



Highlands and Western Isles Valuation Joint Board

**External Audit Annual Report to the Board and the Controller of Audit for the
financial year ended 31 March 2018**

Board meeting 13 September 2018 – Draft

Joanne Brown
Engagement Leader

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Senior Manager



Our audit at a glance



We have fulfilled our responsibilities per International Standards on Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice throughout our work and this final report to the Board and the Controller of Audit concludes our work.



Materiality was set at 1.6% of gross expenditure within our plan, and was updated to reflect the draft financial statements at £49,000. We identified one adjustment to the draft financial statements in relation to defined benefit pension scheme assets and we are satisfied these have been corrected in the financial statements (appendix 2).



Significant audit risks were: management override of controls; the risk of fraud in revenue and expenditure recognition as set out in International Auditing Standards (ISAs UK) practice note 10; and the recognition of defined benefit pension scheme transactions. Our risk assessment remained unchanged and we did not identify any adjustments in these areas in our work.

An audit underpinned by quality



We have built on our understanding and relationship with the Highlands and Western Isles Valuation Joint Board (the VJB) officers during the year supporting our audit process.



Our work was undertaken in accordance with our agreed timetable. The draft financial statements produced by officers were of a good standard with complete information and good supporting working papers. We thank officers for their support and assistance during our work.



A wider scope audit for the VJB as set out in our plan, was considered not appropriate. However we have considered your financial planning and governance arrangements as part of our audit. We have raised one recommendation, following up on a prior year observation, around the need to develop medium term financial plans.

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Adding value through our external audit work

First and foremost our objective is to ensure we deliver a quality external audit which fully complies with International Standards of Auditing (ISAs) UK and the Audit Scotland Code of Practice (2016). By ensuring our audit is efficient and effective, gives you assurance over our opinion.

Through this Annual Report we seek to provide insight and commentary over certain aspects of the VJB's arrangements, sharing relevant practices with the Board and Officers.

We have continued to build on our working relationship with officers and our understanding of as an organisation. During the year we have worked with officers to develop our audit approach through greater understanding of your financial transactions.

Introduction

This report is a summary of our findings from our external audit work for the financial year ended 31 March 2018.

Our work has been undertaken in accordance with International Standards of Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice 2016.

In accordance with our reporting responsibilities the report is jointly addressed to the Auditor General for Scotland.

Once finalised this report will be made publically available on the Audit Scotland website (www.audit-scotland.gov.uk)

We would like to thank the VJB's officers and the finance team for an effective year-end audit process and all their support and assistance in the audit process.

Structure of this report

As set out in our Audit Plan (February 2018) we consider in accordance with the Audit Scotland Code of Practice that the VJB is a smaller body. Therefore full wider scope is not appropriate. Our report concludes on our financial statements audit and certain aspects of the VJB's arrangements as follows:

Financial statements – Section 2 and Appendix 1

Financial and governance arrangements – Section 2



Our Opinion

For the financial year ended 31 March 2018 we plan to issue an **unmodified audit opinion**

- True and fair view of the financial statements
- Other information in the annual report
- Other prescribed matters (which include the audited information in the remuneration report)



Status of the audit as at 5 September 2018

Our audit is substantially complete with the exception of the following:

- Letter of representation
- Subsequent events procedures
- Final Engagement Leader review

The audit process

A complete set of financial statements were made available to the public on 28 June 2018, meeting the statutory deadline of the end of June.

The draft financial statements were supported by good working papers and the audit was efficient.

We identified no changes to the financial statement balances and have no unadjusted differences to report. We identified minor disclosure enhancements and these have been reflected in the financial statements.



The financial statements audit



Our audit work was completed in accordance with International Standards in Auditing (UK) (ISAs) and the Audit Scotland Code of Audit Practice (May 2016). Based on our audit procedures performed we expect to issue an unqualified audit opinion on the financial statements including:

- give a true and fair view in accordance with applicable law and the 2017/18 CIPFA Code of Practice on Local Authority Accounting ('the 2017/18 Code');
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2017/18 Code, and with the requirements of applicable law;
- the information given in the Management Commentary is consistent with the financial statements and that report has been prepared in accordance with statutory guidance;
- the information given in the Annual Governance Statement is consistent with the financial statements and that report has been prepared in accordance with applicable guidance; and
- audited parts of the remuneration have been prepared in accordance with the guidance.

Audit approach and materiality

Our audit approach was set out in our annual audit plan presented to the Board in February 2018. As set out in our plan, our materiality calculations were based on the audited 2016/17 financial statements. We subsequently updated our materiality calculation to be based on the draft 2017/18 financial statements. Overall materiality has been set at £49,000 (1.6% of gross expenditure) and performance materiality is set at £36,750. (75% of materiality). We report to officers any audit difference identified over £2,000 (trivial as 5% of materiality).

We did not identify any additional significant audit risks from those identified in our audit plan.

Internal control environment

During the year we sought to understand the VJB's overall control environment (design) as related to the financial statements. Our understanding has built on our understanding of key financial controls processes in place at the Highland Council. In particular we have:

- Considered procedures and controls around related parties, journal entries and other key entity level controls.
- Performed walkthrough procedures on key financial controls in particular journals, ledger controls, income and expenditure transactions.

Our work over controls is limited to our ISA requirements in understanding an entities control environment. Our audit is not controls based and we do not seek reliance over controls. Our audit is fully substantive based in nature.

We identified no material weaknesses or areas of concern from this work which would have caused us to alter the planned approach, set out in our plan.

Internal Audit

As set out in our external audit plan we have not placed formal reliance on the work of internal audit. We reviewed the internal audit plan and individual reports issued to date, to consider if any impact on our audit approach, with none being noted.

The findings of internal audit do not disagree with our knowledge and understanding of the VJB as an organisation.

Identified audit risks and our conclusions

	Identified audit risk at planning	Work completed	Our conclusion
Risk of fraud in revenue and expenditure	<p>Under ISA 240 (UK) there is a presumed risk that revenue may be misstated due to the improper recognition of revenue. The Financial Reporting Council's Practice note 10 (revised), states that for public sector entities, auditors should also consider the risk that material misstatements occur by the manipulation of expenditure recognition.</p> <p>Given the VJB's income and funding comes primarily through grant funding and requisition funding from constituent authorities, we have rebutted the presumed risk of improper recognition of revenue. However, we consider the risk of manipulation of expenditure incurred by the VJB focused on transactions around the year end.</p>	<ul style="list-style-type: none"> • Developed our understanding of the VJB's material revenue and expenditure streams including walkthrough of key transactions. • Performed targeted review and testing of key revenue and expenditure streams during the year • Performing revenue and expenditure cut off procedures and substantive testing over pre and post year end balances • Testing the existence and recoverability of balances at the year end • Performing procedures to identify potential unrecorded liabilities, including post year end transaction testing 	<p>From our audit procedures performed we are satisfied that revenue and expenditure is free from material misstatement.</p> <p>We are satisfied that transactions have been recognised in the appropriate financial year.</p>
Defined benefit pension scheme transactions	<p>The VJB participates in the Highland Council Local Government Pension Scheme, a defined benefit career average revalued earnings (CARE) scheme. The present value of the pension scheme liabilities are subject to annual actuarial valuation. Given the material nature of the scheme assets and liabilities as well as the level of judgement in the assumptions used in the valuation of liabilities, there is an increased risk of material misstatement.</p>	<ul style="list-style-type: none"> • Obtained the actuarial valuation of the scheme and reviewed the reasonableness of the assumptions applied in the scheme valuation • Performed substantive testing on the underlying data as appropriate • Reviewed the recognition of the defined benefit pension scheme liability in the financial statements 	<p>During the course of our audit we identified that the actuarial valuation understated the value of scheme assets at the balance sheet date. Officers obtained a revised actuarial valuation and amended the financial statements accordingly (appendix 2).</p> <p>We are satisfied, that the defined benefit pension scheme liabilities are free from material misstatement.</p>
Management override of controls	<p>As set out in ISA 240 there is a presumed risk that management override of controls is present in all entities</p>	<ul style="list-style-type: none"> • Developed our understanding of the entity level controls in place at the VJB that reduce the risk of management override • Performed review of journal transactions for unusual transactions or balances. • Evaluated key areas of judgement within the financial statements and the basis for these judgements / application of accounting policies • Reviewed unusual and/or significant transactions 	<p>We did not identify any significant areas of bias in key judgements by officers. We have not identified any unusual or significant transactions during the course of the year that would indicate management manipulation.</p>

Narrative elements of your annual accounts

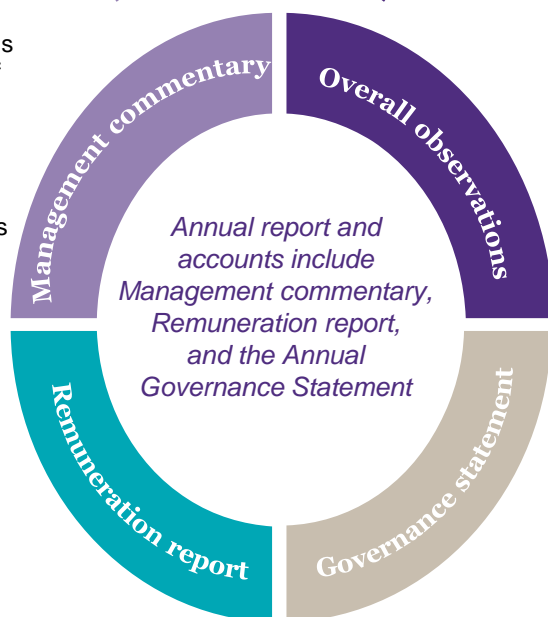
In accordance with our responsibilities we have reviewed your narrative aspects of the Annual Report and Accounts. We have considered the consistency of this narrative with our understanding and the financial statements and have set out our observations below. We have also audited the required information in the remuneration report (marked audited) and have no matters we wish to bring to your attention.

Management commentary

- The Management commentary is in line with our understanding of VJB and in particular the vision and strategic priorities of VJB
- The Management commentary statement is clear and concise
- Financial Outlook and Key Risks are well articulated and there is discussions around service changes and future developments

Remuneration Report

- The remuneration report has been prepared in accordance with Local Authority Accounts (Scotland) Regulations 2014.
- The Senior Post Holders and Senior Councillors note to the accounts.



Overall observations

- VJB continue to look at how the “front end” of the Annual Report and Accounts tells the story of VJB as an organisation including strategic priorities, risks and challenges and opportunities.
- We have considered the management commentary as well as audited the financial information included in the remuneration report and governance statement. We have no matters we wish to bring to your attention.

Governance Statement

- Statement defines the governance framework in place at the VJB and effectiveness of governance arrangements
- Highlights that previous governance issues with respect to risk management processes have been resolved.

Going concern

The VJB is funded through requisitions from constituent authorities to meet annual operating costs. The VJB’s share of defined benefit pension scheme liabilities of £4.9 million exceed the VJB’s assets held. Consequently, the VJB has net liabilities as at 31 March 2018.

Officers are satisfied that the VJB will continue to receive funding from constitution authorities to meet annual operating obligations, including pension charges, in delivering statutory services. As a result they are satisfied that the entity continues to represent a going concern. During 2017/18, the VJB held sufficient reserves to enable underspends against budget of £208,000 to be returned to constituent authorities, We have obtained confirmation of VJB funding for 2018/19 and concur with officer’s going concern assessment.

Fraud and irregularity

In relation to the audit risk of fraud in respect of expenditure we tested the VJB’s cut off arrangements in particular (timing) and identified no issues in accruals or prepayments which would indicate potential fraud. There are no post balance sheet events or legal uncertainties at year-end. There were no frauds identified by officers during the year and no indication of fraud through our audit work.

Key aspects of your financial statements

As set out in our audit plan we consider particular aspects of your financial statements in relation to management judgements including estimates and where management may have particular options or choices in what accounting standards or disclosure requirements to apply. We have summarised where these apply, and our conclusions below.

The VJB's accounting policies are in accordance with the CIPFA Code of Practice on Local Authority Accounting and we consider these to be appropriate to the organisation and consistent with those adopted in prior years.

The VJB's financial statements are not complex with limited areas of judgement or estimation. They provide transparent reporting of income and expenditure throughout the year.

Accounting estimates and judgements

The VJB's significant accounting estimates and judgement impacting on the annual accounts are the following:

- **Defined benefit pension schemes**– the VJB participates in the Highland Council Pension Fund. The VJB recognises its share of the cost of retirement benefits as well as the entity's share of the scheme assets and liabilities. This is estimated through actuarial valuation. As noted above, we identified an audit adjustment to the carrying value of scheme assets as at 31 March 2018. This was due to the actuarial valuation of scheme assets being based on forecast valuation. Due to asset performance exceeding expectation, the actual value of assets was materially higher than outturn position. Management has obtained a revised actuarial valuation and this has been reflected in the final accounts.



Financial and governance arrangements - commentary

Key observations



VJB's financial position and forecast

The VJB reported a breakeven position for the year ended 31 March 2018. The position reflected an underspend against budget of £208,000, primarily through lower than forecast staffing costs. In accordance with CIPFA guidance "Reserves and Balances in a Local Authority" the VJB has a policy of holding reserves at 3% of total annual budget. Consequently, the underspend was returned to constituent authorities through a £208,000 reduction in requisitions.

In setting the budget for 2018/19, the VJB agreed a decrease in the requisitions for the constituent authorities. The VJB will require to manage this funding reduction through delivering operational efficiencies. We have considered the VJBs budget assumptions and consider these reasonable.

The VJB faces significant challenges in the coming years to ensure it can continue to deliver services, critical for both elections as well as council tax collections. With the anticipated transition to three yearly valuation cycles from 2022, it will be critical that the VJB has robust plans in place to ensure that it has sufficient resources to meet these. As the VJB is reliant on constituent authority funding, it is critical that the VJB works closely with the Authority's to ensure there is a clear understanding of its financial requirements.

Action plan follow up 1.

The VJB faces financial and operational pressures going forward. It is critical that the VJB has clear medium term financial plans in place, aligned to its constituent authorities' plans to ensure sufficient resources are in place to meet these.



VJB Governance

The VJB has continued to develop and enhance its governance arrangements, including systems of internal control during the year.

During 2017/18, the VJB enhanced its risk management processes to ensure greater monitoring and oversight of strategic risks facing the organisation. Work continues to enhance internal audit arrangements, including communication between the Assessor and the Corporate Audit Manager to ensure timely resolution of audit issues and required follow up actions.

We are satisfied that the governance arrangements in place at the VJB are appropriate given the organisation's size and operating activities.

The management of financial risks during 2018/19 will continue to be critical for the VJB. The VJB continues to look to enhance its governance arrangements including regular discussion and engagement with Internal Audit.

Appendices

Action plan and follow up of 2016/17 recommendations

Audit adjustments

Independence, fees and fraud responsibilities

Communication of audit matters with the Board

Action plan and follow up of 2016/17 external audit recommendations

We are pleased to report that through our audit work in 2017/18, we have not identified any new risks which we consider are of a higher risk to the VJB. We have also completed follow up of our 2016/17 recommendations and this is reflected below for information.

Follow up of 2016/17 recommendations

Recommendation

Update

Medium term financial planning

Financial planning remains on a single year basis. There is a risk that there is a failure to appropriately consider the medium term financial strategy of the Board.

Recommend that longer term financial plans are developed in consultation with constituent authorities.

Issue outstanding

Financial plans are prepared on a one year basis with an annual budget approved for 2018/19. While we recognise that the VJB operates with one year funding settlements, there is an opportunity for the organisation to engage with constituent authorities to support longer term financial planning. This is increasingly important to ensure robust financial plans are in place to meet forecast operational and resource pressures.

Management response: For 2019/20 budget onwards 3 year estimates will be prepared. This will happen in conjunction with the constituent authorities although at this time they will not be in receipt of information from the Scottish Government on future funding availability and the valuation function is facing a period of uncertainty as it moves towards three yearly revaluations and the implementation of the Barclay Report recommendations that have been accepted by government.

Timescale: Board meeting February 2019

Action Owner: William Gillies, Assessor and Electoral Registration Officer

Identification and delivery of efficiency savings

There is an opportunity to enhance engagement between the Board and constituent authorities around the identification and delivery of efficiency savings.

Superseded

Observation superseded through recommendation above.

Audit adjustments

Uncorrected and corrected misstatements

We are pleased to report that there were no uncorrected misstatements to the financial statements arising during our audit.

The following adjustment was identified during the course of the audit and corrected in the financial statements.

Item	Dr (£'000)	(Cr) (£'000)	Description
1		(225)	<i>Being adjustment to recognise defined benefit pension scheme net assets.</i>
	225		

Disclosure misstatements

In accordance with auditing standards we are required to highlight significant disclosure misstatements to allow the Board to evaluate the impact of these matters on the financial statements. There were no material/significant disclosure misstatements identified we wish to bring to your attention. Minor changes included:

- Minor disclosure amendments inline with recommended disclosures including narrative in the remuneration report.

Fees, independence, fraud arrangements

External Audit Fee

Service	Fees £
External Auditor Remuneration	6,140
Pooled Costs	550
Contribution to Audit Scotland costs	390
Contribution to Performance Audit and Best Value	0
2017-18 Fee	7,080

The audit fee was calculated in accordance with guidance issued by Audit Scotland and agreed with Officers.

The above fee has not changed and our final fee was £7,080.

Fees for other services

Service	Fees £
We can confirm there are no non-audit fees for the 2017/18 financial year	Nil

Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention.

We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

We are required by auditing and ethical standards to communicate any relationships that may affect the independence and objectivity of the audit team.

We can confirm no independence concerns have been identified.

Fraud arrangements

In assessing our audit risks, the audit team was alert to the possibility of fraud at the VJB.

As part of our audit work we are responsible for:

- identifying and assessing the risks of material misstatement of the financial statements due to fraud in particular in relation to management override of controls.
- Leading a discussion with those charged of governance (for the VJB this is assumed to be the Board) on their view of fraud.
- designing and implementing appropriate audit testing to gain assurance over our assessed risks of fraud
- responding appropriately to any fraud or suspected fraud identified during the audit. – None were identified in-year

As auditors we obtain reasonable but not absolute assurance the financial statements as a whole are free from material misstatement, whether due to fraud or error.

We will obtain annual representation from officers regarding officers assessment of fraud risk, including internal controls, and any known or suspected fraud or misstatement.

It is the VJB's responsibility to establish arrangements to prevent and detect fraud and other irregularity. This includes:

- developing, promoting and monitoring compliance with standing orders and financial instructions
- developing and implementing strategies to prevent and detect fraud and other irregularity
- receiving and investigating alleged breaches of proper standards of financial conduct or fraud and irregularity.

Throughout the audit we worked with the VJB to review specific areas of fraud risk, including the operation of key financial controls.

We also examined certain policies in place, strategies, standing orders and financial instructions, as relevant to the fraud framework, to ensure that they provide a reasonable framework of internal control.

No suspected frauds or irregularities have been identified by Officers and reported in-year.

Communication of audit matters with the Accountable Officer

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and officers/those charged with governance who for the VJB we deem to be the Treasurer	•	
Overview of the planned scope and timing of the audit, including planning assessment of audit risks and wider scope risks	•	
Confirmation of independence and objectivity We are independent of the VJB and have not identified any conflicts of interest	•	•
A statement that we have complied with relevant ethical requirements regarding independence. Relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged. Details of safeguards applied to threats to independence We have not incurred any non-audit fees during the year and no threats to independence identified	•	•
Significant matters in relation to going concern No significant going concern matters identified	•	•
Views about the qualitative aspects of the VJB accounting and financial reporting practices, including accounting policies, accounting estimates and financial statement disclosures Set out in the Financial statements Section		•
Significant findings from the audit No significant findings from our audit		•
Significant matters and issues arising during the audit and written representations that have been sought Letter of representation will be shared and signed by the Accountable Officer when signing the financial statements. This is our standard, unmodified letter of representation.		•
Significant difficulties encountered during the audit No difficulties encountered		•
Significant deficiencies in internal control identified during the audit None identified		•
Significant matters arising in connection with related parties None identified		•
Identification or suspicion of fraud involving officers and/or which results in material misstatement of the financial statements None identified. A nil fraud return was submitted to Audit Scotland in April 2018 in accordance with the planning guidance.		•
Non-compliance with laws and regulations None noted		•
Unadjusted misstatements and material disclosure omissions None noted. Minor disclosure amendments only and these were not material in nature		•
Expected modifications to the auditor's report, or emphasis of matter None, an unqualified opinion		•

International Standards on Auditing (UK) (ISA) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table above.

We communicate any adverse or unexpected findings affecting the audit on a timely basis, either informally or via a report to the VJB Officers and the Board

