

Informing the audit risk assessment for Redditch Borough Council 2019/20

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### **Purpose**

The purpose of this report is to contribute towards the effective two-way communication between the Council's external auditors and the Council's Audit, Governance and Standards 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, Governance and Standards 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, Governance and Standards Committee. ISA(UK&I) emphasise the importance of two-way communication between the auditor and the Audit, Governance and Standards Committee and also specify matters that should be communicated.

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

- General Enquiries of Management
- Fraud,
- · Laws and Regulations,
- Going Concern,
- Related Parties, and
- Accounting Estimates.

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, Governance and Standards Committee should consider whether these responses are consistent with its understanding and whether there are any further comments it wishes to make.

## **General Enquiries of Management**

-	
Question	Management response
1. What do you regard as the key events or issues that will have a significant impact on the financial statements for 2019/20?	They key issues that will impact the financial statements for 2019/20 can be split between external and internal. The external impact will be determining the accounting requirements for IFRS 16 and the increased audit scrutiny with regards to fixed assets. Internally, the implementation of the new ERP system is absorbing significant resources within the council so identifying the resources needed to ensure both are successfully completed has been a key priority of the council for the past few months, with additional staff being hired to mitigate this risk.
2. Have you considered the appropriateness of the accounting policies adopted by Redditch Borough Council?  Have there been any events or transactions that may cause you to change or adopt new accounting policies?	The accounting policies are reviewed every year as part of the accounts closedown process. There are no proposed discretionary changes this year as there have been no fundamental changes in council activities.
3. Is there any use of financial instruments, including derivatives?	No
4. Are you aware of any significant transaction outside the normal course of business?	No

## **General Enquiries of Management**

Question	Management response
5. Are you aware of any changes in circumstances that would lead to impairment of non-current assets?	A full review will be conducted as part of the closedown process with officers across the Council and insurance asked to feedback to determine if there have been any potential impacts on non current assets. To date there have been none notified.
6. Are you aware of any guarantee contracts?	No
7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements?	No
8. Other than in house solicitors, can you provide details of those solicitors utilised by Redditch Borough Council during the year. Please indicate where they are working on open litigation or contingencies from prior years?	Anthony Collins Solicitors Browne Jacobson LLP No open matters at this stage.
9. Have any of Redditch Borough Council service providers reported any items of fraud, non-compliance with laws and regulations or uncorrected misstatements which would affect the financial statements?	No
10. Can you provide details of other advisors consulted during the year and the issue on which they were consulted?	Black Radley have been hired by the council to support its implementation of a commercial culture and bring challenge where appropriate to decision making and a company called Dragongate were brought in to support the Council with its investigations into the possible development of a new town hall.



### **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, Governance and Standards Committee and management. Management, with the oversight of the Audit, Governance and Standards 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, Governance and Standards Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As the Council's external 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:

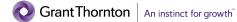
- · assessment that the financial statements could be materially misstated due to fraud,
- · process for identifying and responding to risks of fraud, including any identified specific risks,
- communication with the Audit, Governance and Standards Committee regarding its processes for identifying and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

We need to understand how the Audit, Governance and Standards Committee oversees the above processes. We are also required to make inquiries of both management and the Audit, Governance and Standards 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
Has Redditch Borough Council assessed the risk of material misstatement in the financial statements due to fraud?  How has the process of identifying and responding to the risk of fraud been undertaken and what are the results of this process?  How do Redditch Borough Council's risk management processes link to financial reporting?	The Council has assessed the risk of material misstatement. Although there is an on-going risk of fraud being committed against the Council, arrangements are in place to both prevent and detect fraud. These include work carried out by Internal Audit on overall fraud risk areas and work on Council Tax and Housing Benefit fraud.  There is on-going communication between external audit and responsible officers on emerging technical issues. Officers also attend technical updates. Financial monitoring reports also highlight areas of variance within the capital and revenue budgets and this assists management in identifying areas of material misstatement within the accounts  Management considers there is a low risk of material misstatement in the financial statements due to fraud and none has been detected to date.
2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?	There are some areas that are inherently at risk from fraud such as:  -Council Tax -Benefit Fraud -Single person discount
3. Are you aware of any instances of actual, suspected or alleged fraud, errors or other irregularities either within Redditch Borough Council as a whole or within specific departments since 1 April 2019?  As a management team, how do you communicate risk issues (including fraud) to those charged with governance?	The Audit, Governance & Standards Committee receives any adhoc fraud reports.  There are no material instances of fraud that have been identified during the year.  The Audit, Governance & Standards Committee would consider the fraud and the actions put forward by officers to ensure fraud is mitigated in the future.

Question	Management response
4. Have you identified any specific fraud risks?  Do you have any concerns there are areas that are at risk of fraud?  Are there particular locations within Redditch Borough Council	Evidence published within the Annual Fraud Indicator report suggests that fraud is committed in all organisations to varying degrees, so it is likely that some fraud is occurring in the Council. Locations handling income, particularly in the form of cash, are more likely to be at risk of fraud. However, management does not consider these to be significant risks
where fraud is more likely to occur?	
5. What processes does Redditch Borough Council have in place to identify and respond to risks of fraud?	Financial monitoring reports highlight areas of variance within the capital and revenue budgets and this assists management in identifying areas of material misstatement within the accounts.
<ul> <li>6. How would you assess the overall control environment for Redditch Borough Council including:</li> <li>the process for reviewing the effectiveness the system of internal control;</li> <li>internal controls, including segregation of duties;</li> <li>exist and work effectively?</li> <li>If not where are the risk areas and what mitigating actions have been taken?</li> </ul>	Internal Audit include fraud risks in their planning process and act as an effective internal control against fraud.  Sound systems of internal control with roles and responsibilities are defined in various places such as constitution.  The role of Internal Audit provides assurance that the Council's internal controls are in place. An annual report is produced and is available prior to the annual accounts being signed and approved.
What other controls are in place to help prevent, deter or detect fraud?	The regular monitoring of budgets and the allocation of financial professional support to budget holders provide control and mitigation against such overrides.
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)?	



Question	Management response
7. Are there any areas where there is potential for misreporting?	Due to the control environment in place, there are no areas which are particularly at risk of misreporting.
8. How does Redditch Borough Council communicate and encourage ethical behaviours and business processes of it's staff and contractors?	There is a Fraud Strategy and Whistleblowing procedure in place which explain the procedures to follow.
How do you encourage staff to report their concerns about fraud?	These policies have been reviewed and are in place for 2019/20.
What concerns are staff expected to report about fraud?	Employees are aware of the anti-fraud and corruption strategy, details are available on the website.
Have any significant issues been reported?	Staff are encouraged to report anything that they perceive as being "out of the ordinary", and no issues have been raised to date.
9. From a fraud and corruption perspective, what are considered to be high-risk posts?	There are not any significantly high-risk posts identified.
How are the risks relating to these posts identified, assessed and managed?	
10. Are you aware of any related party relationships or transactions that could give rise to instances of fraud?	2018/19 financial statements disclosure of related party transactions does not identify potential fraud risk.
	Members and officers are required to make full disclosure of any relationships that impact on their
How do you mitigate the risks associated with fraud related to related party relationships and transactions?	roles.
	Members are required to declare any relevant interests at Council and Committee meetings.

Question	Management response
11. What arrangements are in place to report fraud issues and risks to the Audit, Governance and Standards Committee?	Internal Audit provide the Audit, Governance & Standards Committee with updates of their work on fraud prevention and detection, including any significant identified frauds and the action taken.
How does the Audit, Governance and Standards Committee exercise oversight over management's	Any adhoc investigations are reported to the Audit, Governance & Standards Committee.
processes for identifying and responding to risks of fraud and breaches of internal control?  What has been the outcome of these arrangements	The Corporate risk register is reviewed by the Committee and the Member risk champion reports to the Committee at each meeting on updates from managers in relation to departmental registers.
so far this year?	To date, no issues or concerns have been raised.
12. Are you aware of any whistle blowing potential or complaints by potential whistle blowers? If so,	We are not aware of any whistleblowing reports.
what has been your response?	If there was such a report then members would consider the appropriate course of action.
13. Have any reports been made under the Bribery Act?	We are not aware of any whistleblowing reports.



## Law 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, Governance and Standards 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, Governance and Standards 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
How does management gain assurance that all relevant laws and regulations have been complied with?	The Monitoring Officer will advise the Council's Management team and Councillors as appropriate.
What arrangements does Redditch Borough Council have in place to prevent and detect non-compliance with laws and regulations?	The reporting arrangements include sections for both financial and legal implications to ensure managers have considered compliance with laws and regulations. In addition staff have professional training and conduct in place to support compliance.
Are you aware of any changes to Redditch Borough Council's regulatory environment that may have a significant impact on Redditch Borough Council's financial statements?	We are not aware of any changes to Redditch Borough Council's regulatory environment that may have a significant impact on the Redditch Borough Council's financial statements
2. How is the Audit, Governance and Standards Committee provided with assurance that all relevant laws and regulations have been complied with?	Assurance of complying with the Council's Constitution is provided through the Annual Governance Statement which is reported to the Audit, Governance & Standards Committee.
3. Have there been any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2019 with an on-going impact on the 2019/2020 financial statements?	No.
4. Is there any actual or potential litigation or claims that would affect the financial statements?	None.

# Impact of laws and regulations

Question	Management response
5. What arrangements does Redditch Borough Council have in place to identify, evaluate and account for litigation or claims?	The legal and finance team liaise on a regular basis to identify and evaluate any potential claims.
6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	No.

### **Going Concern**

#### Issue

### Matters in relation to going concern

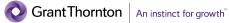
ISA(UK&I)570 covers auditor responsibilities in the audit of financial statements relating to management's use of the going concern assumption in the financial statements.

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.

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



Question	Management response
Has the management team carried out an assessment of the going concern basis for preparing the financial statements for Redditch Borough Council? What was the outcome of that assessment?	The Council has a four year plan in place for the budget, which forecasts sufficient resources are available to fund all planned expenditure as well as having sufficient reserves to fund any significant unplanned expenditure. The MTFP required a detailed review of all the councils activities, so it can be confident that it is accurate. As such, the council is confident that it is a going concern.
2. Are the financial assumptions in that report (e.g., future levels of income and expenditure) consistent with Redditch Borough Council's Business Plan and the financial information provided to Redditch Borough Council throughout the year?	The MTFP is the culmination of the years reports and savings programme. As such, it is reflective of the approvals which have been made throughout the year.



Question	Management response
3. Are the implications of statutory or policy changes appropriately reflected in the Business Plan, financial forecasts and report on going concern?	Yes, appropriate statutory and policy changes are referenced where appropriate and the implications factored in.
4. Have there been any significant issues raised with the Audit, Governance and Standards 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).	External audit have highlighted that some of the savings have not been identified in a high level of detail as yet, however they are being developed at present.
5. Does a review of available financial information identify any adverse financial indicators including negative cash flow or poor or deteriorating performance against the better payment practice code?  If so, what action is being taken to improve financial performance?	No, robust processes are in place and are reviewed regularly to ensure that this is not the case.



Question	Management response
6. Does Redditch Borough Council have sufficient staff in post, with the appropriate skills and experience, particularly at senior manager level, to ensure the delivery of the Redditch Borough Council's objectives? If not, what action is being taken to obtain those skills?	Yes.
7. Does Redditch Borough Council have procedures in place to assess its ability to continue as a going concern?	Yes – the Council conducts quarterly monitoring and quarterly updates of the savings programme, which at present is delivering greater savings than were initially planned.
8. Is management aware of the existence of events or conditions that may cast doubt on Redditch Borough Council's ability to continue as a going concern?	No.

Question	Management response
9. Are arrangements in place to report the going concern assessment to the Audit, Governance and Standards Committee? How has the Audit, Governance and Standards Committee satisfied itself that it is appropriate to adopt the going concern basis in preparing financial statements?	Yes - as part of the year end accounts presentation.  Audit, Governance & Standards has reviewed the work conducted by external audit on the year end accounts and savings programme as well as the professional opinion of the S151 Officer, and as such is satisfied that it is appropriate to adopt the going concern basis.



# **Related Parties**

### Issue

#### Matters in relation to Related Parties

Local Authorities are required to comply with IAS 24 and disclose transactions with entities/individuals that would be classed as related parties. These may include:

- entities that directly, or indirectly through one or more intermediaries, control, or are controlled by the Council (i.e. subsidiaries);
- associates;
- joint ventures;
- an entity that has an interest in the Council that gives it significant influence over the Council;
- · key management personnel, and close members of the family of key management personnel, and
- post-employment benefit plans (pension fund) for the benefit of employees of the Council, or of any entity that is a related party of the Council.

A disclosure is required if a transaction (or series of transactions) is material on either side, i.e. if a transaction is immaterial from the Redditch Borough Council perspective but material from a related party viewpoint then the Redditch Borough Council must disclose it.

ISA (UK&I) 550 requires us to review your procedures for identifying related party transactions and obtain an understanding of the controls that you have established to identify such transactions. We will also carry out testing to ensure the related party transaction disclosures you make in the financial statements are complete and accurate.

# **Relating Parties**

Question	Management response
What controls does Redditch Borough Council have in place to identify, account for and disclose related party transactions and relationships?	A number of arrangements are in place for identifying the nature of a related party and reported value including:  Maintenance of a register of interests for Members, and a register for pecuniary interests in contracts for Officers and Senior Mangers requiring disclosure of related party transactions.  Annual return from senior managers/officers requiring confirmation that they have read and understood the declaration requirements and stating details of any known related party interests.  Review of in-year income and expenditure transactions with known identified related parties from prior year or known history.  Review of the accounts payable and receivable systems and identification of amounts paid to/from assisted or voluntary organisation.  Review of year end debtor and creditor positions in relation to the related parties identified.  Review of minutes of decision making meetings to identify any member declarations and therefore related parties.



# **Accounting estimates**

### Issue

### Matters in relation to Related Accounting estimates

Local Authorities apply appropriate estimates in the preparation of their financial statements. ISA (UK&I) 540 sets out requirements for auditing accounting estimates. The objective is to gain evidence that the accounting estimates are reasonable and the related disclosures are adequate.

Under this standard we have to identify and assess the risks of material misstatement for accounting estimates by understanding how Redditch Borough Council identifies the transactions, events and conditions that may give rise to the need for an accounting estimate.

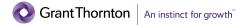
Accounting estimates are used when it is not possible to measure precisely a figure in the accounts. We need to be aware of all estimates that Redditch Borough Council is using as part of its accounts preparation; these are detailed in appendix 1 to this report. The audit procedures we conduct on the accounting estimate will demonstrate that:

- the estimate is reasonable: and
- estimates have been calculated consistently with other accounting estimates within the financial statements.

We would ask the Audit, Governance and Standards Committee to satisfy itself that the arrangements for accounting estimates are adequate.

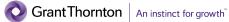
## **Accounting Estimates**

Question	Management response
1. Are management aware of transactions, events, conditions (or changes in these) that may give rise to recognition or disclosure of significant accounting estimates that require significant judgement (other than those in Appendix A)?	No.
2. Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?	Yes, Officers have reviewed the estimates and believe they are reasonable.
3. How is the Audit, Governance and Standards Committee provided with assurance that the arrangements for accounting estimates are adequate?	The professional judgement of the s151 Officer is accepted by the Committee.



### **Appendix A Accounting Estimates**

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Property plant & equipment valuations	The Council has a contract with Bruton Knowles to manage its asset base, including undertaking annual valuations. The Valuer is a RICS/CIB Member) and reviews are made inline with RICS guidance on the basis of 5 year valuations with interim reviews.	Technical Accountant notifies the valuer of the program of rolling valuations or of any conditions that warrant an interim re-valuation	Yes, Bruton Knowles	Valuations are made in line with RICS guidance –reliance on expert.	No



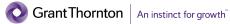
### **Appendix A Accounting Estimates**

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Estimated remaining useful lives of PPE	The following asset categories have general asset lives:  Buildings 50 years  Equipment/vehicles 5 years  Plant 12 years  Infrastructure 40 years	Consistent asset lives applied to each asset category.	Yes, Bruton Knowles	The method makes some generalisations. For example, buildings tend to have a useful life of 50 years. Although in specific examples based upon a valuation review, a new building can have a life as short as 25 years or as long as 70 years depending on the construction material used. This life would be recorded in accordance with the local qualified RICS or CIB Member.	No



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Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Depreciation and Amortisation	Depreciation is provided for on all fixed assets with a finite useful life on a straight-line basis.	Consistent application of depreciation method across all assets.	No	<ul> <li>The length of the life is determined at the point of acquisition or revaluation according to:</li> <li>Assets acquired in the first half of a financial year and depreciated on the basis of a full year's charge; assets acquired in the second half are not depreciated until the following financial year.</li> <li>Assets that are not fully constructed are not depreciated until they are brought into use.</li> </ul>	No



Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Impairments	Assets are assessed at each year-end as to whether there is any indication that an asset may be impaired. Where indications exist and any possible differences are estimated to be material, the recoverable amount of the asset is estimated and, where this is less than the carrying amount of the asset, an impairment loss is recognised for the shortfall.	Assets are assessed at each yearend as to whether there is any indication that an asset may be impaired.	Bruton Knowles	Valuations are made in line with RICS guidance –reliance on expert.	No



Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Measurement of Financial Instruments	Council values financial instruments at fair value based on the advice of their internal treasury consultants and other finance professions.	Take advice from finance professionals.	Yes	Take advice from finance professionals.	No

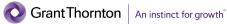


Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Provisions for liabilities	Provisions are made where an event has taken place that gives the Council a legal or constructive obligation that probably requires settlement by a transfer of economic benefits or service potential, and a reliable estimate can be made of the amount of the obligation. Provisions are charged as an expense to the appropriate service line in the CIES in the year that the Council becomes aware of the obligation, and are measured at the best estimate at the balance sheet date of the expenditure required to settle the obligation, taking into account relevant risks and uncertainties.	Charged in the year that the Council becomes aware of the obligation.	No	Estimated settlements are reviewed at the end of each financial year —where it becomes less than probable that a transfer of economic benefits will now be required (or a lower settlement than anticipated is made), the provision is reversed and credited back to the relevant service. Where some or all of the payment required to settle a provision is expected to be recovered from another party (e.g. from an insurance claim), this is only recognised as income for the relevant service if it is virtually certain that reimbursement will be received by the Council.	No.



Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Accruals	We use standard accruals accounting –accruals are based on expenses incurred that have not yet been paid.	Monthly management accounts provides rigorous analysis so that any accruals are highlighted and actioned throughout the year	N/A.	N/A.	No.
Non Adjusting events – events after the balance sheet date	S151Officer makes the assessment. If the event is indicative of conditions that arose after the balance sheet date then this is an unadjusting event. For these events only a note to the accounts is included, identifying the nature of the event and where possible estimates of the financial effect.	Heads of Services notify the s151 Officer.	This would be considered on individual circumstances.	This would be considered on individual circumstances.	N/A

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Bad Debt Provision	A provision is estimated using a proportion basis of an aged debt listing.	An aged debt listing is provided routinely and finance calculate the provision.	No	Consistent proportion used across aged debt as per the Code.	No.
Overhead Allocation	The Finance Team apportion central support costs to services based on fixed bases as detailed in the 'Allocation Summary' spread sheet.	All support service cost centres are allocated according to the agreed 'Allocation Summary' spread sheet.	No	Apportionment bases are reviewed each year to ensure equitable.	No





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