

Code of Audit Practice

Audit Dimensions and Smaller Bodies Supplementary guidance

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.

Contents

Introduction	4
Purpose.....	4
General points.....	4
Audit dimensions	4
Planning work on the dimensions	5
Audit dimension prompts	6
Proper arrangements	10
Reporting against the audit dimensions.....	10
Small bodies	12

Introduction

Purpose

1. The 2016 Code of Audit Practice (the Code) refers to supplementary guidance on a number of key areas. This guidance expands upon and clarifies some of these areas and is provided primarily to inform and support auditors carrying out audit work for the Auditor General for Scotland and the Accounts Commission.
2. This guidance is mainly focussed on:
 - supporting auditors to successfully deliver those areas relating to the audit dimensions as laid out in the Code
 - how auditors should make the assessment of what a small body is when using the audit dimensions.
3. Much of the audit work around audit dimension risks and on obtaining assurances will be able to be integrated with the work and assurances required for the financial statements audit.

General points

4. Appointed auditors must comply with the principles and requirements of the Code when planning and reporting their audit work. Audit Scotland will monitor audit outputs to ensure compliance with the Code and relevant guidance as part of the quality assurance work that it undertakes to provide assurances to the Auditor General and the Accounts Commission.

Audit dimensions

5. The most significant change that the 2016 Code brings about is to set out the expectations of appointed auditors on the wider scope of public audit in Scotland.
6. This change is important and in many areas it codifies what was being delivered by a number of appointed auditors during the previous appointment round under the 2011 Code. It clarifies that auditors should make the most of the financial audit work that they carry out and that they express clear conclusions in their reports.
7. The Code frames a significant part of local auditor's wider scope responsibilities in terms of four audit dimensions. These dimensions represent identifiable areas that auditors should consider and report against as part of the annual audit.
8. At the centre of these dimensions is Best Value. The Accounts Commission is developing a new approach to the audit of Best Value in local government. Additional guidance is available in the Best Value audit manual published by the Performance Audit and Best Value (PABV)

team. This manual will support appointed auditors in meeting their responsibilities in providing assurance on local authorities' Best Value arrangements.

Audit dimensions



Planning work on the dimensions

9. The auditor must consider these dimensions when undertaken their annual risk assessment of the audited body and preparing their annual audit plans.
10. The Code states the following on planning the audit:

Paragraph 76

As part of the annual audit planning process, appointed auditors should prepare an annual audit plan that documents how they intend to meet their responsibilities, in the light of their assessment of risks and wider scope responsibilities. These plans should be communicated to those charged with governance.

11. If auditors do not have sufficient evidence or have identified significant risks related to the audit dimensions then they should explain the work that they plan to do in the year. This work should enable them to obtain sufficient evidence to provide judgements and conclusions on the area.
12. If no significant risks are identified to the audit dimensions then annual audit plans should say this. These plans will be reported to those charged with governance and provided to Audit Scotland in line with annual planning guidance timetables.

Audit dimension prompts

13. For each dimension Audit Scotland has prepared a series of key question as examples of what auditors should consider when planning their audit work. These prompts are not exhaustive and may change in response to the shift in focus of the risks facing external audit during the course of an audit appointment. In particular, auditors should consider whether they have sufficient evidence to conclude on the dimensions in their annual audit reports. If not, auditors should plan to do work to obtain sufficient and appropriate evidence to support their conclusions.
14. Local government auditors will also consider work described in the [Best Value Assessment Guidance](#). The dimensions and best value assessment guidance are two ways of looking at a body, and there is considerable overlap. These have been mapped in the auditor BV Assessment Guidance which explain how the dimensions cross over with statutory Best Value characteristics and the BV assurance framework to avoid any unnecessary duplication of work.

Audit dimension prompts

Dimension	Background Key questions	Issues to consider
Financial sustainability	<p>Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.</p> <p><i>Can short-term (current and next year) financial balance be achieved?</i></p> <p><i>Is there a long-term (5-10 years) financial strategy?</i></p> <p><i>Is investment effective?</i></p>	<ul style="list-style-type: none"> • Will (or has) financial balance be achieved? • Have any short-term financial challenges been identified and addressed through a financial recovery plan? • Is a reserves strategy in place? Is the current level of reserves in line with the strategy? • Are any planned deficits able to be met from reserves? Is this sustainable? • How effective are the financial planning systems in identifying and addressing risks to financial sustainability across the shorter and longer terms? • How appropriate are the arrangements put in place to address any identified funding gaps? • Are efficiency targets realistic? • Does the financial strategy meet the requirements specified in Exhibit 3 of Scotland's public finances: a follow-up audit (June 2014), including scenario planning and sensitivity analysis? • Are there any significant concerns with the balance sheet, eg significant liabilities? • Do financial projections include the assets and

Dimension	Background Key questions	Issues to consider
		<p>liabilities and make clear links to capital investment and estates plans?</p> <ul style="list-style-type: none"> • Does the body understand the long-term pressures, including demand pressures, and have these been built into plans and strategies? • Are the long-term revenue consequences of borrowing and other forms of financing on affordability clearly set out? • Are reports showing performance against budget accurate and regularly provided to budget holders? • Can the body demonstrate that these arrangements are working? • Can the body demonstrate the affordability and effectiveness of funding and investment decisions it has made? • Are investment decisions informed by clear business cases? • Is it clear how investments will be funded and is there a clear link to financial plans and strategies? • Are the benefits of investment clearly articulated at the outset and is success measured? • Is there a clear long-term capital investment programme in place?
Financial management	<p>Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.</p> <p><i>Is financial management effective?</i></p> <p><i>Are the budget setting</i></p>	<ul style="list-style-type: none"> • Does the body have arrangements to ensure systems of internal control are operating effectively? • Can the body demonstrate the effectiveness of the budgetary control system in communicating accurate and timely financial performance? • Is it clear why budgets have changed during the year, including how income and expenditure have changed since the budget was set at the beginning of the year? • Is public money applied in accordance with

Dimension	Background Key questions	Issues to consider
	<p><i>and monitoring processes operating effectively?</i></p> <p><i>Is there sufficient financial capacity?</i></p>	<p>appropriate standards of conduct and financial rules?</p> <ul style="list-style-type: none"> • Are standing financial regulations comprehensive, current and promoted within the body? • Is financial forecasting an embedded part of financial management and reporting arrangements? • How accurate is financial forecasting? • Is an appropriate approach taken to budget setting, eg priority-based? • Are reports showing performance against budget accurate and regularly provided to budget holders? • Are there suitably qualified and experienced officials leading the body's finance team? • Is there sufficient financial skills, capacity and capability in the body? • Are there appropriate and effective arrangements for the prevention and detection of fraud and corruption?
<p>Governance and transparency</p>	<p>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.</p> <p><i>Is governance effective?</i></p> <p><i>Is there effective leadership?</i></p> <p><i>Is decision making transparent?</i></p>	<ul style="list-style-type: none"> • Can the body demonstrate that the governance arrangements are appropriate and operating effectively (including services delivered by, or in partnership with, others such as ALEOs, subsidiaries and associates)? • Is there effective scrutiny, challenge and transparency on decision making and financial and performance reports? • Is the quality and timeliness of financial and performance reporting appropriate for the needs of users? • Do finance and performance reports support effective scrutiny and challenge? • Is the governance framework sound? • Are the governance arrangements effective? • Is the internal audit function sound and can it be relied upon? • Is the Governance Assurance Statement

Dimension	Background Key questions	Issues to consider
	<p><i>Is there transparent reporting of financial and performance information?</i></p>	<p>complete and does it reflect key findings from audit, scrutiny and inspection?</p> <ul style="list-style-type: none"> • Is appropriate and effective leadership in place? • Is there sufficient and effective scrutiny and challenge (political and board level)? • Is there a positive culture? • Do decision makers have the information they need to make robust decisions that meet Best Value? • Is it clear what decisions have been made, who made them and the rationale they had? • Is there a clear link between financial information reported in the year and the annual accounts? • Do performance reports contain clear objectives, targets, benchmarks and comparisons? • Is there a flow from corporate plans to performance reports? • Are the public performance reporting arrangements effective? • Is the quality of reporting improving?
Value for money	<p>Value for money is concerned with using resources effectively and continually improving services.</p> <p><i>Are resources being used effectively?</i></p> <p><i>Are services improving?</i></p> <p><i>Is Best Value demonstrated?</i></p>	<ul style="list-style-type: none"> • Can the body provide evidence that it is demonstrating value for money in the use of resources? • Can the body demonstrate that there is a clear link between money spent and outputs and the outcomes delivered? • Are outcomes improving? • Is there sufficient focus on improvement? • Is the pace of improvement appropriate to the risk and challenges facing the body? • How much money is spent? • Is management cost and performance information used effectively? Are inter-relationships between the two clear? • Are cost drivers known?

Dimension	Background Key questions	Issues to consider
		<ul style="list-style-type: none"> • Is it clear how planned savings or cost-reduction might affect quality? • Are savings plans risk assessed and are they regularly monitored to ensure savings are being delivered? • Have alternative models of service of delivery been considered? Where they are in place, are they having a positive impact on services? • Is benchmarking carried out to identify areas for improvement? • Are user needs and views considered in the evaluation of service delivery and quality? • Are equalities issues adequately addressed?

15. The *Local Government Audit Manual - Auditing Best Value* (available on the [extranet](#)) supplementary guidance is designed to support the Local Government Best Value work but may also be referred to where appropriate by auditors of other sectors.

Proper arrangements

16. The work that auditors do on the audit dimensions should be based on the understanding that it is the audited body's responsibility to ensure that they have proper arrangements in place.
17. It is these 'proper arrangements' that appointed auditors are reviewing and coming to a conclusion on when discharging their wider scope responsibilities. These arrangements should be appropriate and proportionate to the nature of the public body and the services and functions that it has been created to deliver.
18. Where arrangements are not effective or are absent auditors should make appropriate comment and recommendations for improvement in their annual audit report.
19. Where an auditor finds that the arrangements are generally effective and operating as expected then auditors should report this in their annual audit report.

Reporting against the audit dimensions

20. The Code states the following in terms of annual auditor reporting on the audit dimensions:

Paragraph 71

All annual audit reports should include a summary on each dimension that states any work done in the year by the appointed auditor and the assurances, risks and any good practice

that they have identified. A simple description of the arrangements in place is not sufficient. Appointed auditors should provide clear judgements and conclusions on the effectiveness and appropriateness of the arrangements in place based on any work that they have done. If there are still significant risks, appointed auditors should make recommendations for improvement.

Paragraph 99

These conclusions should provide clear narrative that explains to the reader what the appointed auditor found in respect of the effectiveness and appropriateness of the arrangements that audited bodies have in place regarding the four audit dimensions, including best value characteristics where applicable. Simply describing the arrangements that are in place at an audited body would not meet this responsibility.

21. Annual audit reports should include:
 - a summary of the audit work undertaken in the year in response to identified risks to obtain assurances over the relevant arrangements in place for the audit dimensions
 - a conclusion on the effectiveness and appropriateness of these arrangements
 - any significant risks that were identified
 - recommendations for improvement to mitigate any identified risks.
22. Readers of annual audit reports should be left with a clear understanding of what the auditor's conclusions are on the effectiveness and the appropriateness of the arrangements that the audited body has in place under the audit dimensions.
23. Appointed auditors must apply their professional judgement and professional scepticism in this area to the body that they are auditing. The examples contained within this guidance on the audit dimensions are not an exhaustive list but should be considered in the context of the body and services that it delivers.
24. It is for auditors to assess the evidence required to support their conclusions on the audit dimensions. Auditors may choose to include conclusions or views expressed by other bodies such as internal audit, regulators, scrutiny bodies, national performance audit reports or Best Value assurance reports. Auditors are not required to re-perform such work of others when reporting against the audit dimensions unless they have reason to believe that the work of the other body is not sufficiently robust for the purpose to which it is being put.

Small bodies

25. The Code requires auditors to judge when they conclude that the full application of the wider scope is not appropriate based on the risks, nature and size of an audited body:
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Paragraph 53

The planned audit work should, however, be risk based and proportionate to the nature and size of an audited body. Where the application of the full wider scope is judged by auditors not to be appropriate to an audited body then annual audit work on the wider scope should be undertaken that enables conclusions to be made on the:

- appropriateness of the disclosures in the governance statement
- financial sustainability of the body and the services that it delivers over the medium to longer term.

Paragraph 55

If, in the case of such a small body, an appointed auditor identifies that there is particular risk or public interest in a wider scope issue beyond these areas then the auditor must contact Audit Scotland to discuss the issue and agree an appropriate response.

26. For the majority of audits undertaken by appointed auditors for the Auditor General and the Accounts Commission the full wider scope audit should be delivered.
27. This section of the Code recognises that for some very small audited bodies, in terms of the volume or complexity of financial transactions, it is not likely to be appropriate or proportionate to apply the full wider scope audit. Such bodies are likely to include:
- local government charities, some joint boards and committees
 - small special health boards
 - small further education colleges
 - small central government bodies such as Quality Meat Scotland and commissioner bodies.
28. As a minimum the Code requires annual audit work on governance disclosures and financial sustainability for all audits. These tie in with the work to be undertaken as part of the financial accounts audit around governance disclosures and represent a slight extension of the auditor's opinion on the appropriateness of going concern assumption beyond the 12 to 18 months period. As part of the annual audit, auditors must review and conclude on whether the audited body has arrangements that demonstrate that it has planned effectively over the longer term to continue to deliver its services or the way in which they should be delivered.
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29. Auditors must document when, in their opinion, the small body clause applies to an audit. The auditor must also document the reasoning to support this conclusion. It would be appropriate to reference size and simplicity of the functions delivered by the audited body. However, it should be recognised that where the public interest in a body is high it is unlikely that the small body provision will be supportable. If there is any doubt auditors should discuss their provisional judgement with Audit Strategy staff.
30. The annual audit plan must clearly state that the body is being audited under the small body provisions of the Code to ensure that those charged with governance clearly understand the scope of audit work that is planned.
31. This judgement must be made annually to recognise that the risks to wider scope dimensions can shift in relation to any audited bodies.
32. Where the auditor has identified a particular issue or risk in a small audited body during the audit year that requires additional work or the full wider scope to be applied then the auditor should contact Audit Strategy to discuss the issue and agree an appropriate response and, if necessary, funding.