

EAST LOTHIAN COUNCIL

Annual Audit Plan 2017/18



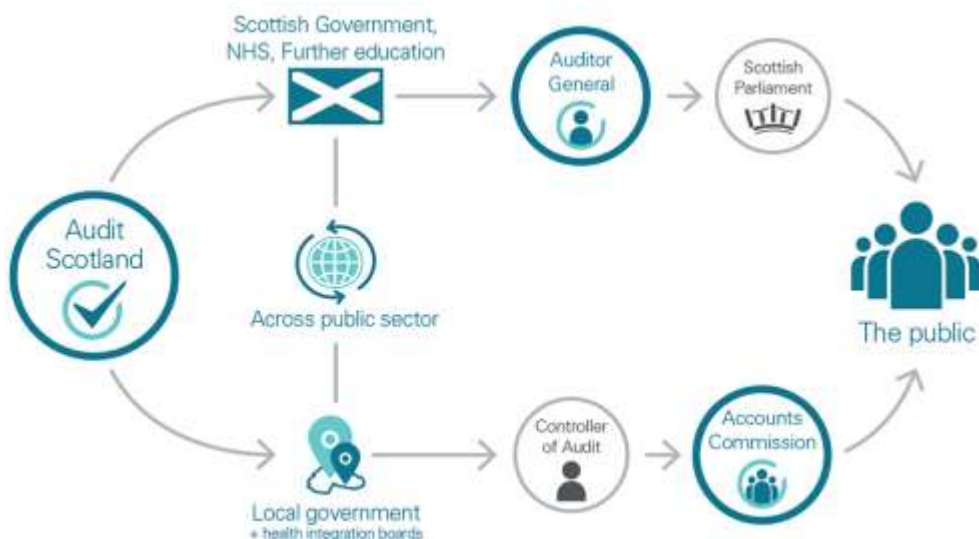
 AUDIT SCOTLAND

Prepared for East Lothian Council
February 2018

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non – executive board chair, and two non – executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world – class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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Risks and planned work

1. This annual audit plan contains an overview of the planned scope and timing of our audit and is carried out in accordance with International Standards on Auditing (ISAs), the [Code of Audit Practice](#), and any other relevant guidance. This plan identifies our audit work to provide an opinion on the financial statements and related matters and meet the wider scope requirements of public sector audit.

2. The wider scope of public audit contributes to conclusions on the appropriateness, effectiveness and impact of corporate governance, performance management arrangements and financial sustainability.

Audit risks

3. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for East Lothian Council (ELC). We have categorised these risks into financial risks and wider dimension risks. The key audit risks which require specific audit testing are detailed in [Exhibit 1](#).

Exhibit 1: 2017/18 Key audit risks

| Audit Risk | Source of assurance | Planned audit work |
|---|---|--|
| Financial statement issues and risks | | |
| <p>1 Risk of management override of controls</p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p> | <p>Owing to the nature of this risk assurances from management are not applicable in this instance.</p> | <p>Detailed testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Focused testing of accruals and prepayments.</p> <p>Evaluation of significant transactions that are outside the normal course of business.</p> |
| <p>2 Risk of fraud over income</p> <p>ELC receives a significant amount of income in addition to Scottish Government funding. The extent and complexity of income means that, in accordance with ISA 240, there is an inherent risk of fraud.</p> | <p>All income is reviewed monthly.</p> <p>Monthly monitoring and performance reporting for council tax and rental income.</p> <p>Specific grant/account codes used for other income and verified via monthly monitoring and bank reconciliations.</p> | <p>Analytical procedures on income streams.</p> <p>Detailed testing of revenue transactions focusing on the areas of greatest risk.</p> |

| Audit Risk | Source of assurance | Planned audit work |
|--|---|---|
| <p>3 Risk of fraud over expenditure</p> <p>Most public sector bodies are net expenditure bodies and therefore the risk of fraud is more likely to occur in expenditure.</p> | <p>Clear procedures in place for staff.</p> <p>Financial authorisation limits in place for authorising and approving expenditure.</p> <p>Budget monitoring and review with significant variances investigated and discussed with budget holders.</p> | <p>Reviews work on the National Fraud Initiative matches.</p> <p>Assess high level key controls in areas of significant expenditure.</p> <p>Focused substantive testing of expenditure and housing benefit transactions.</p> |
| <p>4 Estimation and judgements</p> <p>There is a significant degree of subjectivity in the measurement and valuation of the material account areas such as non current assets and provisions. This subjectivity represents an increased risk of misstatement in the financial statements.</p> | <p>Valuations carried out every 5 years for all assets as part of rolling revaluation programme.</p> <p>Procurement and contract criteria ensure valuations are carried out by reputable valuers.</p> <p>Detailed discussions between valuers and ELC Estates team.</p> <p>Detailed working papers retained to support asset reviews and impairments.</p> | <p>Completion of 'review of the work of an expert' in accordance with ISA 500 for the professional valuer.</p> <p>Focused substantive testing of asset valuations and asset useful lives.</p> <p>Focused substantive testing of provisions.</p> |
| <p>5 Rent arrears</p> <p>The Council's risk register (at November 2017) includes a high residual risk in relation to Welfare Reform and the rollout of Universal Credit (UC). It notes that rent arrears for UC claimants are increasing with 82% of ELC tenants claiming UC now in arrears.</p> <p>There is a risk that debtors could be overstated if the provision for doubtful debts is not adequate in light of rising rent arrears. There is an increased risk to the overall delivery of services in line with the Council's strategic objectives.</p> | <p>Impact of UC subject to monthly monitoring by the local team.</p> <p>High level scrutiny group established to monitor the impact of rent arrears and rent collection.</p> <p>Bad debt provision monitored to ensure it remains at reasonable and prudent level.</p> | <p>Monitor rent arrears levels and provision for doubtful debts.</p> |

Wider dimension risks

| | | |
|---|---|---|
| <p>5 Financial sustainability</p> <p>ELC's 2018-19 to 2022-23 Financial Strategy recognises that it faces significant financial challenges resulting from the expected reduction in grant funding and a rapidly expanding population.</p> <p>Current approved spending plans require the delivery of over £9 million of additional efficiencies between 2017-18 and 2019-20.</p> | <p>The Financial Strategy covering the period from 2018-19 to 2022-23 was approved in December 2017. The period covering the Financial Strategy has been extended to cover a 5 year planning horizon in recognition of the future financial challenges and uncertainty around the future financial resources which will be made available to the Council.</p> | <p>Review the Council's change / transformation plans as part of the Best Value Audit Review.</p> <p>Assessing the robustness of the Council's transformation plans and other items supporting longer term plans.</p> |
|---|---|---|

| Audit Risk | Source of assurance | Planned audit work |
|---|--|--|
| <p>The total estimated level of revenue savings required over the next 5 years in addition to the current planned savings has been calculated based on a number of different scenarios and ranges from £12.4 million to £39 million.</p> <p>The Council recognises that the scale of the further savings required over the coming years presents a significant challenge.</p> | <p>The Council budget covering a 3 year revenue horizon and five year capital and Housing Revenue Account, will be considered by Council on 13 February and requires the Council to consider how future spending obligations can be delivered within anticipated resources. The budget which is presented by the Administration will require the delivery of £12.5m of efficiencies over the next 3 financial years.</p> <p>The delivery of these efficiencies will be monitored during the financial year by the Council Management Team and progress reported to Council through the quarterly financial reports.</p> <p>The efficiencies include the delivery of a Transformational Change Programme, and this is monitored through a Transformational Change Programme Board which is chaired by the Council's Chief Executive and includes senior officers from the Council's Executive Team.</p> | |
| <p>6 Financial management</p> <p>The Quarter 2 financial report for 2017/18 identifies two services areas (Adult Wellbeing and Children's Wellbeing) as high risk of not operating within approved budgets. Both service areas had difficulty operating within budget and required additional funding in the last financial year.</p> <p>There is a risk that the Council will not achieve a balanced year end position and also of future budget overspends if a sustainable budget is not developed timeously.</p> | <p>Director of Health & Social Care, respective Heads of Service and the Health & Social Care Management Team have been asked to identify further options to bring these financial commitments back in line with available resources.</p> | <p>Review of financial monitoring reports and the Council's financial position.</p> |
| <p>7 Following the Public Pound</p> <p>In our 2016/17 Annual Audit Report, we reported that no reports were presented to the Audit and Governance Committee during 2016/17 regarding enjoyleisure or the other significant Group</p> | <p>Arrangements in place for enjoyleisure to report to future Audit and Governance Committees. First report was presented to the Committee in November 2017.</p> | <p>Attendance / observation of relevant Committee(s).</p> <p>Review of arrangements put in place by the Council in response to 2016/17 recommendation.</p> |

| Audit Risk | Source of assurance | Planned audit work |
|---|---------------------|--------------------|
| <p>components and we could not find evidence of any routine performance monitoring / reporting to Council committees in this area. Formal reporting and monitoring arrangements should be put in place for significant Group components.</p> <p>There remains a risk that the Council is not complying with the duties set out in the Code of Guidance on Funding External Bodies and Following the Public Pound ensuring they are holding the various group components to account.</p> | | |

Reporting arrangements

4. Audit reporting is the visible output for the annual audit. All annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

5. 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 relevant officer(s) to confirm factual accuracy.

6. We will provide an independent auditor's report to East Lothian Council and the Accounts Commission setting out our opinions on the annual accounts. We will provide the Section 95 Officer and the Accounts Commission with an annual report on the audit containing observations and recommendations on significant matters which have arisen in the course of the audit.

Exhibit 2: 2017/18 Audit outputs

| Audit Output | Target date | Audit Committee (or equivalent) Date |
|------------------------------|-------------------|--------------------------------------|
| Annual Audit Plan | 12 February 2018 | 20 February 2018 |
| Management (Interim) Report | 4 June 2018 | 12 June 2018 |
| Annual Audit Report | 25 September 2018 | 25 September 2018 |
| Independent Auditor's Report | 25 September 2018 | 25 September 2018 |

Audit fee

7. The proposed audit fee for the 2017/18 audit of East Lothian Council including the Dr Bruce Charitable Fund is £237,010 (2016/17: £236,070). In determining the audit fee we have taken account of the risk exposure of East Lothian Council, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited financial statements with a complete working papers package on 29 June 2018.

8. 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.

Responsibilities

Audit Committee and Accountable Officer (or equivalent)

9. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

10. The audit of the financial statements does not relieve management or the Audit and Governance Committee, as those charged with governance, of their responsibilities.

Appointed auditor

11. Our responsibilities as independent auditor are established by the 1973 Act for local government, and the Code of Audit Practice (including supplementary guidance) and guided by the auditing profession's ethical guidance.

12. Auditors in the public sector give an independent opinion on the financial statements and other specified information accompanying the financial statements. We also review and report on the arrangements within the audited body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Financial statements

13. The statutory financial statements audit will be the foundation and source for the majority of the audit work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of East Lothian Council and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how East Lothian Council will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free of material misstatement.

14. We will give an opinion on the financial statements as to:

- whether they give a true and fair view of the financial position of the council and its group as at 31 March 2018 and of their expenditure and income
- whether they have been properly prepared in accordance with IFRS' as adopted by the European Union, as interpreted and adapted by the Code
- whether they have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Authority Accounts (Scotland) Regulations 2014 and the Local Government in Scotland Act 2013.

Materiality

15. We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinion in the independent auditor's report.

16. We calculate materiality at different levels as described below. The calculated materiality values for East Lothian Council are set out in [Exhibit 3](#).



Exhibit 3: Materiality values

| Materiality level | Amount |
|--|----------------|
| Planning materiality – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It has been set at 1% of gross expenditure for the year ended 31 March 2018 based on the latest audited accounts. | £3.8 million |
| Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 50% of planning materiality. | £1.9 million |
| Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 1% of planning materiality. | £0.038 million |

Source: Audit Scotland (prepared from East Lothian Council 2016/17 audited accounts)



17. We also set separate materiality levels for the Council's charitable trust, the Dr Bruce Fund, and this has been set to 1% of gross expenditure (£2).

18. We review and report on other information published with the financial statements including the management commentary, annual governance report and the remuneration report. Any issue identified will be reported to the Audit and Governance Committee.

Timetable

19. To support the efficient use of resources it is critical that a financial statements timetable is agreed with us for the production of the unaudited accounts. An agreed timetable is at [Exhibit 4](#) and takes account of submission requirements and planned Audit and Governance Committee dates:

Exhibit 4: Financial statements timetable

|  Key stage |  Date |
|---|--|
| Consideration of unaudited financial statements by those charged with governance | 12 June 2018 |
| Latest submission date of unaudited annual accounts with complete working papers package | 29 June 2018 |
| Latest date for final clearance meeting with Head of Council Resources | 14 September 2018 |
| Issue of letter of representation and proposed independent auditor's report | 14 September 2018 |
| Agreement of audited unsigned annual accounts | 25 September 2018 |
| Issue of Annual Audit Report including ISA 260 report to those charged with governance | 25 September 2018 |
| Independent auditor's report signed | 26 September 2018 |



Key stage



Date

Latest date for signing of WGA return

30 September 2018

Internal audit

20. 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 assessment of the internal audit function. Internal audit is provided by an East Lothian Council Internal Audit section overseen by a Chief Internal Auditor.

Adequacy of Internal Audit

21. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carried out an early assessment of the internal audit function and concluded that it has sound reporting procedures in place and complies with the main requirements of the Public Sector Internal Audit Standards (PSIAS). Further review of the internal audit working papers will be undertaken for the planned areas of reliance.

Areas of Internal Audit reliance

22. To support our audit opinion on the financial statements we plan to place formal reliance on the following planned internal audit reviews:

- Council Tax Income
- Non Domestic Rates Income – IT access controls

23. In respect of our wider dimension audit responsibilities we also plan to consider other areas of internal audit work including:

- Counter Fraud Arrangements
- ALEOs
- Review of Overtime
- Housing Rent Arrears
- NFI
- Controls assurance statement to inform 2017/18 Governance Statement

Audit dimensions

24. Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#).

Exhibit 5: Audit dimensions



Source: Code of Audit Practice

25. In the local government sector, the appointed auditor's annual conclusions on these four dimensions will help contribute to an overall assessment and assurance on best value.

Financial sustainability

26. As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the body's financial sustainability in the longer term. We define this as medium term (two to five years) and longer term (longer than five years) sustainability. We will carry out work and conclude on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of arrangements in place to address any identified funding gaps.

Financial management

27. Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. We will review, conclude and report on:

- whether East Lothian Council has arrangements in place to ensure systems of internal control are operating effectively
- whether East Lothian Council can demonstrate the effectiveness of budgetary control system in communicating accurate and timely financial performance
- how East Lothian Council has assured itself that its financial capacity and skills mix are appropriate
- whether East Lothian Council has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

Governance and transparency

28. Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and, transparent reporting of financial and performance information. We will review, conclude and report on:

- whether East Lothian Council can demonstrate that the governance arrangements in place are appropriate and operating effectively
- whether there is effective scrutiny, challenge and transparency in decision-making and on finance and performance reports
- the quality and timeliness of financial and performance reporting.

Value for money

29. Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether:

- East Lothian Council can provide evidence that it is demonstrating value for money in the use of its resources
- East Lothian Council can demonstrate that there is a clear link between money spent, output and outcomes delivered
- East Lothian Council can demonstrate that outcomes are improving.

Best Value

30. The Accounts Commission agreed the overall framework for a new approach to auditing Best Value in June 2016. The introduction of the new approach coincides with the new five year audit appointments.

31. A key feature of the new approach is that it integrates Best Value into the wider scope annual audit which will influence audit planning and reporting. Best Value will be assessed comprehensively over the five year audit appointment both through the on-going annual audit work and also through discrete packages of work to look at specific issues. Conclusions and judgements on Best Value will be reported through:

- The Annual Audit Report for each council that will provide a rounded picture of the council overall.
- An Annual Assurance and Risks report that the Controller of Audit will provide to the Accounts Commission that will highlight issues raised across all 32 council annual audit reports.
- A Best Value Assurance Report (BVAR) for each council that will be considered by the Accounts Commission at least once in a five year period.

32. The six councils on which a BVAR will be published during the second year of the new approach (2017/18) are listed in [Exhibit 6](#). Reports will be considered by the Accounts Commission in the period between April 2018 and November 2018.

Exhibit 6: 2017/18 Best Value Assurance Reports

| | |
|-------------------------------|-----------------------------|
| East Lothian Council | Glasgow City Council |
| Dumfries and Galloway Council | West Dunbartonshire Council |
| East Ayrshire Council | Fife Council |

Source: Audit Scotland

33. The work planned in East Lothian Council this year will focus on the Council's arrangements for demonstrating Best Value in the following areas:

- leadership, governance and scrutiny - vision, priorities, member and officer roles and responsibilities
- outcomes and performance - overall assessment of outcomes, performance and public reporting
- improvement - self-evaluation and, change / transformation plans and programmes
- partnership working - Community Planning Partnership including community empowerment

34. The results of this work will be reported in the Best Value Audit Report to the Accounts Commission in October 2018.

Independence and objectivity

35. Auditors appointed by the Accounts Commission or Auditor General must comply with the Code of Audit Practice and relevant supporting guidance. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council 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 Director of Audit Services who serves as Audit Scotland's Ethics Partner.

36. The engagement lead for East Lothian Council is Gillian Woolman, Assistant Director. Auditing and ethical standards require the appointed auditor, Gillian Woolman, 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 East Lothian Council.

Quality control

37. 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.

38. 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 (and relevant supporting guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the

required quality standards, Audit Scotland conducts peer reviews, internal quality reviews and is currently reviewing its arrangements for external quality reviews.

39. 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 welcome feedback at any time and this may be directed to the engagement lead.

Adding Value

40. Through our audit work we aim to add value to East Lothian Council. We do this by ensuring our Annual Audit Report provides a summary of the audit work completed in the year together with clear judgements and conclusions on how well East Lothian Council has discharged its responsibilities and how well it has demonstrated the effectiveness of its arrangements. Where it is appropriate we will recommend actions that support continuous improvement and summarise areas of good practice identified from our audit work.

EAST LoTHIAN COUNCIL

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Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
T: 0131 625 1500 E: