

To: All Members and Officers of the Audit and Standards Committee.

Please ask for: Carol Bloxham  
Telephone: (01785) 276155  
e-mail: carol.bloxham@staffordshire.gov.uk

**My Ref:**

**Your Ref:**

**Date:** 10 March 2016

Dear Sir/Madam,

**Audit and Standards Committee - Monday, 21st March, 2016**

I have recently forwarded to you a copy of the agenda for the next meeting of the Audit and Standards Committee.

I am now able to enclose, for consideration at next Monday, 21st March, 2016 meeting of the Audit and Standards Committee, the following reports that were unavailable when the agenda was printed.

7. **External Audit Plan 2015-16 (Pages 1 - 6)**

Report of Ernst & Young LLP - TO FOLLOW

8. **Staffordshire Pensions Fund External Audit Plan 2015-16 (Pages 7 - 12)**

Report of Ernst & Young LLP - TO FOLLOW

John Tradewell  
Director of Law and Governance

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# Staffordshire County Council

Year ending 31 March 2016

9 March 2016

Ernst & Young LLP



Building a better  
working world

# 1. Overview

## 1.1 Context for the audit

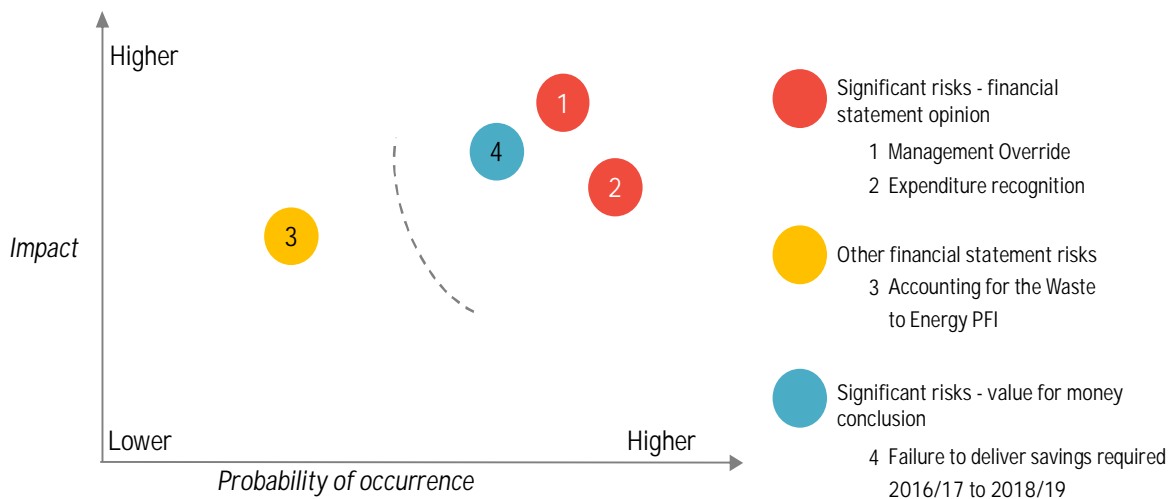
The Audit Plan covers the work that we plan to perform to provide you with:

- ▶ Our audit opinion on whether the financial statements of Staffordshire County Council (the Council) give a true and fair view of the financial position as at 31 March 2016 and of the income and expenditure for the year then ended; and
- ▶ A statutory conclusion on the Council's arrangements to secure economy, efficiency and effectiveness (the Value for Money conclusion).

The Audit Plan includes mandatory communications with the Audit Committee. We expect Members of the Audit Committee to have read the full audit plan to discharge their responsibilities as those charged with governance.

## 1.2 Audit risks

At this planning stage, the following 'dashboard' summarises the significant matters that we believe are relevant for our year-end audit:



## 1.3 Financial Statement Risks

### Significant risks

### Our audit approach

#### Management override risk

The risk of fraud exists in any organisation. However, frauds involving the manipulation of results to achieve performance targets would be particularly harmful to the Council's reputation.

Management has the primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has put in place a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

Based on the requirements of auditing standards our approach will focus on:

- ▶ Identifying fraud risks during the planning stages.
- ▶ Inquiry of management about risks of fraud and the controls put in place to address those risks.
- ▶ Understanding the oversight given by those charged with governance of management's processes over fraud.
- ▶ Consideration of the effectiveness of management's controls designed to address the risk of fraud.
- ▶ Determining an appropriate strategy to

## Significant risks

## Our audit approach

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	<p>address those identified risks of fraud.</p> <ul style="list-style-type: none"><li>▶ Developing a testing approach to journal entries.</li><li>▶ Assessing accounting estimates, particularly provisions, for evidence of management bias.</li><li>▶ Develop a testing strategy to test whether the Council has inappropriately capitalised revenue expenditure.</li><li>▶ Evaluating the business rationale for significant unusual transactions.</li><li>▶ Performing mandatory procedures regardless of specifically identified fraud risks.</li></ul>
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## Revenue and expenditure recognition

Under ISA 240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.

Having considered the risk factors set out in ISA240 and the nature of the revenue streams at Staffordshire County Council, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because:

- ▶ There is little incentive to manipulate revenue recognition.
- ▶ Opportunities to manipulate revenue recognition are very limited.

Revenue in this context has been modified by Practice Note 10 which states that auditors should also consider the risk that material misstatements due to fraudulent financial reporting may arise for the manipulation of expenditure recognition. We believe that a significant risk of expenditure recognition does exist within the financial statements of Staffordshire County Council.

Having considered the factors for expenditure recognition, we believe the risk lies within other operating expenditure and in particular the completeness of short term creditors (specifically accruals) and the completeness of 'other service expenditure' (as defined by the Council in its financial statements).

We will:

- ▶ Review and test expenditure recognition policies.
- ▶ Review and discuss with management any accounting estimates on expenditure recognition for evidence of bias.
- ▶ Develop a testing strategy to test material revenue and expenditure streams.
- ▶ Develop a testing strategy to test material creditors at the year end.

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We have identified other key areas of the audit that have not been classified as significant risks but are still important when considering the risks of material misstatement to the financial statements and disclosures.

## Other financial statement risks

## Our audit approach

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<p>PFI</p> <p>The Council has four PFI Schemes, the most significant of which is the Waste to Energy PFI Scheme, which has a liability at 1 April 2015 of £165 million.</p> <p>Accounting for this material scheme requires the use of a complex financial model, the calculation of estimates and the application of management judgement. As such, it is an area of particular focus and requires the use of specialist input in this first year.</p>	<p>We plan to:</p> <ul style="list-style-type: none"><li>▶ Confirm the accounting arrangements under IFRIC 12 Accounting for Service Concessions.</li><li>▶ Review and audit the consequential accounting entries that result from the decisions made under IFRIC 12, including the calculation of the overall liability, valuation of the asset, and identifying the correct split between capital and revenue within the contract.</li><li>▶ Test the integrity of the financial model used by the Council.</li><li>▶ Test the completeness and accuracy of the inputs to the financial model and the subsequent correct application of the outputs to the financial statements.</li></ul>
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## **1.4 Respective responsibilities in relation to fraud and error**

Management has the primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

## **1.5 Economy, Efficiency and Effectiveness**

We are only required to determine whether there are any risks that we consider significant.

Our risk assessment supports the planning of sufficient work to enable us to deliver a safe conclusion on arrangements to secure value for money and enables us to determine the nature and extent of further work that may be required. If we do not identify any significant risks there is no requirement to carry out further work.

Our risk assessment has therefore considered both the potential financial impact of the issues we have identified, and also the likelihood that the issue will be of interest to local taxpayers, the Government and other stakeholders.

Having completed our risk assessment, we believe a significant risk exists in relation to the Council's medium term financial position.

Our approach to this risk will be to:

- ▶ Document the Council's approach to the identification, development and implementation of efficiencies and savings.
- ▶ Assess the Council's overall arrangements, plans and risk strategy.
- ▶ Review key financial reports, including the 2015/16 outturn position to evaluate the Council's record of financial management.
- ▶ Assess the Council's key financial performance indicators.
- ▶ Evaluate the Council's internal risk assessment of savings identified across 2016/17 to 2018/19.

We will remain alert to the possibility of new or emerging significant risks as our audit progresses. In particular, we will keep under review:

- ▶ The work and reports of regulators, such as the Care Quality Commission and OFSTED.
- ▶ The local health economy, including adult social care, and in particular the outcome measures of the Better Care Fund.
- ▶ The outcome of other aspects of assurance work, such as the audited financial position and the Head of Internal Audit's opinion.

## **1.6 Fees**

PSAA has published a scale fee for all authorities. The indicative scale fee for the audit of Staffordshire County Council is £109,755.

## 1.7 Timetable of communication and deliverables

Audit phase	Timetable	Audit Committee timetable	Deliverables
High level planning	January 2016	February 2016	
Risk assessment and interim testing of routine processes and controls	February 2016	March 2016	Audit Plan
Year-end audit	July 2016		
Completion of audit	August 2016	September 2016	Report to those charged with governance via the Audit Results Report Audit report (including our opinion on the financial statements; and overall value for money conclusion). Audit completion certificate Reporting to the NAO on the Whole of Government Accounts return.
Conclusion of reporting	October 2016	October 2016	Annual Audit Letter
Benefit claim	May – November		Certified claim
Reporting on certification work	December	December 2016	Annual certification work report

## 1.8 Further reading in the Audit Plan

Areas not covered in this summary, but should be read by the Audit Committee to discharge its governance responsibilities:

- ▶ Financial Statement risk assessment
- ▶ Responsibilities in relation to fraud and error
- ▶ Value for money conclusion risk assessment
- ▶ Audit process and strategy
- ▶ Group audit scope
- ▶ Key processes
- ▶ Use of analytics
- ▶ Internal audit
- ▶ Use of management and EY experts
- ▶ Mandatory procedures required by auditing standards
- ▶ Materiality
- ▶ The audit team
- ▶ Fees and assumptions
- ▶ Independence
- ▶ Required communications with those charged with governance.

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Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

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# Staffordshire Pension Fund

Year ending 31 March 2016

Audit Plan

21 March 2016

Ernst & Young LLP



# 1. Overview

## 1.1 Context for the audit

This Audit Plan covers the work that we plan to perform to provide you with:

- ▶ Our audit opinion on whether the financial statements of Staffordshire Pension Fund (the Pension Fund) give a true and fair view of the financial position as at 31 March 2016 and of the income and expenditure for the year then ended; and
- ▶ Our opinion on the consistency of the pension fund financial statements within the pension fund annual report with the pension fund financial statements

The Audit Plan includes mandatory communications with the Audit Committee. We expect Members of the Audit Committee to have read the full audit plan to discharge their responsibilities as those charged with governance.

## 1.2 Risks

As part of our initial analysis we have identified the following two external risk areas:

Local Government Pension Scheme Investment Reform	Challenging Market Conditions
<ul style="list-style-type: none"> <li>• On 25 November 2015, the Department for Communities and Local Government published their Investment Reform Criteria and Guidance along with a consultation on Local Government Pension Scheme Regulations 2016. We note that:</li> <li>• Authorities are required to collaborate and invest in asset pools, each with at least £25bn of Local Government Pension Scheme assets.</li> <li>• In February you submitted your initial response to pooling and progress towards formalising arrangements with other authorities. Refined and completed submissions are expected in July 2016.</li> </ul>	<ul style="list-style-type: none"> <li>• The current global economic, political and market conditions, have created uncertainty for investors. We note that:</li> <li>• European markets have achieved variable results given continued concern over the ISIS situation and the refugee crisis. Furthermore, the VW diesel emissions scandal has created uncertainty towards the perception of European manufacturers generally.</li> <li>• The International Monetary Fund expects China's economy to grow by 6.3% this year and 6% in 2017, marking its slowest growth in a quarter of a century. China's growth is seen as a driver of the global economy, and is a major concern for investors globally.</li> <li>• Oil prices hit a four-year low in November eroding any small gains by the oil-producing nations, which has translated into rising financial distress and postponement of capital investment across the sector.</li> </ul>

## 1.3 Financial statement risks

Significant risks (including fraud risks)

Our audit approach

### Risk of management override

Under ISA (UK and Ireland) 240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. At EY, we identify that the risk of fraud in revenue recognition at a pension fund is applicable to contribution income and investment

Contributions

We will:

- ▶ Perform a detailed analytical review of contributions received compared to our expectations based upon member numbers for each employer and contribution rates,

Significant risks (including fraud risks)	Our audit approach
income. Our audit approach has therefore been split between these two forms of revenue.	<p>which are provided by the actuary</p> <ul style="list-style-type: none"> <li>▶ Review the ratio of member to employer contributions on a monthly basis to ensure there are no unexplained variances</li> <li>▶ Review the timeliness of the payment of contributions to the scheme, including ensuring that contributions relate to the correct financial year</li> </ul>
	<p>Investment Income</p> <p>We will:</p> <ul style="list-style-type: none"> <li>▶ Obtain third party confirmations and agree all investment income to the confirmations</li> <li>▶ Review and test investment reconciliations performed between investment manager and custodian reports</li> </ul>

We have identified other key areas of the audit that have not been classified as significant risks but are still important when considering the risks of material misstatement to the financial statements and disclosures.

Other financial statement risks	Our audit approach
<b>Valuation of complex investments (Unquoted investments)</b>	
<p>The Fund's investments include unquoted pooled investment vehicles and direct property investments.</p> <p>Judgements are taken by the Investment Managers to value those investments whose prices are not publically available. The material nature of Investments means that any error in judgement could result in a material valuation error.</p> <p>Current market volatility means such judgments can quickly become outdated, especially when there is a significant time period between the latest available audited information and the fund year end. Such variations could have a material impact on the financial statements.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>▶ Review the basis of valuation for property, private equity funds and other alternative investments and assess the appropriateness of the valuation methods used</li> <li>▶ Review the latest audited accounts for all underlying investment vehicles and ensure there are no matters arising that highlight weaknesses in the funds valuation</li> <li>▶ Perform tests of valuation such as reviewing transactions around the year end, performing 'look through' testing or obtaining latest available audited accounts and auditing any subsequent cash movements between the date of the audited accounts and the Fund's year end</li> <li>▶ Where necessary our internal valuation specialists will support our work in this area</li> </ul>

## 1.4 Responsibilities in relation to fraud and error

We would like to take this opportunity to remind you that management has the primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

## 1.5 Fees

The indicative fee scale for the audit of Staffordshire Pension Fund is £28,637

## 1.6 Timetable of communication, deliverables and insights

We have set out below a timetable showing the key stages of the audit and the deliverables we have agreed to provide to the Council through the Audit Committee's cycle in 2015/16. These dates are determined to ensure our alignment with PSAA's rolling calendar of deadlines.

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Chair as appropriate.

Audit phase	Timetable	Audit Committee timetable	Deliverables
Risk assessment and setting of scopes	February 2016	21 March 2016	Audit Plan
Testing routine processes and controls	March 16	September 2016	
Year-end audit	Commencing July		
Completion of audit	September 16	September 2016	Report to those charged with governance via the Audit Results Report Audit report on our opinion on the financial statements Audit report on our opinion on the consistency of the financial statements within the pension fund annual report with the pension fund financial statements

## 1.7 Further reading in the Audit Plan

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Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

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