

Item 7



Lothian Valuation Joint Board

Annual Audit Plan
2015/16

Prepared for Members of the Lothian Valuation Joint
Board

January 2016



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The Accounts Commission is a statutory body which appoints external auditors to Scottish local government bodies (www.audit-scotland.gov.uk/about/ac/). Audit Scotland is a statutory body which provides audit services to the Accounts Commission and the Auditor General (www.audit-scotland.gov.uk/about/).

The Accounts Commission has appointed Stephen O'Hagan as the external auditor of the Lothian Valuation Joint Board for the period 2011/12 to 2015/16.

This report has been prepared for the use of Lothian Valuation Joint Board and no responsibility to any member or officer in their individual capacity or any third party is accepted.

The information in this report may be used for the Accounts Commission's annual overview report on local authority audits published on its website and presented to the Local Government and Regeneration Committee of the Scottish Parliament.

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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 (the Board) financial statements.
 2. This report summarises the key challenges and risks facing the Board and sets out the audit work that we propose to undertake in 2015/16. 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.
- they give a true and fair view of the state of affairs of the Lothian Valuation Joint Board as at 31 March 2016 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 2015/16 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: internal controls and the adequacy of internal audit and the governance statement

Summary of planned audit activity

3. Our planned work in 2015/16 includes:
 - an audit of the financial statements and provision of an opinion on whether:

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 2016 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.

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. Planned management action being relied on for 2015/16 includes:
- comprehensive closedown procedures for the Board accompanied by a timetable issued to all relevant staff
 - 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 2015/16.
11. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. Internal audit services are provided by the Internal Audit section of City of Edinburgh Council. 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 to determine whether it has sound documentation standards and reporting procedures in place and complies with the main requirements of the Public Sector Internal Audit Standards (PSIAS).
12. 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 Governance Statement for inclusion within the Annual Accounts.

Materiality

13. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users of financial statements. A misstatement or omission, which would not normally be regarded as material by amount, 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.
14. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements both individually and collectively.
15. Based on our knowledge and understanding of the Board we have set our planning materiality at £69,000 (1% of gross expenditure).
16. We set a lower level, known as performance materiality, when defining our audit procedures. This is to ensure that uncorrected and undetected audit differences do not exceed our planning materiality. 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.

17. For 2015/16 performance materiality has been set at £41,000. We will report, to those charged with governance, all misstatements identified which are greater than £1,000.

Reporting arrangements

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 their 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. A proposed timetable for the audit of the 2015/16 financial statements is included at Exhibit 1 below. Discussions are still ongoing on the timing of Board dates to ensure compliance with the 2014 regulations.

Exhibit 1: Financial statements audit timetable

Key stage	Date
Consideration of unaudited financial statements by those charged with governance	20 June 2016
Latest submission date of unaudited council financial statements with complete working papers package	By 30 June 2016
Progress meetings with lead officers on emerging issues	As required during audit
Latest date for final clearance meeting with the Treasurer	By 31 August 2016
Agreement of audited unsigned financial statements, and issue of Annual Audit Report which includes the ISA 260 report to those charged with governance	By 31 August 2016
Board meeting date	TBC
Independent auditor's report signed	By 30 September 2016

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 Depute Assessor and relevant officers to confirm factual accuracy. Responses to 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. The combined ISA 260 and Annual Audit Report will be issued by 30 September.
24. All annual audit reports produced are published on Audit Scotland's website: www.audit-scotland.gov.uk.
25. Planned outputs for 2015/16 are summarised at [Appendix 1](#).

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. This is to provide reasonable assurance that those 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.

29. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. In significant cases we would change the audit team, however where there are potential issues that are not fundamental to the delivery of the audit, we advise the senior finance officer of the circumstances and of the steps we have taken to manage this. We are not aware of any other such relationships pertaining to the audit of the Board.

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 risk areas for the Board. We have categorised these risks into financial risks and wider dimension risks. The financial statements issues and risks, which require specific audit testing, are summarised below and detail contained in [Appendix 2](#).

Financial statement issues and risks

31. **Risk 1 – 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. **Risk 2 – Creation of a General Reserve:** The Board has reported an increase in its costs as a result of the implementation of Individual Electoral Registration (IER). To date, the additional costs

have been met through IER grant funding from the Cabinet Office however no IER grant has been awarded to date for 2016/17. Should additional IER grant not be received, the Board has discussed addressing the expected budget shortfall for 2016/17 by drawing down from the unspent requisitions creditor balance currently held to finance staffing exit costs. The Board is also considering transferring the existing creditor balance into a general reserve which can be drawn upon as required from 2016/17 onwards.

34. Should the Board decide to establish a general reserve during the 2015/16 financial year, it will need to ensure that this accounting change is properly presented and disclosed in the financial statements. We will review the presentation and disclosure of any changes made in the 2015/16 financial statements.

Wider dimension issues and risks

35. **Risk 3 – Cost Pressures:** The Board continues to manage the provision of services under a 2011/2012 level flat cash budget. IER funding is expected to cease at the end of 2015/16 and the Board will need to fund ongoing IER activity from existing resources. The Board has an established track record of managing expenditure pressures within its budgetary provision and is currently forecasting a projected net underspend of £95,000 for the 2015/16 financial year. However the budgetary pressures the Board faces from 2016/17 onwards are significant and present an unprecedented challenge to the Board to develop a sustainable budget position.

36. We will continue to monitor the Board's financial position, and review its progress towards developing a sustainable budget position going forward, through the course of our audit.
37. **Risk 4 – Review of Policies:** The Board reviewed and updated a number of its key policies in 2013, however this review did not include the existing Financial Regulations, Standing Orders and Scheme of Delegation. We understand that these documents are currently under review, with the outcome due to be reported to the Board in February 2016.
38. Whilst we recognise that the Board does carry out periodic reviews of its key policies, it is good practice to establish an agreed review cycle in order to ensure that policies are reviewed sufficiently regularly and remain fit for purpose.

National performance audit studies

39. Audit Scotland's Performance Audit and Best Value Group undertake a programme of studies on behalf of the Auditor General and Accounts Commission. In line with Audit Scotland's strategy to support improvement through the audit process, we will carry out work to collect relevant financial and performance information to inform Audit Scotland's national reports.

Fees and resources

Audit fee

40. Over the past four years, Audit Scotland has reduced audit fees by 24% in real terms, exceeding our 20% target. Due to further refinement of our audit approach we have been able to maintain audit fees for 2015/16 at the same level as last year. This represents an additional real term fee reduction of 1.6%.
41. In determining the audit fee we have taken account of the risk exposure of the Board, the planned 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 30 June 2016.
42. The proposed audit fee for the 2015/16 audit of Lothian Valuation Joint 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 studies and statutory reports by the Auditor General for Scotland
 - 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

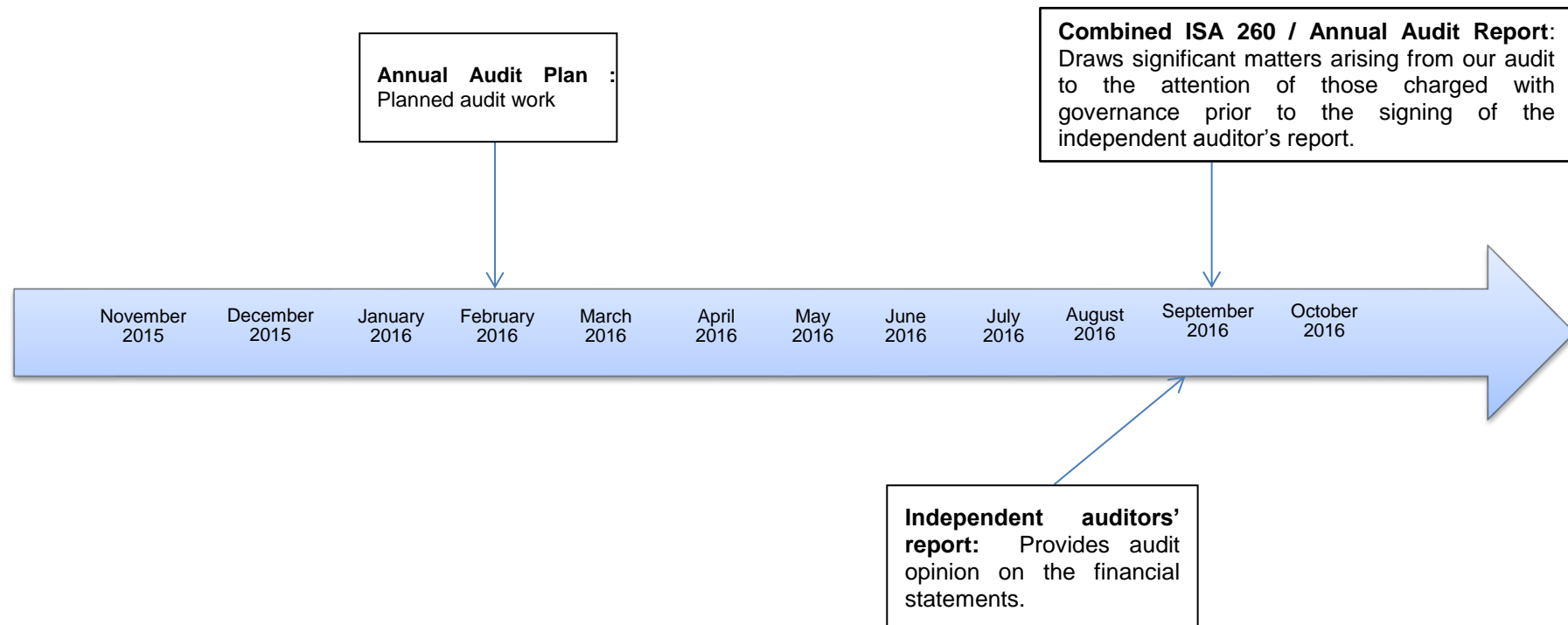
44. Stephen O'Hagan, Senior Audit Manager, Audit Services is your appointed auditor. The local audit team will be led by Carol Foster who will be responsible for day to day management of the audit and who will be your primary contact. Details of the experience and skills of our team are provided in Exhibit 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 19 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 10 years experience of public sector audit with Audit Scotland, covering local and central government. Previously, Carol worked in internal audit in a Scottish Local Authority and in the private sector on a range of public and private sector audits.
Joan Dalglish Auditor	Joan has worked in public sector audit with Audit Scotland for over 15 years, covering local government, central government and health.

Appendix 1: Planned audit outputs

The diagram below shows the key outputs planned for Lothian Valuation Joint Board in 2015/16.



Appendix 2: Significant audit risks

The table below sets out the key audit risks, the related sources of assurance received and the audit work we propose to undertake to address the risks during our audit work.

#	Audit Risk	Source of assurance	Audit assurance procedure
Financial statement issues and risks			
1	<p>Management Override of controls</p> <p>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.</p>	<ul style="list-style-type: none"> N/A 	<ul style="list-style-type: none"> Detailed testing of journal entries Review of accounting estimates for bias Evaluating significant transactions that are outside the normal course of business.
2	<p>Creation of a General Reserve</p> <p>The Board is considering transferring its unspent requisitions creditor balance into a general reserve which can be drawn upon as required from 2016/17 onwards. There is a risk that the presentation and disclosure of this change is not in accordance with the accounting framework requirements.</p>	<ul style="list-style-type: none"> The Board's Treasurer will identify the proposed accounting treatment for presentation and disclosure of this transaction in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom and review this with Audit Scotland prior to inclusion in the annual accounts. 	<ul style="list-style-type: none"> Detailed review of presentation and disclosure of the Board's accounts as part of the 2015/16 financial statements audit.

#	Audit Risk	Source of assurance	Audit assurance procedure
Wider dimension issues and risks			
3	<p>Cost Pressures</p> <p>Additional budget pressures are expected to arise from 2016/17 onwards as IER grant funding comes to an end whilst the Board continues to manage the provision of services under a flat cash budget. There is a risk that these financial pressures impact on the Board's service delivery and performance.</p>	<p>Increased workload is known to be required for both the electoral and valuation service during 2016/17 and beyond. It is recognised that the current high performance standards for delivery of statutory services will not be maintained in the forthcoming years. The following management actions will be undertaken:</p> <ul style="list-style-type: none"> • During 2016/17 all avenues for securing additional funding will be explored • Strategies for containing budget requirement to current levels will be considered • Progress will be reported to the Board 	<ul style="list-style-type: none"> • Review 2015/16 budget outturn information • Review 2016/17 budget • Consideration of the Board's progress towards developing a sustainable budget position from 2016/17
4	<p>Review of Policies</p> <p>Whilst the Board carries out periodic reviews of its key policies, it is good practice to establish an agreed review cycle in order to ensure that policies are reviewed sufficiently regularly and remain fit for purpose.</p>	<ul style="list-style-type: none"> • A timetable and action plan is currently being refined to ensure all Board policies are subject to regular review • The action plan highlights the currency, review date, and status of each policy. • The Financial Regulations, Standing Orders, Contract Standing Orders and Scheme of Delegation are at final review stage and are expected to go to the Board for approval on 8th February 	<ul style="list-style-type: none"> • Monitor progress towards establishing a review cycle for key policies