

Audit strategy

Wyre Forest District Council

Audit 2010/11

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

Contents

| | |
|---|-----------|
| Introduction | 2 |
| Responsibilities | 3 |
| Fee for the audit | 4 |
| Auditors report on the financial statements..... | 5 |
| Value for money conclusion | 10 |
| The audit team..... | 12 |
| Appendix 1 Basis for fee | 14 |
| Appendix 2 Independence and objectivity | 15 |
| Appendix 3 Glossary | 17 |

Introduction

1 This plan sets out the audit work that I propose to undertake for the audit of financial statements 2010/11 and the VFM conclusion. The plan is based on the Audit Commission's risk-based approach to audit planning. It reflects:

- audit work specified by the Audit Commission for 2010/11;
- current national risks relevant to your local circumstances; and
- your local risks.

2 As your appointed auditor, the audit of the financial statements I deliver to you is governed by International Standards on Auditing (ISAs). These standards prescribe the basic principles and essential procedures, with the related guidance, which govern my professional conduct as your auditor.

3 As with all guidance and frameworks, auditing standards are revised and updated, often in a piecemeal fashion. However, in 2009 the auditing profession completed a comprehensive project to improve the clarity of all the ISAs. This is known as the Clarity Project.

4 One of the main objectives of the Clarity Project was to promote greater consistency of application between auditors. This has been done by reducing the ambiguity within existing ISAs and improving their overall readability and understandability.

5 The new clarified framework will apply to my audit of your 2010/11 financial statements. Because of the new standards, you can expect to see some changes in the way my audit team delivers your audit and the information they seek from you. These changes are highlighted throughout the strategy.

6 For 2010/11 the Audit Commission requires me to give my statutory VFM conclusion on your arrangements to secure economy, efficiency and effectiveness in relation to two criteria.

- Securing financial resilience – focusing on whether the Council is managing its financial risks to secure a stable financial position for the foreseeable future.
- Challenging how the Council secures economy, efficiency and effectiveness – focusing on whether the Council is prioritising its resources within tighter budgets and improving productivity and efficiency.

7 This strategy also includes the work required in order for me to issue a VFM conclusion.

Responsibilities

8 The Audit Commission's Statement of Responsibilities of Auditors and of Audited Bodies sets out the respective responsibilities of the auditor and the audited body. The Audit Commission has issued a copy of the Statement to every audited body.

9 The Statement summarises where the different responsibilities of auditors and of the audited body begin and end, and my audit work is undertaken in the context of these responsibilities.

10 I comply with the statutory requirements governing my audit work, in particular:

- the Audit Commission Act 1998; and
- the Code of Audit Practice.

Fee for the audit

11 The fee for the audit is £112,890 as indicated in my letter of 27 April 2010.

12 In setting the fee, I have assumed that:

- the level of risk in relation to the audit of accounts is consistent with that for 2009/10;
- good quality working papers will continue to be supplied to support the financial statements;
- Internal Audit undertakes appropriate work on material systems during the year ended 31 March 2011; and
- significant additional work will not be required to address any weaknesses in controls.

13 Based upon the above and taking into accounts matters reported in my Annual Governance Reports the fee proposed for 2010/11 is 2.86 per cent above the scale fee indicated by the Audit Commission and is within the normal level of variation specified by the Commission. If the above assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee. Where this is the case, I will discuss this in the first instance with the Director of Finance and I will issue supplements to the strategy to record any revisions to the risk and the impact on the fee.

Fee rebate

14 The published fee scale for 2010/11 included a 6 per cent increase to cover the costs of additional work arising from the introduction of International Financial Reporting Standards (IFRS). In July 2009, in recognition of the financial pressures that public bodies are facing in the current economic climate, the Commission confirmed that it would subsidise the 'one-off' element of the cost of transition to IFRS for local authorities. The council received a rebate in April 2010 of £6,453.

15 The Commission has also confirmed that district councils will receive a further rebate of 1.5 per cent of the scale fee, hence the net fee after rebates is £104,913.

16 Further information on the basis for the fee is set out in Appendix 1.

Specific actions the Council could take to reduce its audit fees

17 The Audit Commission requires its auditors to inform audited bodies of specific actions it could take to reduce its audit fees. As in previous years, I will work with staff to identify any specific actions that the Council could take and to provide ongoing audit support.

Auditors report on the financial statements

18 I will carry out the audit of the financial statements in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board (APB).

19 I am required to issue an audit report giving my opinion on whether the accounts give a true and fair view of the financial position of the Councils at 31 March 2011.

Materiality

20 I will apply the concept of materiality in both planning and performing the audit, in evaluating the effect of any identified misstatements, and in forming my opinion.

Identifying opinion audit risks

21 I need to understand fully the audited body to identify any risk of material misstatement (whether due to fraud or error) in the financial statements. I do this by:

- identifying the business risks facing the Council, including assessing your own risk management arrangements;
- considering the financial performance of the Council;
- assessing internal control - including reviewing the control environment, the IT control environment and Internal Audit; and
- assessing the risk of material misstatement arising from the activities and controls within the Council information systems.

I have considered the additional risks that are appropriate to the current opinion audit and have set these out overleaf.

Table 1: Specific risks

| Risk area | Audit response |
|---|--|
| <p>IFRS Restatement</p> <p>The 2009/10 financial statements need to be restated using the International Financial Reporting Standards. Officers have already provided the restated balance sheet and will provide the remaining statements and notes by March 2011.</p> <p>There is a risk that the accounts may not be fully compliant with the IFRS.</p> | <ul style="list-style-type: none"> ■ Liaise with relevant finance staff to ensure that key decisions that result in significant changes are discussed in advance. ■ Audit the changes to the 2009/10 financial statements prior to the main 2010/11 audit. |
| <p>Purchase order payment system</p> <p>In 2010/11 a new module has been added to the general ledger that enables orders to be raised, authorised and goods received notes to be received electronically.</p> <p>There is a risk that the system may not be operating as desired and thus expenditure misstated.</p> | <p>We will update our understanding of the system through review of the work undertaken by internal audit and a walkthrough of the system. We will then consider what additional testing we will need to undertake to address any risks.</p> |
| <p>Icelandic Investments</p> <p>The accounts contain some significant estimates and specific accounting entries in relation to the Icelandic Investments. Any errors in these assumptions could have material impact.</p> <p>There is an ongoing legal challenge to Councils' 'preferred status'. This could be resolved by the year end.</p> | <p>We will review the accounting entries in relation to the Icelandic investments and ensure that these are consistent with up to date guidance. We will continue to monitor the position in relation to the legal challenge and consider any implications for the accounts.</p> |

Testing strategy

22 On the basis of risks identified above I have developed a testing strategy, similar to previous years, which consists of a combination of testing key controls of testing key controls and/or substantive tests of transaction streams and material account balances at year end.

23 My testing can be carried out both before and after the draft financial statements have been produced (pre and post- statement testing). However, one of the changes brought about by the ISA Clarity project is a greater focus on tests of a substantive nature. The testing strategy has been developed alongside your finance team to maximise the efficiency of the approach.

24 All of the controls assurance work will be completed by April 2011 and wherever possible, I will complete some of the substantive testing earlier in the year before the financial statements are available for audit. Wherever possible I will seek to rely on the work of Internal Audit to help me meet my responsibilities.

ISA clarity

25 As well as a greater focus on substantive testing there are a number of other specific changes. These include the following.

- Journals. ISA (UK&I) 330 (The Auditor's response to assessed risks), requires me to review all material year-end adjustment journals. I had previously sample checked these.
- Related Party Transactions. ISA (UK&I) 550 (Related parties) requires me to review your procedures for identifying related party transactions and obtain an understanding of the controls that you have established to identify such transactions. I will also carry out testing to ensure the related party transaction disclosures you make in the financial statements are complete and accurate. This is a clarification of existing practice.
- Deficiencies in internal control. ISA (UK&I) 265 (Communicating Deficiencies In Internal Control to Those Charged With Governance And Management) is a new standard. It requires that if I identify a deficiency in any of your internal controls during the audit, I will undertake more audit testing to decide whether the deficiency is significant. If I decide the deficiency is significant, I will report it in writing to the Audit and Risk Committee as those charged with governance.

26 The most noticeable change is to the way I review accounting estimates. ISA (UK&I) 540 (Auditing Accounting Estimates, Including Fair Value Accounting Estimates, And Related Disclosures) requires me to look at your accounting estimates in detail. As part of my audit I will request a list of these from you. I will need to know in particular:

- the process you use to make your accounting estimates;
- the controls you use to identify them;
- whether you use an expert to help you in making the accounting estimates;
- whether any alternative estimates have been discussed and why they have been rejected;
- how you assess the degree of estimation uncertainty (this is the uncertainty arising because the estimate cannot be precise or exact) ;
and
- the prior year's accounting estimates outcomes, and whether there has been a change in the method of calculation for the current year.

IFRS restatement

27 As noted in table 1 above the 2009/10 financial statements need to be restated using the International Financial Reporting Standards (IFRS). There will be a number of changes to the 2009/10 financial statement including:

- classification of leases;
- inclusion of employee benefits accrual; and
- removal of some disclosure such as building control and new disclosures such as assets held for sale.

Officers have already provided the restated balance sheet and will provide the remaining statements by March 2011. We will aim to complete our review of the restated accounts prior to the submission of the 2010/11 financial statements.

Key milestones and deadlines

28 The key stages in the process of producing and auditing the financial statements are shown in table 2.

Table 2: **Audit strategy key milestones**

| Task | Deadline |
|---|---|
| Receipt of the IFRS restated 2009/10 financial statements | 8 April 2011 |
| Interim work covering controls testing, early substantive testing and review of any Internal Audit work | April 2011 |
| Receipt of the Financial statements for audit | 30 June 2011* |
| Forwarding of audit working papers to the auditor. | At the latest by the start of the onsite audit 11 July 2011 |
| Start of detailed testing. | 11 July 2011 |
| Progress meetings with finance staff | Weekly |
| Appointed day | 1st September |
| Exit meeting with Financial Accountants | Early September |
| Present report to those charged with governance at the Audit and Accounts Committee. | 26 September 2011* |
| Issue of opinion. | Before 30 September 2011* |

* *Still draft*

Value for money conclusion

29 As your appointed auditor I have a continuing statutory responsibility to give a conclusion on whether the Council has proper arrangements in place for securing economy, efficiency and effectiveness in its use of resources (commonly known as my value for money (VFM) conclusion). The work I undertake is directed by the Audit Commission which announced in October 2009 that it would be reviewing its approach to this work to ensure that it was more targeted and gave better value.

30 The aim is to now focus this work on an auditor's core responsibilities and on local audit issues. For 2010/11 I am required to give my statutory VFM conclusion on your arrangements to secure economy, efficiency and effectiveness in relation to:

- securing financial resilience – focusing on whether the Council is managing its financial risks to secure a stable financial position for the foreseeable future; and
- challenging how the Council secures economy, efficiency and effectiveness – focusing on whether the Council is prioritising its resources within tighter budgets and improving productivity and efficiency.

31 The VFM conclusion will be in the form of either an unqualified or, if I am not satisfied that the Council has adequate arrangements in place, qualified VFM conclusion. The key messages from my VFM conclusion work, including suggested areas for improvement, will be reported to the Audit and Accounts Committee via the annual governance report and annual audit letter.

32 I have considered the risks that are appropriate to the current value for money conclusion and have set these out overleaf.

Table 3: **VFM conclusion risks**

| Risk area | Audit response |
|--|---|
| Securing financial resilience | |
| <p>Financial Planning: There is an implicit risk that the Council's financial planning may not be robust.</p> | <ul style="list-style-type: none"> ■ Review the medium term financial plans and the 2011/12 budgets to ensure that the Council has taken appropriate account of the current economic climate and the plans are supported by detailed and robust assumptions. Reviewing your reporting on progress against these plans. |
| <p>Savings Plan: There is a risk that the Council's savings plans are not being properly managed and delivered.</p> | <ul style="list-style-type: none"> ■ Review the process for the identification, monitoring and reporting of your savings plans. |
| <p>Single Site: This is a significant capital project and thus we will review evidence that this will provide value for money.</p> | <ul style="list-style-type: none"> ■ Following the receipt of tenders, we will review the updated business case. |

The audit team

33 The key members of the audit team for the 2010/11 audit are shown in the table below.

Table 4: **Audit team**

| Name | Contact details | Responsibilities |
|-----------------------------------|---|---|
| Elizabeth Cave Engagement Lead | l-cave@audit-commission.gov.uk 0844 798 7552 | Responsible for the overall delivery of the audit including the quality of outputs, signing the opinion and conclusion, and liaison with the Chief Executive. |
| Zoe Thomas Audit Manager | z-thomas@audit-commission.gov.uk 0844 798 7557 | Manages and coordinates the different elements of the audit work. Key point of contact for the Executive Director (Resources and Support Services). |
| Kathryn Lewis Team Leader | k-lewisl@audit-commission.gov.uk 0844 798 3957 | Responsible for the day-to-day delivery of the audit work. |

Independence and objectivity

34 I am not aware of any relationships that may affect the independence and objectivity of the District Auditor and the audit staff, which I am required by auditing and ethical standards to communicate to you.

35 I comply with the ethical standards issued by the APB and with the Commission's requirements in respect of independence and objectivity as summarised in appendix 2.

Quality of service

36 I am committed to providing you with a high quality service. If you are in any way dissatisfied, or would like to discuss how I can improve my service, please contact me in the first instance. If I am unable to satisfy your concerns, you have the right to make a formal complaint to the Audit Commission. The complaints procedure is set out in the leaflet 'Something to Complain About' which is available from the Commission's website or on request.

Planned outputs

37 My team will discuss and agree reports with the right officers before issuing them to the Audit Committee.

Table 5: **Planned outputs**

| Planned output | Indicative date |
|--|-----------------|
| Annual governance report | September 2011 |
| Auditor’s report giving an opinion on the financial statements | September 2011 |
| Annual audit letter | November 2011 |

Appendix 1 Basis for fee

The Audit Commission is committed to targeting its work where it will have the greatest effect, based upon assessments of risk and performance. This means planning work to address areas of risk relevant to our audit responsibilities and reflecting this in the audit fees.

The risk assessment process starts with the identification of the significant financial and operational risks applying to the Council with reference to:

- my cumulative knowledge of the Council;
 - planning guidance issued by the Audit Commission;
 - the specific results of previous and ongoing audit work;
- interviews with Council officers; and
- liaison with Internal Audit.

Assumptions

In setting the fee, I have assumed the following.

- The level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2009/10.
- You will inform us of significant developments impacting on the audit.
- Internal Audit meets the appropriate professional standards.
- Internal Audit undertakes appropriate work on all systems that provide material figures in the financial statements sufficient that I can place reliance for the purposes of our audit.
- you provide:
 - good quality working papers and records to support the financial statements by 11 July;
 - information asked for within agreed timescales;
 - prompt responses to draft reports; and
- there is no allowance for extra work needed to address questions or objections raised by local government electors.

Where these assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee.

Appendix 2 Independence and objectivity

Auditors appointed by the Audit Commission are required to comply with the Commission's Code of Audit Practice and Standing Guidance for Auditors, which defines the terms of the appointment. When auditing the financial statements, auditors are also required to comply with auditing standards and ethical standards issued by the Auditing Practices Board (APB).

The main requirements of the Code of Audit Practice, Standing Guidance for Auditors and the standards are summarised below.

International Standard on Auditing (UK and Ireland) 260 (Communication of audit matters with those charged with governance) requires that the appointed auditor:

- discloses in writing all relationships that may bear on the auditor's objectivity and independence, the related safeguards put in place to protect against these threats and the total amount of fee that the auditor has charged the client; and
- confirms in writing that the APB's ethical standards are complied with and that, in the auditor's professional judgement, they are independent and their objectivity is not compromised.

The standard defines 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case, the appropriate addressee of communications from the auditor to those charged with governance is the Audit Committee. The auditor reserves the right, however, to communicate directly with the Council on matters which are considered to be of sufficient importance.

The Commission's Code of Audit Practice has an overriding general requirement that appointed auditors carry out their work independently and objectively, and ensure that they do not act in any way that might give rise to, or could reasonably be perceived to give rise to, a conflict of interest. In particular, appointed auditors and their staff should avoid entering into any official, professional or personal relationships which may, or could reasonably be perceived to, cause them inappropriately or unjustifiably to limit the scope, extent or rigour of their work or impair the objectivity of their judgement.

The Standing Guidance for Auditors includes a number of specific rules.

The key rules relevant to this audit appointment are as follows.

- Appointed auditors should not perform additional work for an audited body (i.e. work over and above the minimum required to meet their statutory responsibilities) if it would compromise their independence or might give rise to a reasonable perception that their independence could be compromised. Where the audited body invites the auditor to carry out risk-based work in a particular area that cannot otherwise be justified as necessary to support the auditor's opinion and conclusions, it should be clearly differentiated within the Audit and Inspection Plan as being 'additional work' and charged for separately from the normal audit fee.
- Auditors should not accept engagements that involve commenting on the performance of other auditors appointed by the Commission on Commission work without first consulting the Commission.
- The District Auditor responsible for the audit should, in all but the most exceptional circumstances, be changed at least once every seven years, with additional safeguards in the last two years.
- The District Auditor and senior members of the audit team are prevented from taking part in political activity on behalf of a political party, or special interest group, whose activities relate directly to the functions of local government or NHS bodies in general, or to a particular local government or NHS body.

The District Auditor and members of the audit team must abide by the Commission's policy on gifts, hospitality and entertainment.

Appendix 3 Glossary

Audit of the accounts

The audit of the accounts of an audited body comprises all work carried out by auditors in accordance with the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

Audited body

A body to which the Audit Commission is responsible for appointing the external auditor, comprising both the members of the body and its management (the senior officers of the body). Those charged with governance are the members of the audited body. (See also 'Members' and 'Those charged with governance'.)

Auditing Practices Board (APB)

The body responsible in the UK for issuing auditing standards, ethical standards and other guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

Auditing standards

Pronouncements of the APB, which contain basic principles and essential procedures with which auditors are required to comply, except where otherwise stated in the auditing standard concerned.

Auditor(s)

Auditors appointed by the Audit Commission.

Code (the)

The Code of Audit Practice.

Commission (the)

The Audit Commission for Local Authorities and the National Health Service in England.

Directors

Members of the board who are collectively and individually responsible for the overall direction and control of the audited body. In NHS bodies there is a unitary board, consisting of executive members and part-time non-executive members, chaired by a non-executive member. The chief executive is responsible to the board for the day-to-day management of the organisation but, as accountable officer, is also responsible to the Department of Health for the proper stewardship of public money and assets. (See also 'Those charged with governance' and 'Audited body').

Ethical standards

Pronouncements of the APB that contain basic principles that apply to the conduct of audits and with which auditors are required to comply, except where otherwise stated in the standard concerned.

Financial statements

The annual statement of accounts or accounting statements that audited bodies are required to prepare, which summarise the accounts of the audited body, in accordance with regulations and proper practices in relation to accounts.

Internal control

The whole system of controls, financial and otherwise, that is established in order to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

Materiality (and significance)

The APB defines this concept as 'an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor's report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects'.

The term 'materiality' applies only in relation to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, in addition to their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

The concept of 'significance' applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit in relation to the financial statements. Significance has both qualitative and quantitative aspects.

Members

The elected, or appointed, members of local government bodies who are responsible for the overall direction and control of the audited body. (See also 'Those charged with governance' and 'Audited body'.)

Regularity (of expenditure and income)

Whether, subject to the concept of materiality, the expenditure and income of the audited body have been applied for the purposes intended by parliament, and whether they conform with the authorities that govern them.

Remuneration report

Audited bodies are required to produce, and publish with the financial statements, a remuneration report that discloses the salary and pension entitlements of senior managers.

Statement on internal control/Annual Governance Statement

Local government bodies are required to publish a statement on internal control (SIC) with their financial statements (or with their accounting statements in the case of small bodies). The disclosures in the SIC are supported and evidenced by the body's assurance framework. At local authorities the SIC is known as the Annual Governance Statement and is prepared in accordance with guidance issued by CIPFA. Police authorities also produce a SIC in accordance with relevant CIPFA guidance. Local probation trusts are required to prepare a SIC in accordance with the requirements specified by HM Treasury in Managing Public Money.

NHS bodies are required to publish a statement on internal control (SIC) with their financial statements. Specific guidance on the preparation of the SIC is issued by the Department of Health. The chief executive, as accountable officer, is required to sign the SIC on behalf of the board. The disclosures in the SIC are supported and evidenced by the body's assurance framework.

Those charged with governance

Those charged with governance are defined in auditing standards as ‘those persons entrusted with the supervision, control and direction of an entity’.

In local government bodies, those charged with governance, for the purpose of complying with auditing standards, are:

- for local authorities – the full council, audit committee (where established) or any other committee with delegated responsibility for approval of the financial statements;
- for police or fire authorities – the full authority, audit committee (where established) or other committee with delegated responsibility for approval of the financial statements;
- for local probation boards and trusts – the board or audit committee; and
- for other local government bodies – the full authority or board or council, audit committee (where established) or any other committee with delegated responsibility for approval of the financial statements.

Audit committees are not mandatory for local government bodies, other than police authorities and local probation trusts. Other bodies are expected to put in place proper arrangements to allow those charged with governance to discuss audit matters with both internal and external auditors. Auditors should satisfy themselves that these matters, and auditors’ reports, are considered at the level within the audited body that they consider to be most appropriate.

In NHS bodies, those charged with governance, for the purpose of complying with auditing standards, are the board of directors and, in respect of certain responsibilities, the audit committee on behalf of the board. Audit committees are mandatory in NHS bodies and are non-executive committees of the board. The main objective of the audit committee is to contribute independently to the board’s overall process for ensuring that an effective internal control and risk management system is maintained.

Whole of Government Accounts

The Whole of Government Accounts initiative is to produce a set of consolidated financial accounts for the entire UK public sector on commercial accounting principles. Local government bodies, other than probation boards and trusts, are required to submit a consolidation pack to the department for Communities and Local Government which is based on, but separate from, their statutory accounts.

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The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors, members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
- any third party.



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