

HUNTINGDONSHIRE DISTRICT COUNCIL

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| Title: | External Audit Plan 2014/15 |
| Meeting/Date: | Corporate Governance Panel 25 March 2015 |
| Executive Portfolio: | Resources: Councillor J A Gray |
| Report by: | Head of Resources |
| Ward(s) affected: | All Wards |

Executive Summary:

PricewaterhouseCoopers are appointed by the Audit Commission as the Councils auditors and have been with the authority since 2010/11. In preparation for the 2014/15 audit, the auditors are required to inform “those charged with governance” what their plans are in respect of the forthcoming audit. The external audit plan (see Annex) shows:

- how the auditors intend to undertake the 2014/15 audit.
- the risks that they have to consider.
- considerations in respect of fraud.
- the external audit team, and
- the Audit Fee in respect of the 2014/15 audit.

Recommendation(s):

It is recommended that the Panel notes the External Audit Plan for 2014/15 (attached) and:

1. comments on the plan in general, and
2. gives the auditors its views in respect of:
 - i. the £90,000 triviality threshold, and
 - ii. fraud

1. PURPOSE

1.1 PricewaterhouseCoopers are appointed as the Council's external auditors by the Audit Commission. As part of this appointment they are required to audit the accounts of the Council. To achieve this they issue an External Audit Plan, which is annexed to this report. The plan shows:

- how the auditors intend to undertake the 2014/15 audit.
- the risks that they have to consider.
- considerations in respect of fraud.
- the external audit team, and
- the Audit Fee in respect of the 2014/15 audit.

2. BACKGROUND

2.1 The Audit Commission, as part of their responsibility of audit of local government, have appointed PricewaterhouseCoopers as the Councils external auditor.

2.2 Part of their responsibility is the audit of the Councils accounts, the Annual Financial Report and as part of achieving this responsibility they issue an Audit Plan. The key auditor's responsibilities of the audit plan are:

- Perform an audit of the accounts in accordance with the Auditing Practice Board's International Standards on Auditing.
- Report to the National Audit Office on the accuracy of the consolidation pack which the Authority is required to prepare for the Whole of Government Accounts.
- Form a conclusion on the arrangements the Authority has made for securing economy, efficiency and effectiveness in its use of resources.
- Consider the completeness of disclosures in the Authority's annual governance statement, identify any inconsistencies with the other information of which we (*the auditors*) are aware from our work and consider whether it complies with CIPFA / SOLACE guidance.
- Consider whether, in the public interest, we (*the auditors*) should make a report on any matter coming to our notice in the course of the audit.
- Determine whether any other action should be taken in relation to our (*the auditors*) other responsibilities under the Audit Commission Act.
- Issue a certificate that we (*the auditors*) have completed the audit in accordance with the requirements of the Audit Commission Act 1998 and the Code of Practice issued by the Audit Commission

2.3 As the Corporate Governance Panel has responsibility for approving the Councils Annual Financial Report and the Annual Governance Statement, the Panel is asked to note the report and comment where it considers necessary.

3. AUDIT APPROACH FOR 2014/15

3.1 PwC's audit is built on a foundation of smart people, a smart approach and smart technology. This together with their six-step audit process (see below), results in an audit that is robust, insightful and relevant. The core elements of the audit are:

3.2 STEP 1: Client acceptance and independence

Audit engagement begins with an evaluation of the Council through the external auditor's 'acceptance & continuance system' which highlights an overall engagement risk score and highlights areas of heightened risk.

3.3 **STEP 2: Deep business understanding**

Audit will review the processes that the Authority has put in place to meet the increasingly challenging environment within which it operates. This will include a review of the Council's newly introduced zero based budgeting process and work involved in developing Shared Services.

3.4 **STEP 3: Relevant risks**

The two main categories in respect of the audit of the accounts are those relating to significant or elevated risks and the definitions of each are as follows:

- **Significant**
Those risks with the highest potential for material misstatement due to a combination of their size, nature and likelihood and which, in our judgement, require specific audit consideration.
- **Elevated**
Although not considered significant, the nature of the (£) balance/area requires specific consideration

3.4.1 **Significant**

i. Management override of controls

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. Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and thus a significant risk.

For example: accounting policies; estimation bases; journal entries; key controls in respect of bank reconciliation, purchasing and loans.

ii. Revenue and expenditure recognition

When identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue/expenditure recognition, evaluate which types of revenue/expenditure, revenue/expenditure transactions or assertions give rise to such risks.

For example: key controls in respect of revenue income and expenditure; application of the Code of Practice on Local Authority Accounting; detailed testing of areas considered to be of greatest risk.

3.4.2 **Elevated: Valuation of non-current assets**

This will require a review of the processes surrounding asset valuations.

3.4.3 **Other areas for audit review**

The auditors will review the following areas as they are considered areas that may affect the financial statements but are not considered significant or elevated:

i. NDR appeals provision

As part of the 2013/14 accounts, the Council used an external advisor to quantify the potential provision in respect of NDR appeals. The auditors will again review this provision to ensure that the risk due to incomplete or unrepresentative data is minimised.

ii. Value for Money

The auditors will again gain assurance that the Authority has the required financial resilience to continue to function, providing statutory services over the medium to long term. This is considered as a significant risk on the Value for Money opinion, not in relation to the opinion on the accounts.

3.5 STEP 4: Intelligent scoping - Materiality

Materiality for 2014/15 has been set at £1.852m, which is based on 2% of 2013/14 expenditure.

Further, the auditors have set the “triviality” level as £90,000 i.e. errors that will not have a material effect on the financial statements, even if accumulated. The auditors have requested that the views of the Panel in respect of the Triviality threshold are sought. Please note that this is the same level as was applied in 2013/14.

Opinion of Responsible Financial Officer:

£90,000 is a fair level for the triviality threshold. It is “large enough” to absorb the inevitable minor errors and omissions that occur within accounts closure but not too large to distort the final “financial outturn”. The types of error that are typically included within this threshold include:

- Expenditure/income that has been miscategorised – no net impact.
- Non-cash items where estimation techniques followed by the Council differ to those calculated by the auditors.

3.6 STEP 5: Robust testing

The audit is risk based and work is focused on those areas which are most likely to lead to a material misstatement. Further, audit work is conducted in such a way so there is full consideration and evaluation of any impacts so the final audit has “no surprises” at the year-end. There is also appropriate testing in respect of Value for Money, the Annual Governance Statement and the Whole of Government Accounts

3.7 STEP 6: Meaningful conclusions

The auditors fundamentally believe their audits should be valuable to their clients and to properly fulfil their role as auditors. Consequently, the primary objective is to form an independent audit opinion on the financial statements. Further audit value is achieved from the same source as audit quality so the work that is undertaken as part of the support of the audit opinion also means that the auditors should be adding value through the auditors observations, recommendations and insights.

4 FRAUD

The auditors will review the Councils management responsibility in respect of fraud and whether this is being discharged appropriately.

As part of the audit of the Annual Financial Report the auditors will enquire of the Panel:

- Whether you have knowledge of fraud; whether this is actual, suspected or alleged, including those involving management?
- What fraud detection or prevention measures (e.g. whistleblower lines) are in place in the entity?
- What role you have in relation to fraud?
- What protocols / procedures have been established between those charged with governance and management to keep you informed of instances of fraud, either

actual, suspected or alleged?

5. THE PRICEWATERHOUSECOOPERS AUDIT TEAM

The three principal audit team members are:

- **Engagement Leader;** Clive Everest.
It is Clive's fourth year as engagement leader with the Council.
- **Engagement Manager;** Dan Deacon
Dan has taken over from Jacqui and is an experienced audit manager within the local government sector.
- **Team Leader;** Chris Paterson
Chris has worked previously at the Council and will lead the audit field team.

6. AUDIT FEE

6.1 The total audit "scale fee" for 2014/15, as set by the Audit Commission, is £98,861; this represents a significant reduction of 39% since 2011/12. A summary breakdown of audit fees is shown below:

| Audit Fee | | | | | |
|---|---------------------------|---------------------------|---------------------------|--------------------------|-------------------------------------|
| | Actual 2011/12 | Actual 2012/13 | Actual 2013/14 | Scale 2014/15 | Change since 2011/12 |
| | £ | £ | £ | £ | % |
| Audit work performed under the Code of Audit Practice (*) | 124,301 | 77,768 | 83,834 | 78,481 | -37 |
| Certification of Claims and Returns | 35,000 | 24,484 | 26,269 | 18,380 | -47 |
| Total | 159,301 | 102,252 | 110,103 | 96,861 | -39 |
| * This includes audit work relating to the Annual Financial Report, Value for Money and Whole of Government Accounts | | | | | |

6.2 The Panel will note that there is a significant reduction in the fees relating to the Certification of Claims and Return for 2014/15 when compared to the 2013/14; however what this does not reflect is any additional work that may be required if during the audit errors are found that requires additional testing.

6.3 However, as noted in paragraph 3.3 the auditors will undertake additional non-recurrent work to respond to local audit risks in respect of the Value for Money opinion. The main element of this work will be around the Councils new "Zero Based Budgeting" approach. The work will review the new processes, evaluate the underlying assumptions in the Medium Term Financial Strategy, review supporting savings plans and verify the calculations involved in setting the budget; this is estimated to incur an audit fee of up to £7,500 (this is included in the numbers within the table above).

6.4 The auditors will update those charged with governance regarding the impact of this additional testing on the proposed audit fees in due course. The auditors have based the fee level on the following assumptions:

- Officers meeting the timetable of deliverables, which we will agree in writing;
- We do not review more than three iterations of the statement of accounts and accounting statements;
- We are able to obtain assurance from your management controls;

- No '40+' testing is required for the certification of the Housing Benefit return;
- No significant further work is required on the zero based budgeting approach and the NDR appeals calculation;
- No significant changes being made by the Audit Commission to the local value for money work requirements; and
- Our value for money conclusion and accounts opinion being unqualified.

If the above prove to be unfounded, the auditors will seek a variation order to the agreed fee, to be discussed and agreed in advance with you and the Audit Commission.

7. LEGAL IMPLICATIONS

7.1 There are no direct legal implications arising from this report.

8. RESOURCE IMPLICATIONS

8.1 The 2014/15 budget for External Audit Fees is £116,682. This should be sufficient to meet the scale fee of £96,861 and any additional charge that may accrue if errors are found following the certification of grants and returns. For 2015/16 this budget, following zero based budgeting has been reduced to £90,000, reflecting further efficiencies once the external audit transfers to Ernst and Young for 2015/16 onwards.

LIST OF APPENDICES INCLUDED


Annex – Huntingdonshire District Council “External Audit Plan 2014/15”

BACKGROUND PAPERS


Working papers in Financial Services.

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