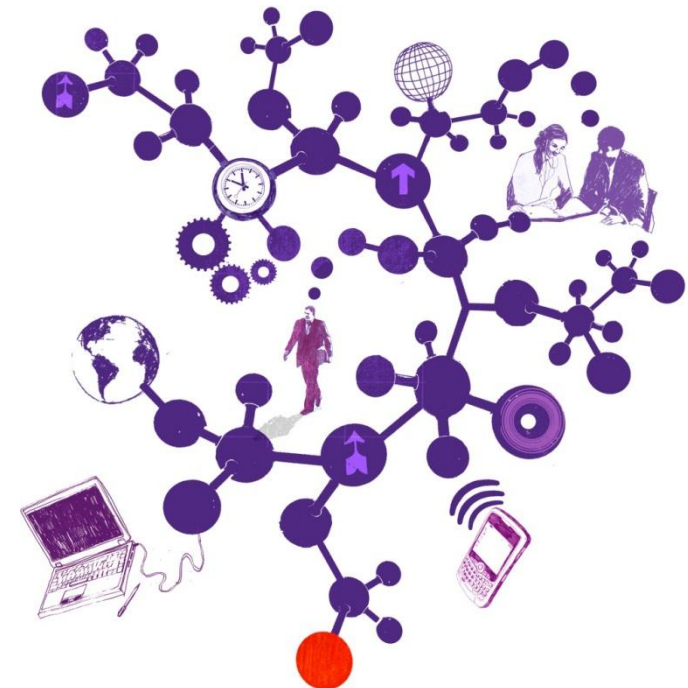
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# Purpose

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

## Background

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

This two-way communication assists both the auditor and the Audit 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 Audit Committee and supports the Audit 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 and the Audit Committee's oversight of the following areas:

- fraud
- laws and regulations
- going concern.

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

# Fraud

## Issue

### 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 Audit Committee and management. Management, with the oversight of the 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 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 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 Audit Committee oversees the above processes. We are also required to make inquiries of both management and the 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.

## Fraud risk assessment

Question	Management response
<p>Has the Council assessed the risk of material misstatement in the financial statements due to fraud? What are the results of this process?</p>	<p>Yes. The critical financial systems are the subject of routine review through either internal audit or external audit, including grant claims that result. The assessment of risk, therefore, follows as a product of this review work. No risks of material misstatements due to fraud were highlighted.</p>
<p>What processes does the Council have in place to identify and respond to risks of fraud?</p>	<p>The council has a comprehensive system of internal controls, and associated operating procedures and guidelines by which operations are then the subject of internal audit scrutiny according to risk-based judgements. The council's position on fraud and counter fraud activity is governed by policy arrangements that are communicated to staff, and supported and enforced through management responsibility, and the work of the internal audit team, and our internal fraud investigation team. Protocols to handle alleged fraudulent activity and its investigation are also stated, these protocols require notification to senior officers, including the statutory officers, and the Audit Committee.</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>None has been identified specifically relating to the financial statements. However, and simply to highlight our abilities, a significant electoral fraud involving postal voting was identified, following a 2011 local election, and investigated by our fraud investigation team, before handover to the police. This investigation led to a successful prosecution.</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>As mentioned in a response above, the council does have comprehensive internal control procedures, which are reviewed and developed to fit changing circumstances. Internal audit's review work over the year in question, and continuing, shows substantial assurance is given to the effectiveness of the control environment.</p>



## Fraud risk assessment (continued)

Question	Management response
<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>There is a wide scope activity relating to the financial reporting process. At lower levels of transaction handling and reporting our internal controls operate to ensure compliance and proper accounting and reporting are maintained. During the process of translating transactions into the financial statements and other reports, this is overseen by the Finance Manager and his team; scrutiny within the team is also maintained. As Section 151 officer I will also scrutinise financial reporting and the financial statements. So the assurance is that our internal controls, the associated routine checks that surround these, plus the various divisions of responsibilities to authorise and scrutinise, plus the professional ethical codes to which professional officers are obligated are designed and serve to remove inappropriate influence within the reporting process. Both internal and external audit work also contributes to eliminate the potential for material override of controls.</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>For similar reasons to the above the answer here is 'no'.</p>
<p>How does the 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 Audit Committee?</p>	<p>The Audit Committee has the responsibility for oversight of the council's internal controls, governance, risk management, and counter-fraud arrangements. This oversight is exercised through development of specific policies and procedures (for example the Audit Committee has in the past year steered a complete review of the council's strategic risks and the development of appropriate mitigation plans), and the communication of policies and procedures through the council's various internal communications channels. Operational oversight is exercised through management and the specific role of the internal audit team, and our dedicated counter-fraud team (this team's core focus is benefit fraud, but has developed a growth in focus in other areas, most notably housing tenancy fraud). Accountability to the Audit Committee for operational oversight is through the regular reporting of review outcomes to the committee. Structured annual reviews of governance, and counter-fraud activity are embodied in the committee's annual cycle, with specific reports therefore submitted, such as the Annual Governance Statement, the Annual Fraud Report, and the Annual Internal Audit Report. Specifically on fraud, the council has in place an Anti-Fraud and Corruption Strategy (and operational reporting protocol) supported by a 'whistleblowing' policy, a money laundering policy, and the council's complaints procedures. These protocols provide for notification of any fraud activity to be reported to the Audit Committee.</p>

## Fraud risk assessment (continued)

Question	Management response
How does the Council communicate and encourage ethical behaviour of its staff and contractors?	Communication is achieved through the internal publication of counter-fraud policies and procedures, and occasional staff briefings. These are also published on the council's website. Contracts have anti-fraud clauses and refer to the whistleblowing arrangements, and the whistleblowing policy and procedures are required to be appended to contracts. All new staff entrants are introduced to the procedures. A complete refresh of our intranet is now underway and this provides the opportunity to give even more prominence to these policies and procedures. The whistleblowing policy is due to be updated, and it is a requirement that it is submitted to each member of staff on an annual basis. Finally, the council has well-developed hospitality and declaration of interest procedures for staff and members. Hospitality and declarations arrangements together with the authorisation arrangements are now on-line, and details published on our transparency page of the council's website.
How do you encourage staff to report their concerns about fraud? Have any significant issues been reported?	The council has a 'whistleblowing' policy, and it has been used occasionally in the past. No reports were made in the last year. The policy is being updated and as stated it is a requirement that it is submitted to staff each year.
Are you aware of any related party relationships or transactions that could give rise to risks of fraud?	Related party relationships or transactions are annually documented through declarations that members and staff are required to provide.
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?	There were no instances of internal fraud or fraud affecting council services directly. I have previously mentioned an electoral fraud that was identified and successfully dealt with, this however did not arise from any internal activity of the council.

# Laws and regulations

## Issue

### 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 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 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.

# Impact of laws and regulations

Question	Management response
<p>What arrangements does the Council have in place to prevent and detect non-compliance with laws and regulations?</p>	<p>Formally the council's statutory Monitoring Officer and Chief Financial Officer have responsibilities to ensure compliance and report on any non-compliance or potential non-compliance by the council. There were no circumstances that gave rise to a need for either officer to exercise any statutory reporting. Both statutory officers are supported by professional staff (including internal audit) and the many processes designed to ensure compliance with the law. The statutory officers (or their nominees) are represented at Management Team, and contribute to the scrutiny of all reports for decision by members to ensure there is compliance. The approach is thorough depending on the issues and risks involved. For example the recent introduction (developed during 2012-2013) of a localised council tax support scheme by the council probably had more detailed scrutiny for compliance than in many other places, all to ensure our non-compliance risk, and risk of challenge was minimised. Other services, for example the Personnel Service and the Planning Service, are also responsible for ensuring compliance and triggering the development of new arrangements when needed. Regular training and updates for staff on new law, and emerging new law, is carried out across services. Our approach to new legislation is also thorough, with legal and non-legal staff contributing to ensure that important new legislation is understood by decision-makers (members and officers), and that appropriate policies and supporting procedures are developed. Here we may cite as an example, a very thorough approach to the various requirements of the Localism Act where our work to ensure compliance was worked through officer and member task groups, before recommendations for new arrangements made to cabinet.</p>
<p>How does management gain assurance that all relevant laws and regulations have been complied with?</p>	<p>Through the processes outlined above.</p>

## Impact of laws and regulations (continued)

Question	Management response
How is the Audit Committee provided with assurance that all relevant laws and regulations have been complied with?	The Committee is responsible for approving the Annual Governance Statement. The AGS draws together the council's governance and compliance procedures and the material outcomes of review work in the year. The AGS relies on input by the statutory officers and others, including the head of internal audit. It is through this process that once each year the Committee carries out a formal review. During each year the committee will receive advice and reports from officers on risks and any material non-compliance issues; but as far legal non-compliance is concerned there were none reported during the past year.
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
What arrangements does the Council have in place to identify, evaluate and account for litigation or claims?	The Head of Legal and Democratic Services (also the Monitoring Officer) has primary responsibility for identifying and managing litigation and claims against the council. Each year in drawing up the financial statements an assessment is made of whether risks associated with such actions are highlighted as contingent risks or liabilities, or to be satisfied that such risks are otherwise covered through the council's reserves. Similarly insurance risks are assessed.
Is there any actual or potential litigation or claims that would affect the financial statements?	One specific action is highlighted in the financial statements relating to the Stour Leisure Centre; this has been the subject of regular reporting in the accounts since the potential for action by the council was first raised.
Have there been any reports from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	None for the council.

# Going concern

## Issue

### 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.

## Going concern considerations

Question	Management response
Does the Council have procedures in place to assess the Council's ability to continue as a going concern?	Yes, the ongoing and regular reviews of the council's financial position and its position over the medium term are the processes through which assurance and actions plans are developed to ensure the council continues to operate as a going concern.
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?	Management and members are well aware of the risks to the council's financial position, but through risk and longer term financial planning the council is managing very well the impacts and potential impacts of these risks.
Has management reported on going concern to the Audit Committee?	Not specifically other than as part of the annual financial statements, though in the context of the Committee's responsibilities for risk management and governance, the committee is well aware of 'going concern' issues for the council and had adopted suitable strategies to ensure risks are highlighted and managed.
Are the financial assumptions in that report (e.g. future levels of income and expenditure) consistent with the Council's Business Plan and the financial information provided to the Council throughout the year?	In short 'yes'. The point of the medium term financial plan review, which supports the business plan is to ensure the council's operational and strategic plans are consistent with resources potentially available.



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