

Informing the audit risk assessment for City of Wolverhampton Council 2020/2021

Jon Roberts
Partner
T 0117 305 7699
E jon.roberts@uk.gt.com

Nicola Coombe
Senior Manager
T 0121 232 5206
E nicola.coombe@uk.gt.com

Matthew Berrisford
Assistant Manager
T 0117 232 5352
E matthew.j.berrisford@uk.gt.com



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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 and Risk 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 and Risk Committee under auditing standards.

Background

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

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

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

Purpose

This report includes a series of questions on each of these areas and the response we have received from City of Wolverhampton Council's management. The Audit and Risk 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
<p>1. What do you regard as the key events or issues that will have a significant impact on the financial statements for 2020/21?</p>	<p>Asset valuations and the net pension liability estimate, have the potential to have a significant impact on the financial statements due to their materiality and the fact that they are based on various assumptions, e.g. investment returns, retirement ages, mortality rates.</p>
<p>2. Have you considered the appropriateness of the accounting policies adopted by City of Wolverhampton Council? Have there been any events or transactions that may cause you to change or adopt new accounting policies?</p>	<p>Accounting policies are kept under review throughout the year by Strategic Finance, but formally reviewed each year by the Chief Accountant in preparation of the financial statements.</p> <p>No changes to accounting policies, or new accounting policies are anticipated.</p>
<p>3. Is there any use of financial instruments, including derivatives?</p>	<p>Yes, the Council has equity instruments, investments, borrowings, finance leases, PFI arrangements, cash, receivables and payables. These are disclosed in the notes to the accounts.</p>
<p>4. Are you aware of any significant transaction outside the normal course of business?</p>	<p>In 2020-2021, the Council has received a number of grants in relation to Covid-19, including the distribution of business grants, and test and trace isolation payments.</p>

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?	The outbreak of Covid-19 has impacted on the global financial markets and market activity. A material valuation uncertainty was disclosed in the property valuer's report in 2019-2020 and is likely to also be the case for 2020-2021.
6. Are you aware of any guarantee contracts?	<p>The Council has provided guarantees to: -</p> <ul style="list-style-type: none"> • a number of organisations at the point they were admitted to West Midlands Pension Fund, to fund any potential pension liability; • Walsall Metropolitan Borough Council for the University of Wolverhampton, in relation to grant funding through the Black Country Local Enterprise Partnerships (LEP); • Barclays for the City of Wolverhampton College.
7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements?	None as of today (15.02.2021). This will be reviewed through closedown.
8. Other than in house solicitors, can you provide details of those solicitors utilised by City of Wolverhampton Council during the year. Please indicate where they are working on open litigation or contingencies from prior years?	In terms of individual solicitors the Council has utilised locums from its in-house agency and an external agency; they have not worked on open litigation or contingencies from prior years. The Council has also, where appropriate, used external law firms to assist on some significant projects including contract advice and is happy to provide full details to auditors on this.

General Enquiries of Management

Question	Management response
9. Have any of the Council's service providers reported any items of fraud, non-compliance with laws and regulations or uncorrected misstatements which would affect the financial statements?	None of the Council's service providers have reported any items of fraud, non-compliance with laws and regulations or uncorrected misstatements which would affect the financial statements.
10. Can you provide details of other advisors consulted during the year and the issue on which they were consulted?	There are a number of consultants used, mainly for regeneration projects, to provide financial, legal and professional advice. We have also used barristers for external expert advice. The Council will provide specific details to Grant Thornton.

Fraud

Issue

Matters in relation to fraud

ISA (UK) 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 and Risk Committee and management. Management, with the oversight of the Audit and Risk 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 and Risk Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As City of Wolverhampton 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 and Risk 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 and Risk Committee oversees the above processes. We are also required to make inquiries of both management and the Audit and Risk 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 City of Wolverhampton Council's management.

Fraud risk assessment

Question	Management response
<p>1. Has City of Wolverhampton Council assessed the risk of material mis-statement in the financial statements due to fraud?</p> <p>How has the process of identifying and responding to the risk of fraud been undertaken and what are the results of this process?</p> <p>How does the Council's risk management processes link to financial reporting?</p>	<p>The collective processes for closedown, budget monitoring and outturn take into consideration the risk of material misstatement due to error or fraud. Senior finance officers meet regularly to consider any issues arising from budget monitoring and the closedown process. Should any fraud be reported as part of this or any other process, corrective action would be taken. A strategic and finance leadership risk register is also regularly updated and reviewed.</p>
<p>2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?</p>	<p>There are no particularly high risk areas as such – but those around payments, journals and bank account changes would in all likelihood be most at risk.</p>

Fraud risk assessment

Question	Management response
<p>3. Are you aware of any instances of actual, suspected or alleged fraud, errors or other irregularities either within City of Wolverhampton Council as a whole or within specific departments since 1 April 2020? As a management team, how do you communicate risk issues (including fraud) to those charged with governance?</p>	<p>Yes, there have been a small number of cases – some ongoing (although nothing material) – and where appropriate, a report on instances of fraud will go to the Audit and Risk Committee meetings.</p>
<p>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 City of Wolverhampton Council where fraud is more likely to occur?</p>	<p>The areas of greatest risk are housing tenancy, council tax, personal budgets, Covid-19 related business and other support grants, procurement and business rates.</p> <p>As with all large organisations there is a likelihood that fraud will be taking place in some shape or form, and there are a small number of ongoing investigations into cases of suspected fraud. The Council takes into account the findings in publications such as the CIPFA “Fraud Tracker Survey” which identifies fraud trends, and those areas more susceptible to fraud. From this a Fraud Risk Register has been developed, which in turn, is used to inform and drive the Counter Fraud plan. The Council also works closely with Wolverhampton Homes in order to help tackle the risk of housing and tenancy related fraud.</p>
<p>5. What processes does City of Wolverhampton Council have in place to identify and respond to risks of fraud?</p>	<p>The Counter Fraud Team, which sits within Audit Services, leads in raising fraud awareness across the Council and in promoting an anti-fraud culture. The team carries out investigations into areas of suspected or reported fraudulent activity. The team maintains the Council’s fraud risk register and produces and maintains the Counter Fraud Plan. In addition, they lead on the Cabinet Office’s National Fraud Initiative (NFI) exercise.</p>

Fraud risk assessment

Question	Management response
<p>6. How do you assess the overall control environment for City of Wolverhampton Council, including:</p> <ul style="list-style-type: none"> the existence of internal controls, including segregation of duties; and the process for reviewing the effectiveness the system of internal control? <p>If internal controls are not in place or not effective where are the risk areas and what mitigating actions have been taken?</p> <p>What other controls are in place to help prevent, deter or detect 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>Audit Services have given an unqualified opinion on the adequacy and effectiveness of the Council's internal control system for a number of years. Individual internal audit reviews are undertaken in-year, and Audit Services report back, where appropriate, on individual areas where controls could be improved. Recommendations will then be made in order to improve any weaknesses found, and key recommendations are later followed up.</p> <p>Audit also report any key control weaknesses at each meeting of the Audit and Risk Committee. The Council's Counter Fraud Team which sits within Audit Services incorporates a broad skills base which provides the resources to perform counter fraud and investigation activities and strengthens the council's ability to respond to fraud. There are not any known areas where there is a potential for override of controls or inappropriate influence over the financial reporting process.</p>
<p>7. Are there any areas where there is potential for misreporting?</p>	<p>There are no known areas for potential misreporting. The fraud risk register, counter fraud plan and audit plan are in place to minimise the potential for misreporting.</p>

Fraud risk assessment

Question	Management response
<p>8. How does City of Wolverhampton Council communicate and encourage ethical behaviours and business processes of it's staff and contractors?</p> <p>How do you encourage staff to report their concerns about fraud?</p> <p>What concerns are staff expected to report about fraud?</p> <p>Have any significant issues been reported?</p>	<p>The Council has the following policies and procedures (which broadly set out the nature of concerns they cover) to help raise the awareness of, and combat fraud:</p> <ul style="list-style-type: none"> • Anti-Fraud and Corruption Policy and Procedure • Whistleblowing Policy and Procedure • Anti-Money Laundering Policy and Procedure • Raising Fraud Awareness Guide <p>Where appropriate, these documents are reviewed by the Audit and Risk Committee, and are available on the internet. The internet page on fraud has been designed to help strengthen the ease in which potential fraud can be reported on-line. Employees will also learn about business practices and ethical behaviour through the following:</p> <ul style="list-style-type: none"> • Codes of Conduct • induction training • accountability arrangements signed by all senior officers • contracts and their standard exclusions • adherence to procurement procedures • aide memoires from Monitoring Officer around gifts & hospitality policy at key times of the year. <p>The policies referred to above encourage employees to report any concerns, and these include full contact details – including a confidential hotline. The Council's internet site allows on-line reporting.</p> <p>The Council has also recently entered into an arrangement with See Hear Speak Up who offer an independent whistleblowing service which allows employees to report any matters of concern they may have in a secure and confidential manner. The availability of this service has been well promoted across the Council.</p> <p>There have been no significant issues recently reported.</p>

Fraud risk assessment

Question	Management response
<p>9. From a fraud and corruption perspective, what are considered to be high-risk posts?</p> <p>How are the risks relating to these posts identified, assessed and managed?</p>	<p>Senior Officers and Members who have powers to influence decisions are potentially the highest risk posts in respect of fraud and corruption.</p> <p>Senior Officers and Members are required to declare interests on a register of interests and at meetings.</p>
<p>10. Are you aware of any related party relationships or transactions that could give rise to instances of fraud?</p> <p>How do you mitigate the risks associated with fraud related to related party relationships and transactions?</p>	<p>No instances of related party relationships or transactions are known to be fraudulent.</p> <p>Conditions of contact with third parties are in place to mitigate fraud risk, this includes refraining from providing gifts and payments.</p> <p>The Council's auditors would seek access where appropriate to third party records if fraud is suspected.</p>
<p>11. What arrangements are in place to report fraud issues and risks to the Audit and Risk Committee? How does the Audit and Risk Committee exercise oversight over management's processes for identifying and responding to risks of fraud and breaches of internal control? What has been the outcome of these arrangements so far this year?</p>	<p>A Counter Fraud Update report is presented to each meeting of the Audit and Risk Committee detailing how the Council is tackling issues around fraud and where applicable includes details of any recent investigations into suspected fraudulent activity. The members of the Committee satisfy themselves that the outcomes are appropriate and any improvements in control have been identified.</p> <p>The committee also reviews and approves all of the Council's Anti-Fraud Policies and Procedures on a regular basis. This includes a detailed Counter Fraud Plan charting out the actions to be taken going forward, and the Council's Fraud Risk Register. As part of the Annual Internal Audit Plan, Audit Services undertake annual reviews of many of the Council's key financial systems – consideration of fraud forms part of these.</p> <p>The Council also fully participates in the Cabinet Office's National Fraud Initiative, and other national fraud benchmarking exercises, as appropriate.</p>

Fraud risk assessment

Question	Management response
12. Are you aware of any whistle blowing potential or complaints by potential whistle blowers? If so, what has been your response?	Any potential whistle blowing complaints are logged and investigated. Where appropriate disciplinary and prosecution action is taken against the individuals involved.
13. Have any reports been made under the Bribery Act?	The Council has not received any reports under the Bribery Act.

Law and regulations

Issue

Matters in relation to laws and regulations

ISA (UK) 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 and Risk Committee, is responsible for ensuring that City of Wolverhampton 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 and Risk 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>1. How does management gain assurance that all relevant laws and regulations have been complied with?</p> <p>What arrangements does City of Wolverhampton Council have in place to prevent and detect non-compliance with laws and regulations?</p> <p>Are you aware of any changes to the Council's regulatory environment that may have a significant impact on the Council's financial statements?</p>	<p>A number of controls are in place. Management place reliance on these controls. In addition, there is an annual programme of work from Audit Services which in part covers legal matters. Directors also meet daily in the morning to discuss issues of topical concern including any legal matters. SEB also meets weekly for wider briefings across the business.</p> <p>We are not aware of any changes to the Council's regulatory environment that may have a significant impact on the Council's financial statements.</p>
<p>2. How is the Audit and Risk Committee provided with assurance that all relevant laws and regulations have been complied with?</p>	<p>The findings and recommendations from the work of Audit Services, with key issues being reported back to the Audit and Risk Committee. Also, each Director is required to sign an annual assurance statement, and this helps inform the Annual Governance Statement that is reported to the Audit and Risk Committee.</p>
<p>3. Have there been any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2020 with an on-going impact on the 2020/21 financial statements?</p>	<p>None as at today (15.2.2021)</p>
<p>4. Is there any actual or potential litigation or claims that would affect the financial statements?</p>	<p>None as at today (15.2.2021)</p>

Impact of laws and regulations

Question	Management response
5. What arrangements does City of Wolverhampton Council have in place to identify, evaluate and account for litigation or claims?	All litigation is commenced / defended / settled in consultation with the Monitoring Officer. All prospective prosecutions are evaluated against nationally adopted criteria. An annual appraisal of contingent liabilities is prepared and reported by the Monitoring Officer in consultation with the Risk Manager.
6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	None as at today (15.2.2021)

Related Parties

Issue

Matters in relation to Related Parties

City of Wolverhampton Council is required to 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 City of Wolverhampton Council;
- 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 Council's perspective but material from a related party viewpoint then the Council must disclose it.

ISA (UK) 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.

Related Parties

Question	Management response
<p>1. Have there been any changes in the related parties disclosed in City of Wolverhampton Council's 2019/20 financial statements? If so please summarise:</p> <ul style="list-style-type: none"> • the nature of the relationship between these related parties and City of Wolverhampton Council • whether City of Wolverhampton Council has entered into or plans to enter into any transactions with these related parties • the type and purpose of these transactions 	<p>Yes, Cabinet on 20 January 2021 recommended that the Council invest in a pilot for a new affordable housing product called 'Help to Own' (H2O). Subject to final approval this transaction, which will be in the form of an investment, is likely to take place before year end.</p>
<p>2. What controls does City of Wolverhampton Council have in place to identify, account for and disclose related party transactions and relationships?</p>	<p>Forms re-devised to have prompts including aide-memoire to disclose Directorships. Letters to all councillors (or emails as appropriate) to remind them annually to update interests. Ability for councillors and officers to now update interests in "real-time" on-line through Modern.gov platform from home or wherever that have internet connectivity</p>
<p>3. What controls are in place to authorise and approve significant transactions and arrangements with related parties?</p>	<p>The Council's Monitoring Officer reviews and approves transactions with related parties.</p>
<p>4. What controls are in place to authorise and approve significant transactions outside of the normal course of business?</p>	<p>The Council's Monitoring Officer reviews and approves transactions outside the normal course of business.</p>

Accounting estimates

Issue

Matters in relation to Related Accounting estimates

ISA (UK) 540 (Revised December 2018) requires auditors to understand and assess an entity's internal controls over accounting estimates, including:

- The nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates;
- How management identifies the need for and applies specialised skills or knowledge related to accounting estimates;
- How the entity's risk management process identifies and addresses risks relating to accounting estimates;
- The entity's information system as it relates to accounting estimates;
- The entity's control activities in relation to accounting estimates; and
- How management reviews the outcomes of previous accounting estimates.

As part of this process auditors also need to obtain an understanding of the role of those charged with governance, which is particularly important where the estimates have high estimation uncertainty, or require significant judgement.

Specifically do Audit and Risk Committee members:

- Understand the characteristics of the methods and models used to make the accounting estimates and the risks related to them;
- Oversee management's process for making accounting estimates, including the use of models, and the monitoring activities undertaken by management; and
- Evaluate how management made the accounting estimates?

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

Accounting Estimates - General Enquiries of Management

Question	Management response
1. What are the classes of transactions, events and conditions, that are significant to the financial statements that give rise to the need for, or changes in, accounting estimate and related disclosures?	Valuation, depreciation and impairment of property, plant and equipment Expected credit losses Provision for liabilities (e.g. PFI) Financial guarantees Valuation of defined benefit net pension liability
2. How does the Council's risk management process identify and addresses risks relating to accounting estimates?	Officers undertake an annual risk assessment, identifying and addressing risks prior to closedown. Going forward, this will be included as an agenda item at the Audit and Risk Committee.
3. How do management identify the methods, assumptions or source data, and the need for changes in them, in relation to key accounting estimates?	Management consult guidance, e.g. the Code of Practice on Local Authority Accounting and RICS guidance.
4. How do management review the outcomes of previous accounting estimates?	Management look back retrospectively to assess whether previous accounting estimates were born out in reality. Going forward, this will be included as an agenda item at the Audit and Risk Committee.
5. Were any changes made to the estimation processes in 2020/21 and, if so, what was the reason for these?	So far, no changes have been made to the estimation processes in 2020-2021. This will be reviewed through closedown.

Accounting Estimates - General Enquiries of Management

Question	Management response
<p>6. How do management identify the need for and apply specialised skills or knowledge related to accounting estimates?</p>	<p>Management commission specialist skills or knowledge when, for example when expert knowledge or resource is not available in-house.</p>
<p>7. How does the Council determine what control activities are needed for significant accounting estimates, including the controls at any service providers or management experts?</p>	<p>The Council determines what control activities are needed through liaison with internal audit, referring to the Code of Practice on Local Authority Accounting and other guidance, attendance at seminars and workshops (e.g. Grant Thornton's annual Local Government Accountants Workshop and CIPFA's conference "Capital Valuations Avoiding the Pitfalls") and through liaising with other authorities (e.g. as part of the West Midlands Accountancy Officers Group)</p>
<p>8. How do management monitor the operation of control activities related to accounting estimates, including the key controls at any service providers or management experts?</p>	<p>Management review the output of service providers and the assumptions underpinning them, challenging any discrepancies or unexpected outcomes.</p>
<p>9. What is the nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates, including:</p> <ul style="list-style-type: none"> - Management's process for making significant accounting estimates - The methods and models used - The resultant accounting estimates included in the financial statements. 	<p>Accounting estimates are discussed at Audit and Risk Committee, as part of the financial statements and during training sessions provided to members prior to them receiving the audited financial statements. To further enhance oversight and governance, for 2020-2021 there will be a specific agenda item on accounting estimates, attended by external valuers and the Director of Pensions, where they will explain significant accounting estimates they make.</p>

Accounting Estimates - General Enquiries of Management

Question	Management response
10. 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 the Accounting Estimate Management Summary (dated 3.2.21))?	None as of today (21.02.2021), however this will continue to be monitored through closedown.
11. Are the management arrangements for the accounting estimates, as detailed in the Accounting Estimate Management Summary (dated 3.2.21) reasonable?	Accounting estimates are kept under review throughout the year by Strategic Finance, but formally reviewed each year by the Director of Finance in preparation of the financial statements. The outcome of this formal review is reflected in the Accounting Estimate Management Summary (dated 3.2.21) , which will be presented to the Audit and Risk Committee in agenda item 8. This Committee provides the opportunity for challenge and any queries.
12. How is the Audit and Risk Committee provided with assurance that the arrangements for accounting estimates are adequate ?	Please see above.



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