

# Scottish Government Non- Domestic Rating Account

Annual Audit Plan 2016/17



 AUDIT SCOTLAND

Prepared for Scottish Government

May 2017

## Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



## About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

# Contents

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<b>Risks and planned work</b>	<b>4</b>
Audit risks	4
Reporting arrangements	6
Audit fee	6
Responsibilities	6
<b>Audit scope and timing</b>	<b>8</b>
Financial statements	8
Internal audit	9
Audit dimensions	10
Independence and objectivity	11
Quality control	11

# Risks and planned work

1. This annual audit plan contains an overview of the planned scope and timing of our audit and is carried out in accordance with International Standards on Auditing (ISAs), the [Code of Audit Practice](#), and any other relevant guidance. This plan identifies our audit work to provide an opinion on the financial statements and related matters and meet the wider scope requirements of public sector audit. The wider scope of public audit contributes to conclusions on the appropriateness, effectiveness and impact of corporate governance, performance management arrangements and financial sustainability.

## Audit risks

2. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for the Scottish Government Non-Domestic Rating Account (NDR Account). The NDR account includes transactions that are audited as part of other financial statements (i.e. local authority annual accounts). We have categorised these risks into financial risks and wider dimension risks. The key audit risks, which require specific audit testing, are detailed in [Exhibit 1](#).

## Exhibit 1

Audit Risk	Management assurance	Planned audit work
<b>Financial statement issues and risks</b>		
<p><b>1 Risk of management override of controls</b></p> <p>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.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable.</p>	<p>Detailed testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Evaluation of significant transactions that are outside the normal course of business.</p>
<p><b>2 Income</b></p> <p>Local Authorities receive 50% of all additional income received from the Business Rates Incentivisation Scheme (BRIS) scheme. This audit risk requires us to assess whether all income relating to BRIS is included in Local Authority returns.</p>	<p>Income is audited by Local Authority external auditors.</p>	<p>Detailed testing of revenue transactions focusing on the areas of greatest risk.</p>

Audit Risk	Management assurance	Planned audit work
<p><b>3 Estimation and judgements</b></p> <p>There is a significant degree of management estimation in the measurement and valuation of the Distributable amount. This is because the amount needs to be set in advance of the financial year. This audit risk requires us to assess whether this represents an increased risk of misstatement in the financial accounts.</p>	<p>The LA returns are monitored closely for differences between iterations.</p>	<p>Focused substantive testing of key areas.</p>
<p><b>Wider dimension risks</b></p>		
<p><b>4 Financial sustainability</b></p> <p>There is an increasing divergence between amounts collected and distributed by the NDR account. At the start of 2016/17 it had a negative balance of £284 million that impacts on the Scottish Consolidated Fund.</p> <p>There is a risk that the decisions Ministers have made are insufficient to achieve the year on year balance required to maintain the financial sustainability of the account.</p>	<p>Adjustments of £20 million were made to the distributable amount in this year in an attempt to reduce the negative balance.</p>	<p>Detailed testing of key calculations.</p>
<p><b>5 Governance and transparency</b></p> <p>Governance arrangements for the scrutiny of the NDR Account have changed following the Scottish Government's review of governance in 2016. The Accountable Officer for the NDR Account is the Director General Communities.</p> <p>Scrutiny of annual accounts by an Audit and Risk Committee and/or a Corporate Board is a feature of good corporate governance.</p> <p>We will review the revised governance arrangements and assess whether they provide effective oversight and assurances. This is especially relevant at this time where the shortfall from the NDR account is increasing and impacting on the Scottish Consolidated Fund.</p>	<p>DG Communities fulfils the primary role of formal oversight of the NDR Account. The Scottish Government Audit and Assurance Committee will provide the forum for escalation purposes.</p>	<p>On-going liaison with Scottish Government officials to clarify reporting arrangements to those charged with governance.</p>

## Reporting arrangements

3. Audit reporting is the visible output for the annual audit. All annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest will be published on our website: [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk)
4. 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 relevant officer(s) to confirm factual accuracy.
5. We will provide an independent auditor's report to the Scottish Government, Scottish Parliament and the Auditor General for Scotland summarising the results of the audit of the annual accounts. We will provide the Accountable Officer and Auditor General for Scotland with an annual report on the audit containing observations and recommendations on significant matters which have arisen in the course of the audit.
6. It is the responsibility of DG Communities to prepare the financial statements in accordance with Schedule 12 of the Local Government Finance Act 1992 and present them to Parliament.

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## Exhibit 2

### 2016/17 Audit outputs

Audit Output	Target date
Annual Audit Report including ISA 260 requirements	30 September 2017
Signed Independent Auditor's Report	30 September 2017

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## Audit fee

7. The proposed audit fee for the 2016/17 audit of the NDR account is £10,690. In determining the audit fee we have taken account of the risk exposure of the NDR Account, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited financial statements, with a complete working papers package before 30 June 2017.
8. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises out with our planned audit activity.

## Responsibilities

### Audit Committee and Accountable Officer

9. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.
10. The audit of the financial statements does not relieve management or the Scottish Government Audit and Assurance Committee (SGAAC), as those charged with governance, of their responsibilities.

### **Appointed auditor**

- 11.** Our responsibilities as independent auditor are established by the Public Finance and Accountability (Scotland) Act and the Code of Audit Practice, and guided by the auditing profession's ethical guidance.
  
- 12.** Auditors in the public sector give an independent opinion on the financial statements. We also review and report on the arrangements within the audited body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

# Audit scope and timing

## Financial statements

**13.** The statutory financial statements audit will be the foundation and source for the majority of the audit work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the operation of the Scottish Government Non-Domestic Rating Account and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how the NDR account will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free of material misstatement.

**14.** We will give an opinion on the financial statements as to:

- whether they properly present the receipts and payments for the financial year, and the balances held at the year end
- whether they have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements
- the regularity of the expenditure and income.

## Materiality

**15.** Materiality defines the maximum error that we are prepared to accept and still conclude that that our audit objective has been achieved. It helps assist our planning of the audit and allows us to assess the impact of any audit adjustments on the financial statements. We calculate materiality at different levels as described below. The calculated materiality values for the NDR Account are set out in [Exhibit 3](#).



## Exhibit 3

### Materiality values

Materiality level	Amount
<b>Planning materiality</b> - This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It has been set at 1% of gross expenditure for the year ended 31 March 17 based on the audited accounts for 2015-16.	£27.7 million
<b>Performance materiality</b> - This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 75% of planning materiality.	£20.8 million
<b>Reporting threshold</b> - We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 1% of planning materiality as £0.208 million but rounded to £0.200 million.	£0.200 million

16. We review and report on other information published with the financial statements including the management commentary, and the annual governance report. Any issues identified will be reported to SGAAC.

### Timetable

17. To support the efficient use of resources it is critical that a financial statements timetable is agreed with us for the production of the unaudited accounts. An agreed timetable is included at [Exhibit 4](#) which takes account of submission requirements and planned SGAAC dates:

## Exhibit 4

### Financial statements timetable

 Key stage	 Date
Communication as to clarification of working papers expectation	30 April 2017
Latest submission date of unaudited Scottish Government Non Domestic Rates financial statements with complete working papers package	30 June 2017
Latest date for final clearance meeting with the Local Government Finance team	8 September 2017
Agreement of audited unsigned financial statements; Issue of Annual Audit Report including ISA 260 report to those charged with governance	21 September 2017
Independent auditor's report signed	26 September 2017

### Internal audit

18. 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. However given the audit approach of the NDR Account is wholly substantive in nature and there is no specific internal audit work which we aim to take assurance from this year.

## Audit dimensions

19. Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#).

### Exhibit 5

#### Audit dimensions



#### Financial sustainability

20. As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the body's financial sustainability in the longer term. We define this as medium term (two to five years) and longer term (longer than five years) sustainability. In relation to the NDR account, we will carry out work and conclude on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of arrangements in place to address any identified funding gaps
- whether the Scottish Government can demonstrate the affordability and effectiveness of funding and investment decisions it has made.

#### Financial management

21. Financial management is concerned with financial capacity and whether the control environment and internal controls are operating effectively. Responsibility for the preparation of the NDR account lies with the Scottish Government's Local Government Finance team. They collate and prepare the NDR account based on audited information from other financial statements. In relation to the NDR account, we will review, conclude and report on:

- whether the Scottish Government has arrangements in place to ensure systems of internal control are operating effectively for the preparation of the NDR account
- whether the Scottish Government can demonstrate the effectiveness of their system in communicating accurate and timely financial information in the NDR account

- how the Scottish Government has assured itself that its capacity and skills are appropriate in preparing the NDR account
- whether the Scottish Government has established appropriate and effective arrangements for the prevention and detection of fraud and corruption in preparing the NDR account.

### Governance and transparency

**22.** Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information. In relation to the NDR account, we will review, conclude and report on:

- whether the Scottish Government can demonstrate that the new governance arrangements in place are appropriate and operating effectively
- whether there is effective scrutiny, challenge and transparency of decision-making and reports
- the quality and timeliness of financial reporting.

### Value for money

**23.** Value for money refers to using resources effectively and continually improving services. In relation to the NDR account, we will review, conclude and report on whether:

- the Scottish Government can provide evidence that it is demonstrating value for money in the use of its resources.

### Independence and objectivity

**24.** Auditors appointed by Audit Scotland must comply with the Code of Audit Practice. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council 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.

**25.** The engagement lead for the NDR account is Stephen Boyle, Assistant Director. Auditing and ethical standards require the appointed auditor Stephen Boyle to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of Scottish Government Non-Domestic Rating Account.

### Quality control

**26.** 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.

**27.** 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 Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews, internal quality reviews and is currently reviewing the arrangements for external quality reviews.

# Scottish Government Non-Domestic Rating Account

## Annual Audit Plan 2016/17

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