

Derry City & Strabane District Council

Audit Strategy 2018-19



Contents	Page
1. Key Messages	3
2. Materiality	6
3. Our Audit Approach	7
4. Audit Timetable, Staffing and Fees	13

We have prepared this report for Derry City and Strabane District Council's sole use. You must not disclose it to any third party, quote or refer to it, without our written consent and we assume no responsibility to any other person.

1. Key Messages

Background

The Local Government Auditor is the independent external auditor of Derry City and Strabane District Council's ("the Council") Statement of Accounts under the Local Government (Northern Ireland) Order 2005. In addition to the audit of the financial statements, the Local Government Auditor has a statutory duty to be satisfied the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of its resources.

The Local Government Auditor (LGA) is also required to conduct an improvement audit and assessment each year under Part 12 of the Local Government Act (Northern Ireland) 2014 (the Act) and the statutory '*Guidance for Local Government Performance Improvement 2016*', (the Guidance).

Purpose

The purpose of this document is to highlight to the Chief Financial Officer and the Audit and Risk Committee of the Council:

- how we, on behalf of the Local Government Auditor (LGA), plan to audit the financial statements for the year ending 31 March 2019 including how we will be addressing significant risks of material misstatement to transactions and balances;
- how we, on behalf of the LGA, plan to audit the proper arrangements in place for securing economy, efficiency and effectiveness in the use of resources for the year ending 31 March 2019;
- how we, on behalf of the LGA, plan to conduct an improvement audit and assessment;
- matters of interest and developments in financial reporting and legislation;
- the planned timetable, fees and audit team; and
- matters which we are required to communicate to you under International Standards on Auditing (ISAs), including the scope of the audit, our respective responsibilities, and how we maintain independence and objectivity.

Significant Audit Risks

We plan our audit of the financial statements to respond to the risks of material misstatement to transactions and balances and the risk regarding the legality of the Council's expenditure. We have identified the following significant risk which would impact on our audit approach:

- Uncertainty around the going concern status of the City of Derry Airport (CODA).

Proper Arrangements

We will reissue the Questionnaire we have used in previous years to the Council. We will review the Council's responses and perform additional work in areas considered to be of higher risk. The main financial audit work will also feed into the risk assessment and conclusions of arrangements in place.

Conclusions regarding proper arrangements will be noted in the Report to those charged with Governance including any recommendations for improvement.

Materiality

When setting materiality, we consider both qualitative and quantitative aspects that would reasonably influence the decisions of users of the financial statements. The overall account materiality is £1.6m for Council and £1.65m for the Group. Materiality will be reassessed during the audit.

Performance Improvement

The LGA will undertake a full assessment of whether the Council is likely to comply with its performance improvement responsibilities under the Act in 2019. In preparation for this, the Council should ensure that:

- it has established adequate performance improvement arrangements;
- it has substantive evidence to demonstrate improvement; and
- it has addressed any outstanding Proposals for Improvement made by the LGA in previous years.

Audit team and fee

Mrs Colette Kane will be responsible for the overall audit. The full engagement team is presented on page 16.

Our audit fee for the Council and its Group for this year is estimated to be £55,000. In addition, audit work in respect of the North West regional Development Group may necessitate a further fee of up to £2,000.

Actions for the Audit and Risk Committee

The Committee should discuss:

- Whether our assessment of the risks of material misstatement to the financial statements is complete;
- Whether management has plans in place to address the risks identified by NIAO and whether these plans are adequate;
- Our proposed audit response to address these risks; and
- Whether the financial statements could be materially misstated due to fraud, and communicate any areas of concern to management and the audit team.

2. Materiality

Basis for overall materiality calculation

- Council: £79.6m - Prior Year gross expenditure
- Group: £82.6m - Prior Year gross expenditure

Overall account materiality (X%)

- Council: £1.6 million (2%)
- Group: £1.65 million (2%)

Error reporting threshold

- We report to you all misstatements, whether adjusted or unadjusted, above £16k

A matter is material if its omission or misstatement would reasonably influence the decisions of the users of the financial statements. The assessment of what is material is a matter of the auditor's professional judgement and includes consideration of both the amount and the nature of misstatement.

The concept of materiality recognises that absolute accuracy in financial statements is rarely possible. An audit is therefore designed to provide reasonable, rather than absolute, assurance that the financial statements are free from material misstatement or irregularity. We apply this concept in planning and performing our audit, and in evaluating the effect of identified misstatements on our audit and of uncorrected misstatements, if any, on the financial statements and in forming the audit opinion. This includes the statistical evaluation of errors found in samples which are individually below the materiality threshold but, when extrapolated, suggest material error in an overall population. As the audit progresses our assessment of both quantitative and qualitative materiality may change.

We also consider materiality qualitatively. In areas where users are particularly sensitive to inaccuracy or omission, we may treat misstatements as material even below the principal threshold(s). These areas include:

- the remuneration report;
- movements on reserves;
- the legality of expenditure; and
- our audit fee

3. Our Audit Approach

The NIAO audit approach is risk-based, informed by an understanding of the operations of the Council and an assessment of the risks associated with the financial statements and the legality of underlying transactions. For all significant audit areas, we will use a variety of audit techniques, including analytical procedures and sampling of transactions. We will review other accounting systems and management controls operated by the Council only to the extent we consider necessary for the effective performance of the audit.

Independence

- We are independent of the Council in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed entities/public interest entities. We have fulfilled our ethical responsibilities in accordance with these requirements and have developed important safeguards and procedures in order to ensure our independence and objectivity.
NIAO quality standards and independence can be found at <https://www.niauditoffice.gov.uk/publications/niao-quality-standards-and-independence> .

Management of Personal Data

- During the course of our audit we have access to personal data to support our audit testing. We have established processes to hold this data securely within encrypted files and to destroy it where relevant at the conclusion of our audit.

Using the work of Internal Audit

- We liaise closely with internal audit throughout the audit process and seek to take assurance from their work where their objectives cover areas of joint interest.

Scope of the audit

The scope of our audit and respective responsibilities can be found at

<https://www.niauditoffice.gov.uk/publications/scope-financial-audit-respective-responsibilities-and-other-matters>

The Code of Audit Practice issued by the Local Government Auditor extends to not only the audit of financial statements but also to aspects of financial and corporate arrangements to secure the economic, efficient and effective use of resources. The Code can also be viewed on the NIAO website at

<https://www.niauditoffice.gov.uk/publications/code-audit-practice-2016>.

Respective Responsibilities in the preparation of the financial statements

In line with Auditing Standards we are required to agree the respective responsibilities of the Local Government Auditor, the Council's Chief Financial Officer and the NIAO. These responsibilities are set out in the Statement of Responsibilities of Local Government Auditors and Local Government Bodies issued by the Local Government Auditor. The Statement of Responsibilities can be viewed on the NIAO website at <https://www.niauditoffice.gov.uk/publication/statement-responsibilities-local-government-auditor-and-local-government-bodies>.

The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

Proper Arrangements in place to secure economy, efficiency and effectiveness

Under the Code of Audit Practice we are also required to perform an initial assessment of significant risks to the conclusion on proper arrangements in place to secure economy efficiency and effectiveness in the use of its resources. Our initial assessment indicates audit risk in the following area:

- **Procurement:** In recent years there have been a number of procurement propriety issues. We will review processes and controls in this area against current best practice, and also the results of our procurement/ expenditure sample tests of detail.

Performance Improvement

The Local Government (Northern Ireland) Act 2014 prescribes responsibilities for the Local Government Auditor regarding the audit and assessment of performance improvement arrangements in Councils. This work will be conducted in accordance with the Act, the Guidance, the Local Government Code of Audit Practice 2016 and the LGA's Statement of Responsibilities, and includes:

- an improvement audit for the purposes of determining:
 - (a) whether the Council has, during the year, discharged its duties under section 92 of the Act; and
 - (b) the extent to which the Council has, during the year, acted in accordance with any guidance issued by the Department about any Council duties under section 92;
- an improvement assessment for the purpose of determining whether the Council is likely, during the year, to comply with the requirements of Part 12 of the Act; and
- issuing a report, or reports, in respect of the Council to the Council and the Department, under section 95 of the Act; and
- producing and publishing an annual improvement report under section 97 of the Act.

The Act also allows the LGA to:

- carry out an assessment for the purpose of determining whether the Council is likely to comply with the requirements of Part 12 of the Act in subsequent financial years; and
- carry out a special inspection of the Council's compliance with the requirements of Part 12 if the LGA is of the opinion that the Council may fail to comply with the requirements of Part 12 of the Act.

The audit team will request access to all relevant documents and Council officers. Sharing our 'audit work programme' in advance of the audit will assist the Council in preparing for the audit fieldwork. We suggest the Council prepares a file of audit evidence in advance of the fieldwork stage, cross referenced to specific paragraphs or sections of the documents providing the necessary evidence. This should help us deliver a more efficient audit.

Significant Audit Risks

A significant risk is an identified and assessed risk of material misstatement that, in the auditor's judgement, requires special audit consideration. As part of our work to develop our audit plan, we have identified the following significant risk of material misstatement and our approach to address this risk.

Significant Risk 1

City of Derry Airport (CODA)

In 2017-18 there was some uncertainty around the going concern status of the Airport. The Financial Statements included disclosures explaining this and the Local Government Auditor included an emphasis of matter paragraph with her audit opinion drawing attention to this matter. It is our understanding from recent discussions with senior officials at the Council that a funding package has now been informally approved between CODA, the Government Departments and a Commercial Airline. This package is expected to deliver two PSO routes out of the CODA to London and Manchester over a two year period from May 2019 to May 2021. These routes are critical to the ongoing viability of the Airport.

Failure to deliver this funding package could impact on the Council's Group accounts, including note disclosure in the financial statements, and potential provisions for costs and the carrying value of airport assets.

Audit Response

We will review the signed agreement between the parties and seek evidence of proof of funding in the period post signing letter of offer to date of certification of accounts. This will allow us to properly assess the going concern status of the Airport and whether it impacts on the Council's closing financial position. We will consider the adequacy of disclosures made on the position regarding the Airport within the financial statements.

Under ISA 240, there is a presumed significant risk of material misstatement owing to fraud arising from management override of controls. We will address this risk through our testing of journals, estimates and through a review of any significant or unusual transactions in the year.

There is also a presumed risk of fraud in revenue recognition, albeit rebuttable. While we have rebutted this risk on the grounds that we feel this risk is likely not to be material, being conscious of the amount of cash received by Council at its external sites, we will consider controls over cash income and each year perform cyclical income testing at a sample of Council establishments.

Other risk factors

We have identified a number of other risk factors. We do not consider these to represent a significant risk of material misstatement in the financial statements but are matters which we will continue to monitor and respond to as appropriate throughout the audit. These areas include:

PROVISIONS:

Property revaluations were carried out as at 31st March 2015 for the purposes of Rates. A large number of appeals have been lodged with LPS and are still ongoing. If these appeals are successful there could be a significant hit to the amount of Rates grant received from Central Government. We will assess the impact of any potential reductions to the Rates Grant and ensure adequate disclosures are included within the financial statements.

Software system Upgrade

The Council plan to upgrade the Agresso financial accounting package shortly as it is becoming increasingly difficult for the supplier to provide maintenance support for what is an old software package. There is a risk that the upgrade could have an impact on the preparation of the financial statements. We will assess the impact if any on the financial statements during the course of the audit.

Further matters of interest

Narrative Report / 'Telling the Story'

Last year was the first year the Council presented its accounts in the new format prescribed by the Code which was designed to give users of the accounts a greater understanding of how the Council has utilised its resources. Whilst the minimum requirements were presented in 2017-18, we recommend that additional information is included.

Chapter 3 of the Code of Practice on Local Authority Accounting in the UK [*the Code*] states, "the Narrative Report should provide a commentary on how the authority (including the Group Accounts) has ***used its resources to achieve its desired outcomes in line with its objectives and strategies.***" In our view, Councils could further improve the clarity of the information presented in this respect and therefore we recommend the Council presents more clearly how information in the financial accounts links to the achievement of its strategic objectives and strategies in the period. This will help the users of the accounts understand more clearly the work of the Council and how it has utilised its resources in the reporting period.

Key Changes to the Code in 2018-19

There have been some changes to financial reporting guidance which affect the preparation of your financial statements and will impact on our audit plan. These are detailed below:

- 1) **IFRS 15 Revenue Recognition** – this standard comes into effect for 2018-19 accounts. The main purpose of IFRS 15 is to recognise revenue on the transfer of control rather than the transfer of risks and rewards. It involves reviewing all contracts with service recipients to assess when income should be recognised in the reporting period. The standard also requires additional disclosures to be made.
- 2) **Financial Instruments** – IFRS 9 is adopted by the Code (Chapter 7) for 2018-19 accounts. The standard puts more emphasis on valuing financial instruments at fair value. This is a complex area and there are a number of adaptations made in the Code for Councils' circumstances. Disclosures in the notes to the accounts will also need to be updated for the new standard's requirements.

Brexit

During our audit we will consider any possible impacts Brexit might have on council's activities going forward. We will review the adequacy of disclosures made by Council in this respect.

4. Audit Timetable, Fees and Staffing

Financial Audit and Proper Arrangements Timetable

The timetable comprises an interim visit commencing on 9 January for 3.5 weeks and a final visit commencing 8 July with certification planned for 27 September 2019. This timetable has been agreed with management.

Interim audit testing commences	• 9 January 2019
Electronic version of draft financial statements provided to NIAO	• 28 June 2019
Final audit testing commences	• 8 July 2019
Audit Committee Meeting	• Week commencing 16 September 2019 (TBC)
Council/Committee Meeting to approve final accounts	• Week commencing 16 September 2019 (TBC)
Signed financial statements and Letter of Representation provided to NIAO	• Week commencing 16 September 2019 (TBC)
Financial statements certified by LGA	• by 30 September 2019
Provisional Report issued for management response	• Week commencing 9 September 2019 (TBC)
Final Report to those charged with Governance issued	• 21 October 2019
Annual Audit Letter	28 October 2019

Submission of Accounts

The Council is required to submit its account to the Department for Communities by 30 June following the year end. The Department then forwards on a hard copy of the accounts to NIAO for audit. It would assist the audit process hugely if an electronic version of the accounts, along with the excel spreadsheet underpinning them, were forwarded to NIAO at the same time as being sent to the Department.

Public Notice

The Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015 requires the Council to give notice, by publication on its website, of the date from which the accounts and other documents are available for public inspection and the date from which the exercise of rights under Article 17 and 18 of the Order may be exercised. In the current audit timeframe, notice should be placed on websites in early July. The LGA usually writes to councils closer to the time to remind them of this requirement as the audit of the accounts cannot be certified as being completed until the notice period has been executed in full.

Objections

The 2005 Order allows objections to be raised from interested parties concerning the Council's accounts. We will hear and carefully consider representations by, and objections from, any such interested parties. In conducting our audit we may consider the lawfulness of items of account, the conduct of members and officers, instances where it appears a loss may have arisen and our other statutory duties required of the Local Government Auditor.

Improvement Audit and Assessment Timetable

This timetable has been agreed with management and incorporates dates set out in the 2014 Act and the Guidance.

Planning phase	•April / May 2019
Council publishes performance improvement plan	•Not later than 30 June 2019 *
Fieldwork phase	•July - October 2019
Council to publish an assessment and comparison of its performance	•no later than 30 September 2019
Preliminary Audit Findings report issued to Performance Manager for factual accuracy agreement	•1 November 2019
Reporting Phase - Draft S95 report issued to Chief Executive for factual accuracy agreement	•15 November 2019
Reporting Phase - Final S95 report issued to the Council and Department	•30 November 2019
Publications of Council's Annual Improvement Report	•no later than 31 March 2020

*The Act indicates that councils should publish their improvement plan as soon as practical after the start of the financial year to which it relates. The Guidance recommends this is completed by the end of June to enable the LGA to meet the statutory reporting deadline of 30 November.

Fees

The audit fees are estimated to be as follows:

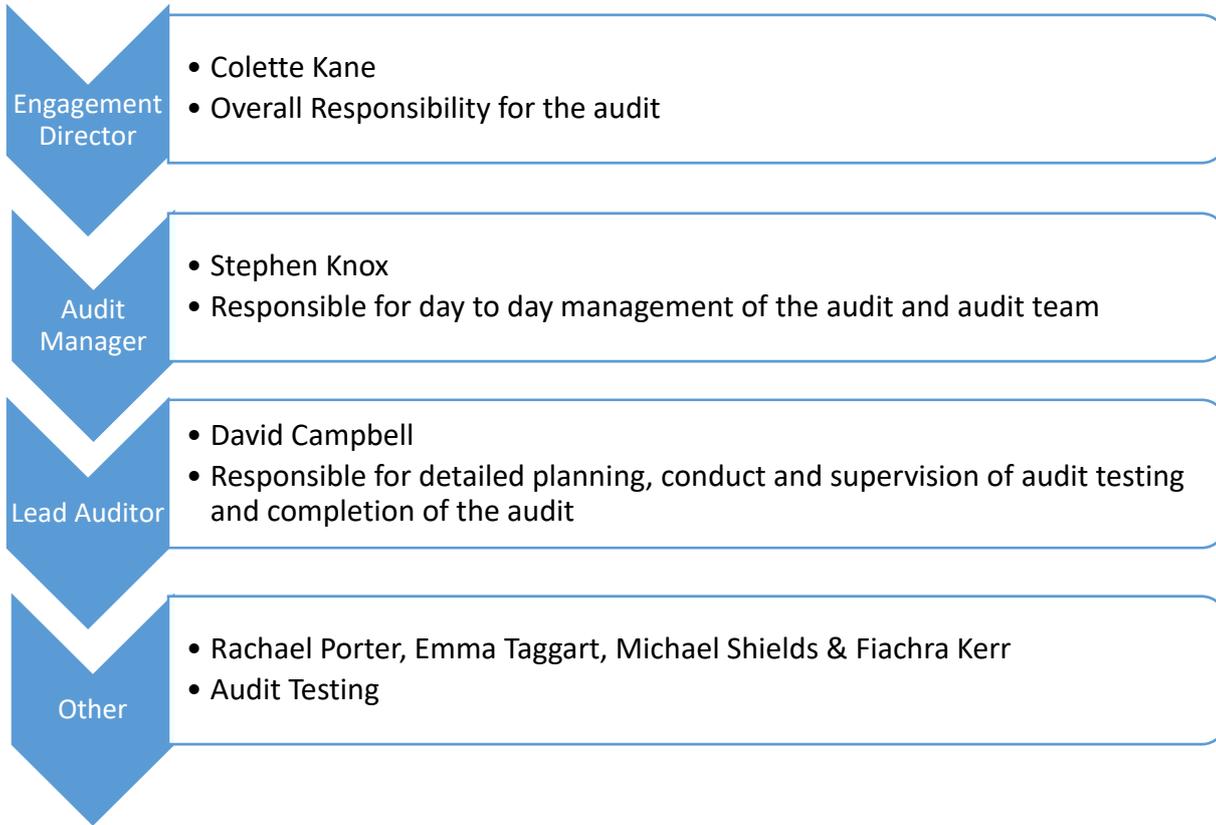
- £57,000 for the Council's Statement of Accounts; and
- £22,000 for the performance improvement audit and assessment; and
- £1,100 for National Fraud Initiative work.

Completion of our audits in line with the timetables and fees are dependent upon:

- The Council delivering on or before 30 June 2019 a complete Statement of Accounts of sufficient quality that have been subject to appropriate internal review.
- The Council delivering good quality supporting documentation and evidence, within the agreed timetables for both the financial and improvement audits;
- Appropriate client staff being available during the audit; and
- Availability of evidence to support our audit work on performance improvement and assessment.

Staffing

Statement of Accounts and Proper Arrangements audit work



Improvement Audit and Assessment work

