

# Stevenage Borough Council

## Accounts Audit Approach Memorandum

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**June 2012**

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# Our accounts audit approach

This memorandum is intended to provide additional detail regarding our audit approach, as set out in our Audit Plan 2011/12 issued in December 2011, as well as an update on our response to key risks from the results of interim audit work carried out to date.

## Audit approach reminder

We will:

- work closely with the finance team to ensure that we meet audit deadlines and conduct the audit efficiently
- plan our audit on an individual task basis at the start of the audit, and agree timetables with all staff involved; and
- consider the materiality of transactions when planning our audit and when reporting our findings.

The logistical details of our annual accounts audit, as agreed with the Assistant Director of Finance, are detailed in Appendix A to this memorandum.

## Planning

- Updating our understanding of the Council through discussions with management and a review of in year internal financial reporting
- Identifying and resolving specific accounting treatment issues.

## Controls evaluation

- Reviewing the design effectiveness and implementation of internal financial controls including IT, where they impact the financial statements
- Assessing audit risk and developing and implementing an appropriate audit strategy
- Testing the operating effectiveness of selected controls
- Assessing the Council's arrangements for complying with tax legislation and Bribery Act requirements
- Assessing the effectiveness of Internal Audit.

## Substantive procedures

- Reviewing material disclosure issues in the financial statements
- Performing analytical review
- Verifying all material income and expenditure and balance sheet accounts, taking into consideration whether audit evidence is sufficient and appropriate.

## Completion

- Performing overall evaluation of our work on the financial statements to determine whether they give a true and fair view
- Determining an audit opinion
- Reporting to the Audit Committee through our ISA 260 report and Annual Audit Letter.

### Materiality

An item would be considered material to the financial statements if, through its omission or non-disclosure, the financial statements would no longer show a true or fair view.

Materiality is set at the outset of planning to ensure that an appropriate level of audit work is planned. It is then used throughout the audit process in order to assess the impact of any item on the financial statements. Any identified errors or differences greater than 2% of materiality will be recorded on a schedule of potential misstatements.

These are assessed individually and in aggregate, communicated to you and, if you agree with any management decisions to not adjust for such items, signed off by you in your letter of representation to us, confirming your view that they are immaterial to the financial statements.

An item of low value may be separately judged to be material by its nature, for example any item that affects the disclosure of directors' emoluments. An item of higher value may equally be judged not material if it does not distort the truth and fairness of the financial statements.

### Work of internal audit

We work with the internal audit function to ensure our audit approach takes account of the risks identified from reviews they have conducted relevant to the financial statements, subject to our review of the effectiveness of the internal audit function.

Where significant risks to the financial statements are identified from our own work, it may be possible to coordinate with the work of internal audit to avoid unnecessary duplication of effort. Where such work takes place this will be specifically detailed in the reporting of our results.

### Review of IT

You use computer systems and accounting applications to routinely process large numbers of transactions. These may be used either directly or indirectly in preparing financial reporting information, including the annual accounts. Accordingly, our approach requires a review of the internal controls in the Council's information technology (IT) environment.

Based on our assessment of the complexity of the overall IT environment, we have involved specialist Technology Risk Services (TRS) team members in our audit work in order to undertake a review of the overall IT control environment. Where significant systems are outsourced, or new systems or applications introduced in year, additional review work may be undertaken on this risk assessed basis.

### Internal controls

Auditing standards require that we evaluate the design effectiveness of internal controls over the financial reporting process to identify areas of weakness that could lead to material misstatement. Therefore, we will focus our control review on the high risk areas of the financial statements.

In order to assess whether controls have been implemented as intended, we will conduct a combination of inquiry and observation procedures, and, where appropriate, transaction walkthroughs. Where further assurance or audit efficiency may be gained, we will consider directly testing any controls that we may consider to be key in relation to the identified risk.

However, our controls work cannot be relied upon to identify all defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive controls review exercise might identify.

# Update on accounts audit risk assessment

As part of our planning and control evaluation work we have reviewed the key audit risks identified in our Audit Plan 2011/12 and have set out in Table 1 below the outcome of work completed to date and further work planned.

We will report our full findings and conclusions in respect of each risk identified in our Annual Report to Those Charged with Governance (ISA 260) on completion of our final accounts audit.

Our updated review of the key risks facing the Council has not identified any new risk areas.

**Table 1. Key accounting risks and planned assurances**

Issue	Audit areas affected	Work completed to date	Further work planned
<p><b>Financial Performance</b></p>	<p><b>All areas of the financial statements</b></p>	<ul style="list-style-type: none"> <li>We have continued to monitor the Council's financial performance for the year against its agreed budget, including discussion at quarterly meetings with the Director of Resources.</li> </ul>	<ul style="list-style-type: none"> <li>We will continue to monitor the financial position of the Council, including performance against savings plans and reviewing the use of general reserves. This will also be informed by our financial resilience work undertaken as part of our Value for Money programme.</li> </ul>

Table 1. Key accounting risks and planned assurances

Issue	Audit areas affected	Work completed to date	Assurances gained
<p>Accounting for Property, Plant and Equipment</p>	<p>Property, Plant and equipment</p>	<ul style="list-style-type: none"> <li>Accounting for Property, Plant and Equipment was discussed with Council Officers during the interim audit. This included the Code of Practice requirement for councils to identify and disclose heritage assets. The Council have completed an initial assessment and have not identified any heritage assets of significant value.</li> <li>We have discussed the on-going requirement for the Council to document key estimates and judgements relating to the valuation of Property, Plant and Equipment.</li> </ul>	<ul style="list-style-type: none"> <li>The process for the identification of heritage assets has been reviewed and appears to be appropriate. The Council are to provide a detailed schedule to evidence the review that has been completed. During our final audit we will review and confirm our agreement that the disclosures meet the relevant Financial Reporting Standards and guidelines</li> <li>The use of valuation experts will be reviewed to ensure that the valuations have been completed in accordance with IFRS requirements. This will include:                         <ul style="list-style-type: none"> <li>the appropriateness of data and instructions provided to the expert</li> <li>the methods and assumptions applied by the expert.</li> </ul> </li> </ul>
<p>Shared benefits service</p>	<p>All areas of the financial statements</p>	<ul style="list-style-type: none"> <li>The Council has entered into a shared benefits service with East Hertfordshire District Council that went operational in December 2011.</li> <li>We have updated our documentation of the system and controls in place following the shared service arrangement.</li> <li>We have completed walkthrough tests as part of our interim audit work to confirm that controls over the benefit payments are in place as expected.</li> </ul>	<ul style="list-style-type: none"> <li>Our year end audit procedures will include detailed testing on benefit payments.</li> </ul>

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Issue	Audit areas affected	Work completed to date	Assurances gained
Stevenage Homes	All areas of the financial statements	<ul style="list-style-type: none"> <li>The Council have brought the management of their housing stock back in house. We have been engaged in discussions throughout this process.</li> </ul>	<ul style="list-style-type: none"> <li>We will continue to liaise with the Council to review the implications of any developing issues. Our audit work will also focus on this area to ensure that the transition has not had any significant impact on the information produced.</li> </ul>
Accounting under IFRS	All areas of the financial statements	<ul style="list-style-type: none"> <li>New accounting issues were discussed with Council officers during the interim audit. Members of the finance team also attended our 2011/12 Technical Update Seminar.</li> <li>Our Arrangement's Letter (issued in February 2012) sets out detailed requirements for working papers that we will review as part of our final audit procedures.</li> </ul>	<ul style="list-style-type: none"> <li>It is not anticipated that there will be any significant impact on the preparation of the financial statements, but we will continue to monitor and discuss any accounting developments with management.</li> </ul>
IT control environment	All areas of the financial statements	<ul style="list-style-type: none"> <li>Our specialist Technology Risk Services (TRS) team have followed up on our 2010/11 review of the IT control environment in place at the Council.</li> <li>We are finalising our findings with officers at the Council and will report on these within our ISA260 report.</li> </ul>	<ul style="list-style-type: none"> <li>We will continue to monitor the IT control environment to ensure that there are no issues with the production of the financial statements and the supporting working papers.</li> </ul>
Use of estimates and judgments	All areas of the financial statements	<ul style="list-style-type: none"> <li>The importance of disclosing estimates and judgements was discussed with Council officers at the interim audit, particularly with regards to Property, Plant and Equipment. It was noted that there are no major new areas of disclosure in 2011/12 required by the Code of Practice.</li> </ul>	<ul style="list-style-type: none"> <li>All significant estimates and judgements will be reviewed at the final audit, as well as their disclosure to ensure that the requirements of the Code of Practice have been met.</li> </ul>

# Results of interim audit work

## Scope

As part of the interim audit work, and in advance of our final accounts audit fieldwork, we considered:

- the effectiveness of the Internal Audit function;
- internal audit's work on the Council's key financial systems;
- a review of closedown procedures in preparation for the final accounts;
- journal entry controls;
- walkthrough testing and tests of controls to confirm whether controls are implemented as per our understanding in areas where we have identified significant accounting assertion risk; and
- a review of Information Technology controls.

## The internal audit function

We have reviewed the Shared Internal Audit Service's (SIAS) overall arrangements against the 2006 CIPFA Internal Audit Standards. Where the arrangements are deemed to be adequate, we can gain assurance from the overall work undertaken by internal audit and can conclude that the service itself is contributing positively to the internal control environment and overall governance arrangements within the Council.

Overall, we have concluded that SIAS provides an independent and satisfactory service to the Council and that we can take assurance from their work in contributing to an effective internal control environment at the Council.

## Closedown procedures

Our review considered the Council's timetable for closedown and the arrangements for preparing the draft accounts, including guidance provided on working papers required to be made available as part of the closedown process.

The Council has established a suitable timetable and expects to meet the deadline for submission of the accounts. The Council also expects to be able to provide detailed working papers to support the accounts at the start of our final accounts audit fieldwork, which is scheduled to commence on 23 July 2012, as well as providing the draft Annual Governance Statement and explanatory foreword in advance of this date.



### Journal entry controls

We have reviewed the Council's journal entry policies and procedures as part of determining our journal entry testing strategy and have not identified any material weaknesses which are likely to adversely impact on the Council's control environment or financial statements.

To date we have undertaken detailed testing on journal transactions recorded for the first nine months of the financial year, by extracting 'unusual' entries for further review. No issues have been identified that require to be reported.

### Additional assurance work

To support our audit for 2011/12, we are in the process of undertaking brief reviews in the following areas:

VAT - a checklist of the Council's current arrangements will be completed to identify whether they are appropriate to ensure VAT is accounted for correctly and in accordance with current legislation

PAYE - a checklist of the arrangements the Council has in place regarding taxation associated with payroll, including National Insurance and PAYE will be completed in order to provide assurance that figures recorded within the financial statements are true and fair and calculated appropriately and in accordance with current legislation

Fraud - we will consider the overall adequacy of the Council's arrangements to ensure that the risk of fraud and corruption is managed effectively.

# Appendices

## A. Logistics

### Timetables and milestones

The following proposed timetable and deadlines have been set and agreed with management:

Event	Date
Pre year end fieldwork including internal controls review	Mar 2012
Completion of outstanding internal controls reviews and housing benefits testing	June 2012
Statutory accounts emailed to auditor	30 June 2012
Commence accounts audit fieldwork	23 July 2012
Partner visit to review work	tbc
Clearance meeting to discuss our findings	tbc
Draft ISA 260 report to be issued by	24 August 2012
Report to Finance Audit and Risk Committee (ISA 260)	10 Sept 2012

The audit process is underpinned by effective project management to ensure that we co-ordinate and apply our resources efficiently to meet your deadlines. It is therefore essential that we work closely with your team to achieve this timetable. An agreed format and schedule of informal update arrangements will be maintained throughout the course of our audit fieldwork in support of this aim.

### Engagement team

In accordance with our Audit Plan 2011/12 issued January 2012, the main engagement team for the accounts audit will include:

Name	Role	Contact details
Phil Westerman	Engagement partner	T: 0207 728 2548 E: <a href="mailto:philip.r.westerman@uk.gt.com">philip.r.westerman@uk.gt.com</a>
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### Information requirements

The information and working paper requirements that would assist us in an efficient and timely audit of the year-end financial statements have been communicated to the finance team within our Arrangements Letter, issued in February 2012.



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