



The Highland Council Annual Audit Plan 2014/15

Prepared for members of The Highland Council

March 2015



Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

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Summary

Introduction

1. Our audit is focused on the identification and assessment of the risks of material misstatement in The Highland Council's (the council's) financial statements.
2. This report summarises the key challenges and risks facing the council and sets out the audit work that we propose to undertake in 2014/15. Our plan reflects:
 - the risks and priorities facing the council
 - 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.
3. The council has two registered charitable trusts with assets totalling £2.6 million which require to be separately audited as the council is the sole trustee. We will undertake the audit of the council's charitable trusts in parallel with the audit of the council's financial statements.

Summary of planned audit activity

4. Our planned work in 2014/15 includes:
 - an audit of the financial statements and provision of an opinion on whether:
 - they give a true and fair view of the state of affairs of the council and its group as at 31 March 2015 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 2014/15 Code of Practice on Local Authority Accounting in the United Kingdom (the Code)
 - an audit of the financial statements and provision of an opinion for the charitable trusts where the local authority is the sole trustee
 - reporting the findings of the shared risk assessment process in a Local Scrutiny Plan. This will summarise identified scrutiny risks and/or any changes to the Local Area Network's (LAN's) assessment since last year
 - a review and assessment of the council's governance and performance arrangements in a number of key areas including: key financial controls, review of adequacy of internal audit, best value, statutory performance indicators, corporate governance and arrangements for the prevention and detection of fraud and corruption

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- provision of an opinion on a number of grant claims and returns, including whole of government accounts
 - reporting of National Fraud Initiative arrangements and results.

Responsibilities

5. The audit of the financial statements does not relieve management, or the Audit and Scrutiny Committee as the body charged with governance, of their responsibilities.

Responsibility of the appointed auditor

6. 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.
7. 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 Director of Finance

8. It is the responsibility of the Director of Finance 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 council and its group as at 31 March 2015 and its income and expenditure for the year then ended.

Format of the accounts

9. The financial statements should be prepared in accordance with the Code which constitutes proper accounting practice. The council prepares a whole of government accounts consolidation pack annually for the Scottish Government. To enable summarisation common accounting principles and standard formats should be used.

Audit Approach

Our approach

10. Our audit approach is based on an understanding of the council's characteristics, responsibilities, principal activities, risks and governance arrangements. We also consider the key audit risks and challenges in the local government sector generally. This approach includes:
 - understanding the business of the council and its group 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 council 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.
11. 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. Management action being relied on for 2014/15 includes:
 - comprehensive closedown procedures for the financial statements accompanied by a timetable issued to all relevant staff
 - clear responsibilities for the preparation of the 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 2014/15
 - representations from the auditors of the council's subsidiaries within the group boundary.
12. 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 early assessment of the internal audit function. Our review concluded that the council's internal audit section generally operates in accordance with the Public Sector Audit Standards, and noted that an action plan has been prepared to address areas of non-compliance.

13. We plan to place formal reliance on the work of internal audit in the following areas to support our audit opinion on the financial statements:
- payroll
 - general ledger
 - council tax – billing & collection
 - non domestic rates – billing & collection
 - treasury management
 - housing benefits (partial reliance on substantive testing for financial statements and grant certification assurances using HBCOUNT methodology)
 - testing of key controls to support the Head of Audit & Risk Management’s opinion on the council’s system of internal control.
14. In respect of our wider governance and performance audit work we also plan to review the findings and consider other areas of internal audit work including:
- statutory performance indicators
 - health and social care integration
 - annual review of local code of corporate governance.

Materiality

15. International Standard on Auditing 320 provides guidance on the concept of materiality. We consider materiality and its relationship to audit risk when planning the nature, timing and extent of our audit and conducting our audit procedures. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
16. Based on our knowledge and understanding of the council we have set our planning materiality at 1% of gross expenditure. For 2014/15 planning materiality is £8.2 million.
17. We set a lower level, known as performance materiality, when defining our audit procedures. 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.
18. For 2014/15 performance materiality has been set at £4.1 million. We will report, to those charged with governance, all misstatements greater than £100,000 (reporting threshold).

19. We set different levels of materiality for the council, its group and individual charities. The levels of materiality, performance materiality and the reporting threshold are set out in Exhibit 1.

Exhibit 1: Materiality levels

	Planning Materiality £	Performance Materiality £	Reporting Threshold £
Council	8,200,000	4,100,000	100,000
Group	8,300,000	6,600,000	100,000
Highland Council Charitable Trusts	720	540	35
Highland Charities Trust	20	15	1

20. In addition, an inaccuracy which would not normally be regarded as material in terms of monetary value 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.

Reporting arrangements

21. 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; and that elected members consider the unaudited annual accounts at a meeting by 31 August. The council must also publish the unaudited accounts on its website and give public notice of the inspection period. This also applies to any charities for which the local authority is the sole trustee.
22. The 2014 regulations require the council (or a committee whose remit includes audit or governance) 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.
23. The council is required to publish on its website its signed audited annual accounts, and the audit certificate, by 31 October, together with the accounts of its subsidiaries. The annual audit report is required to be published on the website by 31 December.

24. An agreed timetable for the audit of the council's and charitable trusts' financial statements is included at Exhibit 2 which takes account of submission requirements and the dates of planned full Council and Audit & Scrutiny Committee meetings.

25. 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 responsible head of service 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 Chief Executive, Director of Finance, relevant senior manager, the Head of Audit & Risk Management and Audit Scotland's Performance Audit and Best Value Group.

26. We will provide independent auditor's reports to members of The Highland Council, the trustees of the council's charitable trusts and the Accounts Commission that the audits of the financial statements have been completed in accordance with applicable statutory requirements.

27. As part of our streamlined audit approach, the Annual Audit Report will be combined with the ISA 260 'Communication with those charged with governance' report this year, and the combined report will be issued by 30 September, one month earlier than previous years. All annual audit reports produced are published on Audit Scotland's website (www.audit-scotland.gov.uk).

Exhibit 2: Financial statements audit timetable

Key stage	Date
Meetings with officers to clarify expectations of working papers and financial system reports	By 31 March 2015
Review and testing of systems of internal control	By 31 May 2015
Planned council approval of unaudited financial statements	25 June 2015
Submission of unaudited financial statements with working papers package (council & charitable trusts)	30 June 2015
Submission of unaudited WGA return for audit	31 July 2015
Progress meetings with lead officers on emerging issues	Fortnightly
Latest date for final clearance meeting with Director of Finance	4 September 2015
Agreement of unsigned financial statements for Audit & Scrutiny Committee agenda, and issue of combined ISA 260 report to those charged with governance and draft Annual Audit Report.	14 September 2015
Audit & Scrutiny Committee	29 September 2015
Independent auditors report signed	30 September 2015
Latest date for signing of WGA return	2 October 2015

28. Planned outputs for 2014/15 are summarised at Appendix I.

Quality control

29. 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. 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).

30. 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 Boyle.

Independence and objectivity

31. 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.

32. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We will advise the Director of Finance, as section 95 officer, of any relationships that may impact on the audit of The Highland Council.

Audit issues and risks

Audit issues and risks

33. Based on our discussions with staff, attendance at committee meetings and a review of supporting information, we have identified the following main financial statements risk areas for the council.

Audit risk of material misstatement in financial statements

34. **Management and supervision of the accounts preparation process:** as noted at paragraph 8, the Director of Finance, as section 95 officer, is responsible for preparing financial statements in accordance with relevant legislation and the Code. Over the last three years, a number of significant adjustments were made to the council's unaudited accounts following our audit. Appropriate management and supervision is required at all stages of the accounts preparation process to ensure that the financial statements submitted for audit comply with the requirements of the Code.

35. There have been changes to the team leading on the preparation of the 2014/15 financial statements. Changes in responsibilities increase the risk that the financial statements' disclosures and supporting working papers will not be prepared to the required quality and by the agreed timescales. The Director of Finance has advised us that an additional level of review involving Finance Managers will be undertaken this year. As part of our audit we will review the council's process for managing and supervising the accounts preparation process and work closely with the finance team to meet the timetable for delivery of the audit as set out in Exhibit 2.

36. **Capital accounting:** in the last three financial years we raised concerns about the council's capital accounting arrangements. Considerable additional work required to be done by finance staff and ourselves before we were able to certify the 2011/12 and 2012/13 accounts. Last year we worked closely with the capital accountant and overall the audit process was much smoother. However, we again identified a lack of audit trail of how key figures in the accounts agreed to the council's asset registers, and a lack of internal consistency in disclosures within the financial statements. We are currently working with officers to address a number of areas carried forward for further discussion in 2014/15 including accounting for non-enhancing capital expenditure, investment and heritage properties, and the operation of the capital fund.

37. Housing rents: last year we identified that the unaudited accounts included an erroneous debtor of £1.372 million. We also reported that the rent account reconciliations provided to audit contained small differences between the ledger position and that recorded in the Housing Information System for which satisfactory explanations could not be provided. In response, the Director of Finance requested that internal audit investigate the rent account reconciliation process to identify why this erroneous debtor (and income) had been included in the council's accounts, and to confirm that differences identified as part of the reconciliation process are promptly investigated and resolved. This work has yet to be concluded but we understand from discussions with internal audit that the Housing Service has made little progress with improving its reconciliation process or explaining the erroneous debtor. This will remain an area of focus for us as part of our 2014/15 audit.

38. Intercompany accounts: our 2013/14 audit identified the need to improve the operation and management of the intercompany accounts used to manage transactions between the council and the pension fund. Officers have continued to review their processes for managing and monitoring these accounts during 2014/15. This will remain an area of focus for us as part of our audit of the 2014/15 financial statements.

39. Local Authority Accounts (Scotland) Regulations 2014: the 2014 regulations introduced a number of key changes with regard to the processes for approval and publication of both the unaudited and audited financial statements. In addition, they require a management commentary to be included in the financial statements for the first time. This requires greater disclosures than have been included to date as part of the explanatory foreword, for example, more information on principal risks and uncertainties, main trends and factors affecting future development and performance, and social, community and human rights issues. We will review the management commentary for compliance with the 2014 regulations as part of our 2014/15 audit.

40. Asset decommissioning: in September 2014, LASAAC issued guidance on 'Asset Decommissioning Obligations' setting out how authorities should account for these obligations, particularly where a retrospective adjustment is required for previously unrecognised liabilities. The council has previously included the costs of decommissioning two landfill sites within its financial statements. As part of our 2014/15 audit, we will confirm that the accounting for these costs complies with the LASAAC guidance and review progress made by the council in estimating the costs of future reinstatement work required to return leased properties to their original condition at the end of the lease.

41. Group accounts and whole of government accounts (WGA) return: this year's Code includes a revised definition of control which requires the council to review its group boundary prior to preparation of the group accounts. Procedures for completing the WGA consolidation pack and management review checklist should also be reviewed to ensure that the pack submitted for audit is in line with the council's financial statements. We will review the revised group boundary and WGA consolidation pack as part of our 2014/15 audit.

42. Income recognition: auditing standards (ISA 240: *the auditor's responsibility to consider fraud in an audit of financial statements*) requires auditors to presume a risk of fraud where income streams are significant. While the council receives a significant amount of funding from the Scottish Government, there are also a range of other sources including council tax, housing rents and charges for services. The extent/complexity of income means there is an inherent risk that income could be materially misstated. The ISA requires auditors to evaluate which types of revenue transactions give rise to such risks. We will, therefore, design and perform audit procedures to address these matters.

43. Management override of controls: 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. We will test journal entries and review accounting estimates for bias as part of our audit of the accounts.

Audit risk from wider responsibilities under Audit Scotland's Code of Audit Practice

44. Financial management and sustainability: in December 2014 the council agreed a package of savings totalling £42.8 million to be phased over four years, with an estimated reduction of 313 full time equivalent (FTE) staff posts over this period. This allowed a balanced revenue budget to be set for 2015/16. A further £13.3 million of savings remains to be identified over the three years to 2018/19. We will continue to monitor the council's progress in delivering its budget savings as part of our 2014/15 audit.

45. Governance of charitable trusts: the council's two charitable trusts are governed by trustees. No trustee meetings were held during 2013/14, and in their absence it is not clear how trustees discharge their duty of proper stewardship of the trusts' funds. The council has agreed to review the governance arrangements for the charitable trusts. We will review the revised arrangements as part of our 2014/15 audit.

46. Heath and social care integration: in April 2012, the council and NHS Highland entered into a Partnership Agreement to provide integrated health and social care services across the Highlands. The Partnership Agreement is currently being updated to reflect the requirements of the Public Bodies (Joint Working) (Scotland) Act 2014. The first two years of the partnership have been financially challenging for both partners as demand for adult care services continues to increase. We will continue to monitor the partnership's arrangements for governance, performance management and funding as part of our 2014/15 audit.

47. Transport infrastructure assets: the 2016/17 Code requires transport infrastructure assets to be measured at depreciated replacement cost with effect from 1 April 2016. This change in accounting policy will require a revised opening balance sheet as at 1 April 2015 and comparative information in respect of 2015/16 to be disclosed within the 2016/17 financial statements. We will review the council's preparedness for this major change in valuation, including the availability of complete and accurate management information on transport infrastructure assets, as part of our 2014/15 audit.

Summary assurance plan

48. In most cases, actions to manage these risks are either planned or already underway within the council. Details of the sources of assurance that we have received for each of these risks and any audit work we plan to undertake is set out in Appendix II. In the period prior to the submission of the unaudited financial statements, we will liaise with senior officers on any new or emerging issues.

National performance audit studies - impact and follow up

49. 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 and to maximise the impact of national performance audits we will carry out work to collect relevant financial and performance information to inform Audit Scotland's national reports.

Fees and resources

Audit fee

50. Over the past four years Audit Scotland has reduced audit fees nationally by 23.5% in real terms, exceeding our 20% target. Due to further refinement of our audit approach we have been able to restrict the increase in audit fees for 2014/15 to 1% which, in real terms, represents a 0.6% reduction at 2014 price levels.
51. In determining the audit fee we have taken account of the council's risk exposure, the 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 a comprehensive working papers package by 30 June 2015.
52. The agreed audit fee for the 2014/15 audit of The Highland Council is £448,885 (2013/14: £444,250). This includes £2,000 (2013/14: £1,000) for the audit of the council's two charitable trusts. Our fee covers:
- the costs of planning, delivering and reporting the annual audit including auditor's attendance at committees
 - your organisation's allocation of the cost of national performance audits and statutory reports by the Accounts Commission

- 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.

53. 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

54. Stephen Boyle, Assistant Director, Audit Services is your appointed auditor. The local audit team will be led by Maggie Bruce 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 3. The core team will call on other specialist and support staff as necessary.

Exhibit 3: Audit team

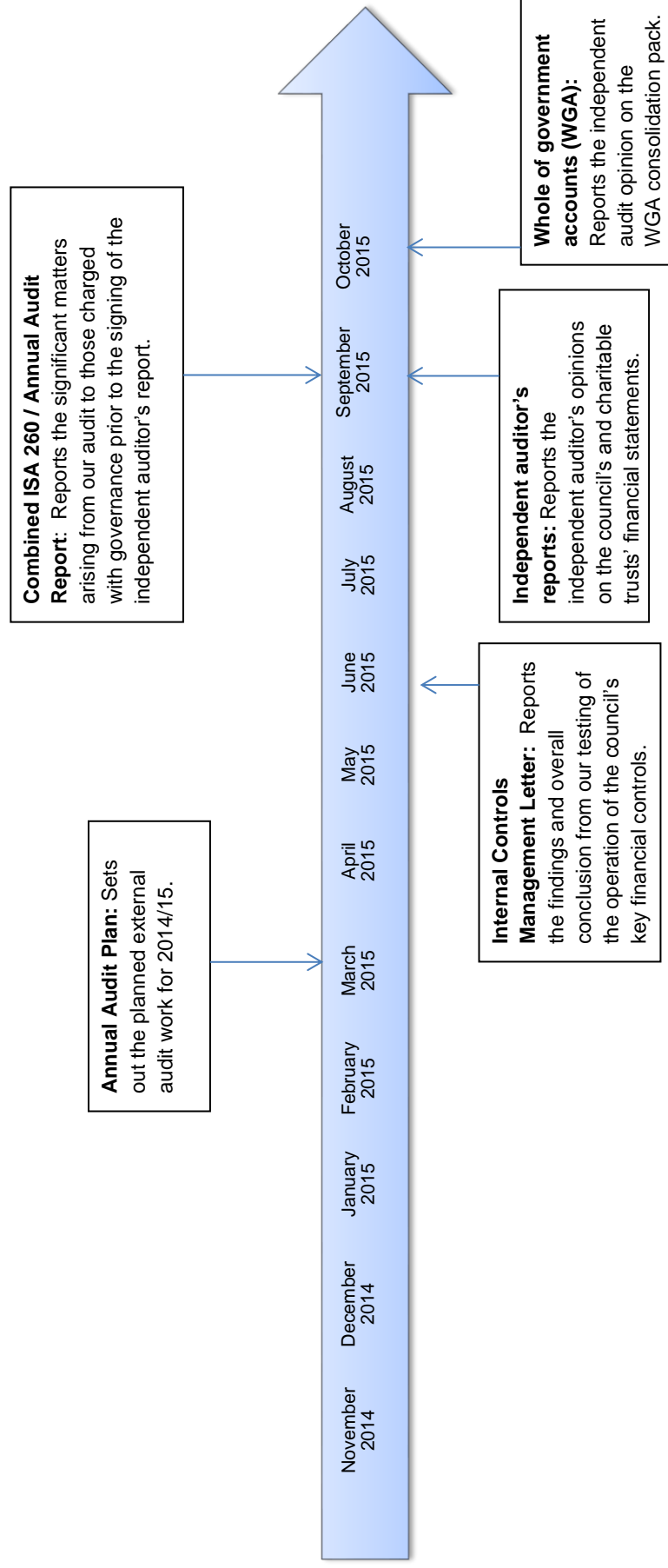
Name	Experience
<p>Stephen Boyle, BAcc CPFA, Assistant Director</p>	<p>Stephen has 18 years experience of public sector finance. He trained as an accountant with a Big 4 firm, before joining Audit Scotland in 2002. He later worked as Head of Finance and Corporate Services for Cube Housing Association, before spending three years with Glasgow Housing Association as Assistant Director of Finance. He re-joined Audit Scotland in June 2013.</p>
<p>Maggie Bruce, MA (Hons) CA, Senior Audit Manager</p>	<p>Maggie has over 20 years experience of public sector audit with Audit Scotland covering the local government, health and further education sectors. Prior to joining Audit Scotland, Maggie trained as an auditor in the private sector.</p>
<p>Jim Convery MA (Hons) CA CPFA, Senior Auditor</p>	<p>Jim has over 25 years experience of public sector audit with Audit Scotland covering the local government, health and further education sectors. Prior to joining Audit Scotland, Jim worked in internal audit in local government and for a private accountancy practice.</p>

Name	Experience
<p>Alison Turner FCCA, Senior Auditor</p>	<p>Alison has over 7 years experience in public sector audit, covering the central government and health sectors. Prior to joining Audit Scotland Alison worked in finance at the police and for a private accountancy practice for 3 years.</p>
<p>Joni McBride BSc (Hons) CPFA, Senior Auditor</p>	<p>Joni joined Audit Scotland in 2008 as part of our graduate training programme and qualified in September 2011. Joni has been involved in a range of audits covering local government, central government and health.</p>
<p>Edward Stansfield BSc (Hons), FCA, CISA, Senior ICT Auditor</p>	<p>Edward has over 10 years experience of public sector audit with Audit Scotland, covering the local government, health and central government sectors. Edward is a Certified Information Systems Auditor specialising in the audit of information technology controls. Prior to joining Audit Scotland he worked for 7 years in industry and for 4 years with a private accountancy practice.</p>

Name	Experience
<p>Nicholas McShane BAcc (Hons), Professional Trainee</p>	<p>Nicholas joined Audit Scotland in 2012 as a professional trainee and is currently studying for the ICAS accountancy qualification. Prior to joining Audit Scotland, Nicholas was a student at Glasgow University.</p>
<p>Lee McDowall, BAacc (Hons), Professional Trainee</p>	<p>Lee joined Audit Scotland in October 2013 as a professional trainee and started studying towards obtaining his ICAS accountancy qualification in the Summer of 2014. Prior to joining Audit Scotland Lee was an Accounting student at the University of Strathclyde.</p>

Appendix I: Planned audit outputs

The diagram below shows the key outputs planned for The Highland Council in 2014/15.



Appendix II: Significant audit risks

We undertake a risk-based audit whereby we focus on those areas where we have identified a risk of material misstatement in the accounts. This section shows how our audit approach focuses on the risks we have identified through our planning procedures. ISA 315 *Identifying and assessing the risks of material misstatement through understanding the entity and its environment* defines a significant risk as “an identified and assessed risk of material misstatement that, in the auditor’s judgement, requires special audit consideration.”

In this section we identify a range of risks facing the council, the related source of assurance received and the audit work we propose to undertake to secure additional assurance. The management of risk is the responsibility of the council and its officers, with the auditor’s role being to review the arrangements put in place by management. Planned audit work, therefore, will not necessarily address all residual risks.

Audit Risk	Source of assurance	Assurance procedure
<p>Audit risk of material misstatement in financial statements</p> <p>Management & supervision of the accounts process: a number of significant audit adjustments were made to the council’s unaudited accounts in previous years. Appropriate management and supervision is required at all stages of the preparation process to ensure that the unaudited accounts comply with the Code. There have been changes to the team preparing the 2014/15 accounts which increases the risk that the accounts and working papers will not be prepared to the required quality and by the agreed timescales.</p>	<ul style="list-style-type: none"> an additional level of review involving Finance Managers will be introduced for 2014/15 a detailed timetable will be prepared and followed. 	<ul style="list-style-type: none"> early financial statements planning meeting review council’s process for managing and supervising the accounts preparation process early discussion of emerging issues.

Audit Risk

Capital accounting: in the last three financial years we raised concerns about the council's capital accounting arrangements. Considerable additional work required to be done by finance staff and ourselves before we were able to certify the 2011/12 and 2012/13 accounts. Last year we worked closely with the capital accountant and overall the audit process was much smoother. However, we again identified a lack of audit trail of how key figures in the accounts agreed to the council's asset registers, and a lack of internal consistency in disclosures within the financial statements. A number of areas have also been carried forward for further discussion with officers in 2014/15 including accounting for non-enhancing capital expenditure, investment and heritage properties, and the operation of the capital fund.

Source of assurance

- capital accounting procedures will be reviewed and amended to reflect the previous year's audit findings.

Assurance procedure

- early financial statements planning meeting
- increased audit testing in this area
- early discussion of emerging issues.

Audit Risk

Housing rents: last year we identified that the unaudited accounts included an erroneous debtor of £1.372 million. We also reported that the rent account reconciliations provided to audit contained small differences between the ledger position and that recorded in the Housing Information System for which satisfactory explanations could not be provided. In response, the Director of Finance requested that internal audit investigate the rent account reconciliation process to identify why this erroneous debtor (and income) had been included in the council's accounts, and to confirm that differences identified as part of the reconciliation process are promptly investigated and resolved. This work has yet to be concluded but we understand from discussions with internal audit that the Housing Service has made little progress with improving its reconciliation process or explaining the erroneous debtor.

Source of assurance

- actions arising from the internal audit report will be implemented
- if issues remain from output from the Housing Information System for accounting purposes at the year end, the housing revenue account will be prepared using only validated debtor balances.

Assurance procedure

- early financial statements planning meeting
- increased audit testing in this area
- early discussion of emerging issues.

Audit Risk	Source of assurance	Assurance procedure
<p>Intercompany accounts: our 2013/14 audit identified the need to improve the operation and management of the intercompany accounts used to manage transactions between the council and the pension fund. Officers have continued to review their processes for managing and monitoring these accounts during 2014/15.</p>	<ul style="list-style-type: none"> the intercompany accounts have been reviewed up to December 2014 with a view to identifying and resolving issues prior to the year end. Plans are in place to share this work with external audit so that any emerging issues can be identified and resolved prior to the preparation of the financial statements. 	<ul style="list-style-type: none"> early financial statements planning meeting increased audit testing in this area early discussion of emerging issues.
<p>Local Authority Accounts (Scotland) Regulations 2014: the 2014 regulations introduced a number of key changes with regard to the processes for approval and publication of both the unaudited and audited financial statements. In addition, they require a management commentary to be included in the financial statements for the first time. This requires greater disclosures than have been included to date as part of the explanatory foreword.</p>	<ul style="list-style-type: none"> changes to regulations and codes are considered and where necessary incorporated as part of the accounts closedown process. 	<ul style="list-style-type: none"> early financial statements planning meeting review of the management commentary for compliance with the 2014 regulations early discussion of emerging issues.

Audit Risk

Asset decommissioning: in September 2014, LASAAC issued guidance on 'Asset Decommissioning Obligations' setting out how authorities should account for these obligations, particularly where a retrospective adjustment is required for previously unrecognised liabilities. The council has previously included the costs of decommissioning two landfill sites within its financial statements. The council also leases a number of buildings which will require to be returned to their original leased condition at the end of the lease. The council currently does not recognise the costs associated with this future reinstatement work within its financial statements but has agreed to investigate, as part of its asset management strategy, whether a reliable estimate can be established in order to make provision for these costs within the financial statements.

Source of assurance

- a review of this asset category will be undertaken by finance staff and the council's valuer.

Assurance procedure

- early financial statements planning meeting
- review of accounting treatment against the requirements set out in the LASAAC guidance
- review progress made in estimating the costs of future reinstatement work required to return leased properties to their original condition at the end of the lease
- early discussion of emerging issues.

Audit Risk	Source of assurance	Assurance procedure
<p>Group accounts and whole of government accounts (WGA) return: the 2014/15 Code includes a revised definition of control which requires the council to review its group boundary prior to preparation of the group accounts. Procedures for completing the WGA consolidation pack and management review checklist should also be reviewed to ensure that the pack submitted for audit is in line with the council's financial statements.</p>	<ul style="list-style-type: none"> the group boundaries will be reviewed during the accounts closure process WGA consolidation pack and management review checklist will be reviewed at year end to ensure in line with the group accounts workings prior to submission to audit. 	<ul style="list-style-type: none"> early financial statements planning meeting review of council's group boundary review of management and supervision of procedures for completing the WGA consolidation pack and management review checklist early discussion of emerging issues.
<p>Income recognition: ISA 240 requires auditors to presume a risk of fraud where income streams are significant. While the council receives a significant amount of funding from the Scottish Government, there are also a range of other sources including council tax, housing rents and charges for services. The extent/complexity of income means there is an inherent risk that income could be materially misstated. The ISA requires auditors to evaluate which types of revenue transactions give rise to such risks.</p>	<ul style="list-style-type: none"> the council operates robust internal controls around the various income streams. 	<ul style="list-style-type: none"> review of the systems of internal control for income recognition perform analytical procedures on significant income streams detailed substantive testing of income transactions.

Audit Risk	Source of assurance	Assurance procedure
<p>Management override of controls: 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"> the council has a strong internal control environment which is regularly tested by internal audit. 	<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.
<p>Audit risk from wider responsibilities under Audit Scotland's Code of Audit Practice</p>		
<p>Financial management and sustainability: in December 2014 the council agreed a package of savings totalling £42.8 million to be phased over four years, with an estimated reduction of 313 full time equivalent (FTE) staff posts over this period. This allowed a balanced revenue budget to be set for 2015/16. A further £13.3 million of cuts remains to be identified over the three years to 2018/19.</p>	<ul style="list-style-type: none"> the council operates robust budget setting and budget monitoring processes corporate savings targets which are not directly removed from service budgets will be the subject of regular reports to the Transformational Savings Board. 	<ul style="list-style-type: none"> monitor financial position comment in Annual Audit Report as appropriate.

Audit Risk	Source of assurance	Assurance procedure
<p>Governance of charitable trusts: the council's two charitable trusts are governed by trustees. No trustee meetings were held during 2013/14, and in their absence it is not clear how trustees discharge their duty of proper stewardship of the trusts' funds.</p>	<ul style="list-style-type: none"> • both charitable trusts are umbrella organisations containing individual trusts. The governance arrangements for the individual trusts have not changed and the accounts for the umbrella organisations are presented to all elected members in their role as trustees • further consideration will be given to any additional stewardship measures required. 	<ul style="list-style-type: none"> • review revised governance arrangements • comment in Annual Audit Report as appropriate.
<p>Health and social care integration: in April 2012, the council and NHS Highland entered into a Partnership Agreement to provide integrated health and social care services across the Highlands. The Partnership Agreement is currently being updated to reflect the requirements of the Public Bodies (Joint Working) (Scotland) Act 2014. The first two years of the partnership have been financially challenging for both partners as demand for adult care services continues to increase.</p>	<ul style="list-style-type: none"> • resource and commissioning groups have been established separately for both Adult and Children's Services to assist with the financial control arrangements. 	<ul style="list-style-type: none"> • review budget monitoring reports and financial outturn • review internal audit's work on governance and performance management within the Lead Agency model • contribute to the Care Inspectorate's inspection of Adult Services and review findings set out in the Inspection Report • comment in Annual Audit Report as appropriate.

Audit Risk

Transport infrastructure assets: the 2016/17 Code requires transport infrastructure assets to be measured at depreciated replacement cost with effect from 1 April 2016. This change in accounting policy will require a revised opening balance sheet as at 1 April 2015 and comparative information in respect of 2015/16 to be disclosed within the 2016/17 financial statements.

Source of assurance

- the depreciated replacement costs for transport infrastructure have been calculated for several years now and reported within the Whole of Government Accounts return. It is acknowledged that some of the elements of these costs are based on estimates as there have not been sufficient resources available to date to identify the actual inventory and/or condition of all transport infrastructure assets. The most significant and valuable elements (e.g. carriageways, bridges etc.) are based on data that is as accurate as can be afforded to date.

Assurance procedure

- review the council's preparedness for this major change in accounting policy
- comment in Annual Audit Report as appropriate.