



# **Lothian Valuation Joint Board**

## **Annual Audit Plan 2014/15**

Prepared for Lothian Valuation Joint Board

March 2015



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Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

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# Summary

## Introduction

1. Our audit is focused on the identification and assessment of the risks of material misstatement in the Lothian Valuation Joint Board's financial statements.
2. This report summarises the key challenges and risks facing the Lothian Valuation Joint Board ("the Board") and sets out the audit work that we propose to undertake in 2014/15. Our plan reflects:
  - the risks and priorities facing the Board
  - current national risks that are relevant to local circumstances
  - the impact of changing international auditing and accounting standards
  - our responsibilities under the Code of Audit Practice as approved by the Auditor General for Scotland
  - issues brought forward from previous audit reports.

## Summary of planned audit activity

3. Our planned work in 2014/15 includes:
  - an audit of the financial statements and provision of an opinion on whether:
    - they give a true and fair view of the state of affairs of the Lothian Valuation Joint Board as at 31 March 2015 and its income and expenditure for the year then ended
    - the accounts have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2014 Code of Practice on Local Authority Accounting in the United Kingdom (the Code)
  - a review and assessment of the Board's governance and performance arrangements in a number of key areas including a review of the adequacy of internal audit and the governance statement.

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# Responsibilities

4. The audit of the financial statements does not relieve management or the Board, as the body charged with governance, of their responsibilities.

## Responsibility of the appointed auditor

5. Our responsibilities, as independent auditor, are established by the Local Government (Scotland) Act 1973 and the Code of Audit Practice, and guided by the auditing profession's ethical guidance.
6. Auditors in the public sector give an independent opinion on the financial statements. We also review and report on the arrangements set in place by the audited body to ensure the proper conduct of its financial affairs and to manage its performance and use of resources. In doing this, we aim to support improvement and accountability.

## Responsibility of the Treasurer

7. It is the responsibility of the Treasurer, as the appointed "proper officer", to prepare the financial statements in accordance with relevant legislation and the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). This means:

- maintaining proper accounting records
- preparing financial statements which give a true and fair view of the state of affairs of the Board as at 31 March 2015 and its expenditure and income for the year then ended.

## Format of the accounts

8. The financial statements should be prepared in accordance with the Code which constitutes proper accounting practice.

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# Audit Approach

## Our approach

9. Our audit approach is based on an understanding of the characteristics, responsibilities, principal activities, risks and governance arrangements of the Board. We also consider the key audit risks and challenges in the local government sector generally. This approach includes:
  - understanding the business of the Board and the risk exposure which could impact on the financial statements
  - assessing the key systems of internal control, and considering how risks in these systems could impact on the financial statements
  - identifying major transaction streams, balances and areas of estimation and understanding how the Board will include these in the financial statements
  - assessing and addressing the risk of material misstatement in the financial statements
  - determining the nature, timing and extent of the audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements give a true and fair view.
10. We have also considered and documented the sources of assurance which will make best use of our resources and allow us to focus audit testing on higher risk areas during the audit of the financial statements. The main areas of assurance for the audit come from planned management action and reliance on systems of internal control. Management action being relied on for 2014/15 includes:
  - comprehensive closedown procedures for the financial statements accompanied by a timetable issued to all relevant staff (the Board utilises the financial systems of the City of Edinburgh Council and follows the closedown procedures and timetables of the council)
  - clear responsibilities for preparation of financial statements and the provision of supporting working papers
  - delivery of unaudited financial statements to agreed timescales with a comprehensive working papers package
  - completion of the internal audit programme for 2014/15.
11. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carry out an early assessment of the internal audit function. Internal audit is provided by the internal audit service within the council. Overall, we concluded that the internal audit service operates in accordance with Public Sector Internal Audit

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Standards (PSIAS) and has sound documentation standards and reporting procedures in place.

We plan to place formal reliance on aspects of the work of internal audit in the following areas, to support our audit opinion on the financial statements:

- City of Edinburgh Council systems operated on behalf of the Board, specifically accounts payable
- Audit work carried out in support of the Annual Governance Statement for inclusion with the financial statements.

## Materiality

12. International Standard on Auditing 320 provides guidance on the concept of materiality. We consider materiality and its relationship to audit risk when planning the nature, timing and extent of our audit and conducting our audit procedures. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
13. Based on our knowledge and understanding of the Board we have set our planning materiality at 1% of gross expenditure. For 2014/15 planning materiality is £100,000.
14. We set a lower level, known as performance materiality, when defining our audit procedures. This level depends on

professional judgement and is informed by a number of factors including:

- extent of estimation and judgement within the financial statements
- nature and extent of prior year misstatements
- extent of audit testing coverage.

15. For 2014/15 performance materiality has been set at £50,000. We will report, to those charged with governance, all misstatements greater than £1,000.
16. In addition, an inaccuracy which would not normally be regarded as material in terms of monetary value may be important for other reasons (for example the failure to achieve a statutory requirement, or an item contrary to law). In the event of such an item arising, its materiality has to be viewed in a narrower context; such matters would normally fall to be covered in an explanatory paragraph in the independent auditor's report.

## Reporting arrangements

17. The Local Authority Accounts (Scotland) Regulations 2014 require that the unaudited annual accounts are submitted to the appointed external auditor no later than 30 June each year. The Board is required to consider the unaudited annual accounts at a meeting by 31 August.

18. The Board must publish the unaudited accounts on its website and give public notice of the inspection period.
19. The 2014 regulations require the Board to meet by 30 September to consider whether to approve the audited annual accounts for signature. Immediately after approval, the annual accounts require to be signed and dated by specified members and officers and then provided to the auditor. The Controller of Audit requires audit completion and issue of an independent auditor's report (opinion) by 30 September each year.
20. The Board is required to publish on its website its signed audited annual accounts, and the audit certificate, by 31 October. The annual audit report is required to be published on the website by 31 December.
21. An agreed timetable is included at Exhibit 1 below which takes account of submission requirements and planned Board meeting dates :

#### Exhibit 1: Financial statements audit timetable

Key stage	Date
Planned Board approval of unaudited financial statements	22 June 2015
Submission of unaudited financial statements with working papers package	By 29 June 2015
Progress meetings with lead officers on emerging issues	As required during audit
Latest date for final clearance meeting with Treasurer	By 31 August 2015
Agreement of unsigned financial statements for Board agenda, and issue of combined ISA 260 report to those charged with governance and Annual Audit Report.	By 31 August 2015
Board meeting date	7 September 2015
Independent auditors report signed	By 30 September 2015

22. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the responsible head of service and relevant officers to confirm factual accuracy. Responses to



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draft reports are expected within three weeks of submission. A copy of all final agreed reports will be sent to the Depute Assessor, the Treasurer, internal audit and Audit Scotland's Performance Audit and Best Value Group.

- 23. We will provide an independent auditor's report to the Board and the Accounts Commission that the audit of the financial statements has been completed in accordance with applicable statutory requirements. As part of streamlining our audit approach, the Annual Audit Report will be combined with the ISA 260 report.
- 24. All annual audit reports produced are published on Audit Scotland's website: ([www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk)).
- 25. Planned outputs for 2014/15 are summarised at Appendix I.

## Quality control

- 26. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice issued by Audit Scotland and approved by the Accounts

Commission. To ensure that we achieve the required quality standards, Audit Scotland conducts peer reviews and internal quality reviews and has been subject to a programme of external reviews by the Institute of Chartered Accountants of Scotland (ICAS).

- 27. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We do, however, welcome feedback at any time and this may be directed to the engagement lead, Stephen O'Hagan.

## Independence and objectivity

- 28. Auditors appointed by the Accounts Commission must comply with the Code of Audit Practice. When auditing the financial statements, auditors must also comply with professional standards issued by the Auditing Practices Board (APB) and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has in place robust arrangements to ensure compliance with these standards including an annual "fit and proper" declaration for all members of staff. The arrangements are overseen by the Assistant Auditor General, who serves as Audit Scotland's Ethics Partner.

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29. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of the Board

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# Audit issues and risks

## Audit issues and risks

- 30. Based on our discussions with staff, attendance at Board meetings and a review of supporting information, we have identified the following main financial statements risk areas for your organisation
- 31. **Management override of controls:** ISA 240 highlights the unique position of management to influence the financial statements by overriding controls that otherwise operate effectively. The ability to override these controls exists in all entities and therefore represents a significant financial statements risk due to fraud.
- 32. We will undertake focused substantive testing of journal entries, accounting estimates and significant transactions outside the course of normal business.
- 33. **Accounts Payable ledger:** As part of the 2013/14 financial statements audit process, a number of adjustments were made in the accounts in respect of debit balances that had been posted erroneously to the Board's accounts payable ledger. The Board agreed to process the appropriate entries within the accounts payable ledger during 2014/15 to correct the ledger position.
- 34. We will review the ledger adjustments made by the Board, and perform sample testing of any remaining debit balances in the accounts payable ledger to identify whether these relate to the Board.
- 35. **Related Party Transactions:** The Board does not have a formal process in place for identifying and recording any external interests held by its senior officers therefore there is a risk that it may not identify all relevant related party transactions.
- 36. The Board has agreed to review its procedures and consider whether any improvements could be made.
- 37. **Cost Pressures:** As noted in the previous year's audit plan, the Board continues to manage the provision of services under a 2011/12 level flat cash budget. The Board has an established track record of managing expenditure pressures within its budgetary provision, however as at period 7 of 2014/15, the board was forecasting an outturn much closer to budget than previous years, with a projected underspend of £3,000.
- 38. Following recent confirmation from the Scottish Government of an additional £110,000 contribution towards referendum costs incurred by the Board, the projected year end underspend is

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now £121,000. We will continue to monitor the Board's financial position through the course of our audit.

## Summary assurance plan

39. Within these identified risk areas there is a range of more specific risks and these are summarised at Appendix II. In most cases, actions to manage these risks are either planned or already underway within the organisation. Details of the sources of assurance that we have received for each of these risks and any audit work we plan to undertake is also set out in Appendix II. In the period prior to the submission of the unaudited financial statements, we will liaise with senior officers on any new or emerging issues.

# Fees and resources

## Audit fee

40. Over the past four years, Audit Scotland has reduced audit fees by 23.5% in real terms, exceeding our 20% target. Due to further refinement of our audit approach we have been able to restrict the increase in audit fees for 2014/15 to 1% which, in real terms, represents a 0.6% reduction at 2014 price levels.
41. In determining the audit fee we have taken account of the risk exposure of the Board, the management assurances in place, and the level of reliance we plan to take from the work of internal audit. We have assumed receipt of a complete set of unaudited financial statements and comprehensive working papers package by 29 June 2015.
42. The agreed audit fee for the 2014/15 audit of the Board is £7,090. Our fee covers:
- the costs of planning, delivering and reporting the annual audit including auditor's attendance at Board meetings
  - your organisation's allocation of the cost of national performance audits and statutory reports by the Accounts Commission
  - a contribution towards functions that support the local audit process (e.g. technical support and coordination of the

National Fraud Initiative), support costs and auditors' travel and subsistence expenses.

43. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

## Audit team

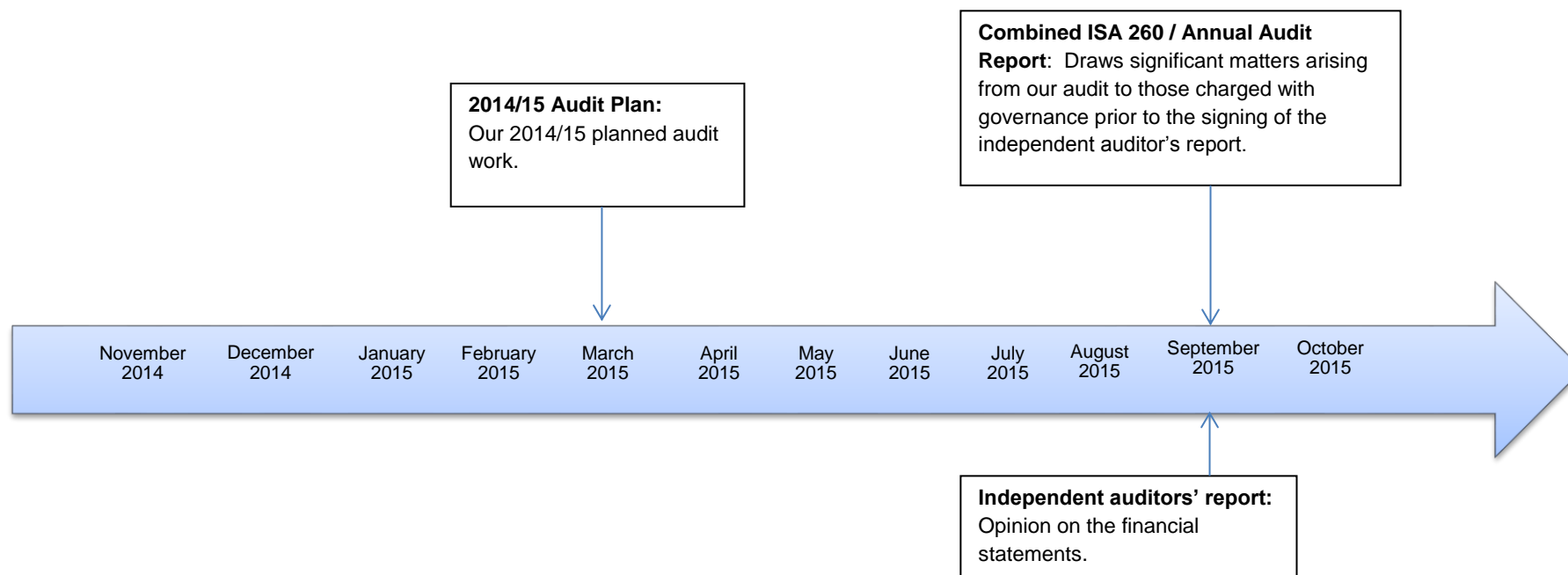
44. Stephen O'Hagan, Senior Audit Manager, Audit Services is your appointed auditor. The local audit team will be led by Carol Foster who will be responsible for day to day management of the audit and who will be your primary contact. Details of the experience and skills of our team are provided in Exhibit 2. The core team will call on other specialist and support staff as necessary.

### Exhibit 2: Audit team

Name	Experience
Stephen O'Hagan, CPFA Senior Audit Manager	Stephen has over 18 years experience of public sector audit with Audit Scotland, covering local government, central government, health and the education sector. Prior to joining Audit Scotland, Stephen worked in local government finance for 5 years.
Carol Foster, ACA Senior Auditor	Carol has over 9 years experience of public sector audit with Audit Scotland, covering local and central government. Previously Carol has worked in internal audit in a Scottish local authority and the private sector on a range of public and private sector audits.
Ross McDonald Auditor	Ross joined Audit Scotland's Health and Local Government team in October 2011. He is currently exam-qualified for the ICAS professional qualification and is expected to achieve the experience requirements for full qualification in the summer of 2015.
Kenny Stewart Auditor	Kenny has been involved in public sector audit for over 20 years, working for Audit Scotland and the National Audit Office.

# Appendix I: Planned audit outputs

The diagram below shows the key outputs planned for the Board in 2014/15.



# Appendix II: Significant audit risks

We undertake a risk-based audit whereby we focus on those areas where we have identified a risk of material misstatement in the accounts. This section shows how our audit approach focuses on the risks we have identified through our planning procedures. ISA 315 *Identifying and assessing the risks of material misstatement through understanding the entity and its environment* defines a significant risk as “an identified and assessed risk of material misstatement that, in the auditor’s judgement, requires special audit consideration.”

In this section we identify a range of risks facing the Lothian Valuation Joint Board, the related source of assurance received and the audit work we propose to undertake to secure additional assurance. The management of risk is the responsibility of the Board and its officers, with the auditor’s role being to review the arrangements put in place by management. Planned audit work, therefore, will not necessarily address all residual risks.

Audit Risk	Source of assurance	Assurance procedure
<b>Management override of controls</b> As stated in ISA 240, management is in a unique position to perpetrate fraud because of management’s ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.	<ul style="list-style-type: none"><li>N/A</li></ul>	<ul style="list-style-type: none"><li>Detailed testing of journal entries</li><li>Review of accounting estimates for bias</li><li>Evaluating significant transactions that are outside the normal course of business.</li></ul>

Audit Risk	Source of assurance	Assurance procedure
<p><b>Accounts payable ledger</b></p> <p>A number of adjustments were made in the 2013/14 accounts in respect of debit balances that had been posted erroneously to the Board's accounts payable ledger. The Board agreed to process the appropriate entries within the accounts payable ledger during 2014/15 to correct the ledger position. There is a risk that these adjustments have not been processed properly and the accounts payable ledger is incorrectly stated.</p>	<ul style="list-style-type: none"> <li>• Corrections made to remove debit balances not relating to the Board from accounts payable ledger</li> </ul>	<ul style="list-style-type: none"> <li>• Review of processed amendments</li> <li>• Detailed testing of debit balances in accounts payable ledger</li> </ul>
<p><b>Related party transactions</b></p> <p>The Board does not have a formal process in place for identifying and recording any external interests held by its senior officers therefore there is a risk that it may not identify all relevant related party transactions.</p>	<ul style="list-style-type: none"> <li>• Review of process</li> </ul>	<ul style="list-style-type: none"> <li>• Evaluation of changes to process</li> </ul>