Technical bulletin 2015/1

January to March

AUDIT SCOTLAND

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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.

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Foreword

Technical bulletins are prepared by Audit Scotland's Technical Services Unit (TSU), and approved by the Assistant Auditor General, to provide external auditors appointed by the Accounts Commission and Auditor General for Scotland with

- information on the main public sector technical developments in the quarter that are relevant to their audit appointment
- guidance from the TSU on any emerging risks identified in the quarter.

Technical bulletins are available to external auditors from Audit Scotland's *Technical reference library,* and published on the Audit Scotland website so that audited bodies and other stakeholders can access them.

It is important that auditors read this technical bulletin promptly so they are familiar with the information and guidance provided. The auditor action checklist section at the end of each chapter should be completed by a senior member of the audit team.

The articles on technical developments are intended to highlight the key points that the TSU considers external auditors require to be aware of. It may still be necessary for auditors to read the source material where greater detail is required. The documents referred to in the articles can be obtained by using the hyperlinks, where available. They are also available to external auditors from Audit Scotland's *Technical reference library*.

While auditors act independently, and are responsible for their own conclusions and opinions, the TSU has a role in ensuring that those conclusions and opinions are reached on the basis of informed judgement. Consistency in similar circumstances is important and **Audit Scotland's *Code of audit practice* therefore states that auditors should normally follow TSU guidance.** Auditors should advise the TSU promptly if they intend not to follow guidance provided in this technical bulletin on an emerging risk.

The TSU encourages feedback on this technical bulletin. Comments should be sent to pobrien@audit-scotland.gov.uk.

More in-depth and extensive guidance is provided in separate technical guidance notes published by the TSU. Technical guidance notes published in the quarter are referred to in this technical bulletin, and can be obtained by using the hyperlinks to the Audit Scotland website.

Headlines

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Local authority chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to the local authority sector.

It should be read by external auditors with appointments in the local authority sector. Auditors should also read the cross-sectoral chapter.

Guidance from the TSU on emerging risks

HRA recharges

1. The TSU has received a number of enquiries from auditors regarding recharges from the general fund to the housing revenue account (HRA). Auditors are reminded of technical bulletin 2014/1 (paragraph 94) which made reference to Guidance on the operation of local authority HRAs in Scotland issued by the Scottish Government.

2. The guidance identifies a number of key HRA operating principles including the need for a robust, written methodology for calculating and allocating costs to the HRA. The methodology should be in sufficient detail for tenants to understand why costs are being charged and who is benefiting from the services they relate to. This includes the allocation to the HRA of the appropriate proportion of trading operation surpluses attributable to council housing activities.

3. Auditors should refer to the Scottish Government guidance when considering a council's methodology for making recharges to the HRA.

Application of the accounts regulations to section 106 bodies

4. Technical bulletin 2014/3 (paragraph 21) advised auditors that The Local Authority Accounts (Scotland) Regulations 2014 have been issued and provided a summary of the main provisions that apply from 2014/15. The article advised that the accounts regulations apply to all bodies covered by section 106 of the *Local Government (Scotland) Act 1973*. The TSU has received a number of enquiries regarding how the regulations apply to these bodies in practice.

5. Section 106 states that the accounts regulations apply to joint committees, joint boards and regional transport partnerships in the same way as they do to a council, subject to any necessary modifications. Auditors should confirm that each body has considered the modifications that are necessary in their context, and have arrangements in place to comply with the regulations. This includes, for example, ensuring appropriate signatories to the accounts are identified and nominated, and that internal audit arrangements have been considered.

6. The accounts regulations also apply to local government pension scheme (LGPS) pension funds as statutory guidance requires that pension fund financial statements within the annual report should be considered an additional abstract of accounts which councils are required to prepare under section 96 of the 1973 Act.

7. Although the accounts regulations also apply to the trustees for any charity covered by section 106, Regulation 12 disapplies most of the provisions other than the inspection process for the accounts.

Audit of 2014/15 charity accounts

8. Auditors will be aware that the TSU agreed with the Office of the Scottish Charity Regulator (OSCR) that an auditor's report was not required for 2013/14 statement of accounts where an application to wind up a charity had been submitted prior to 31 March 2014 (even if the charity remained on the charity register as at that date).

9. The TSU has been in discussions with OSCR over extending that arrangement to 2014/15. OSCR has agreed that an auditor's report is also not required for the 2014/15 statement of accounts for those charities where the application was submitted prior to 31 March 2014.

10. Where a charity is wound up (and hence removed from the charity register) during 2014/15, but the application was not made before 31 March 2014, the charity regulations require the submission of the statement of account to OSCR within 9 months of the date of removal. An auditor's report is required on these accounts as the transitional provisions allowed for 2013/14 do not apply. The financial year covered by the accounts would be the period from 1 April 2014 to the day on which the charity is removed from the register.

11. Auditors should
    - identify which charities were removed from the register since 1 April 2014
    - establish when the application for removal was submitted
    - where the application for removal was after 1 April 2014, audit the 2014/15 accounts for the appropriate period and provide an auditor's report to a timescale that allows the submission of the accounts and auditor's report within nine months of the date of removal.

Other emerging risks

12. This chapter of the technical bulletin also provides guidance from the TSU on the following emerging risks
    - agency disclosures for pension fund accounts (see paragraph 63)
    - reports to audit committees on integration joint boards (see paragraph 88).

Accounting developments

Property, plant and equipment

Updated guidance on accounting for components

13. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued updated guidance on identifying and accounting for asset components. LAAP bulletin 86 (update) Componentisation of property, plant and equipment under the IFRS-based code addresses the requirements of the *Code of practice on local authority accounting in the UK* (the Code) that

- each component of an item of property plant and equipment (PPE) with a cost that is significant in relation to the total cost of the item should be depreciated separately
- where a component is replaced, the carrying amount of the old component should be derecognised to avoid double counting and the new component reflected in the carrying amount. Such recognition and derecognition takes place regardless of whether the replaced part has been depreciated separately.

14. The bulletin explains that components of PPE have different useful lives, may wear out at different rates or have different risks of impairment or obsolescence. It is therefore necessary to depreciate each significant component separately over its useful life in order that the comprehensive income and expenditure statement is fairly charged with the consumption of economic benefits of those assets.

15. It is essential that the principles for component accounting are established together with agreed and documented procedures which will facilitate this process. This should enable authorities to

- identify significant components of their PPE
- establish the value of such components and determine an appropriate depreciation charge which reflects the consumption of the economic benefit of the component.

16. The procedures should be communicated to all relevant staff and include a requirement to document assumptions and the basis on which estimates are made.

17. The stages set out in the bulletin for establishing procedures for component accounting are

- establish appropriate de-minimis thresholds for items of PPE that can be disregarded. Once established, the threshold should be documented, used appropriately and applied consistently.
- assess the materiality of items of PPE. This involves carrying out a review of the authority's PPE to identify those that are above the de-minimis level and therefore require consideration of whether they contain significant components.
- set the principles to be used to determine which components of PPE above the de-minimis are significant. The principles need to specify the basis on which it will be determined whether the cost of a component is significant in relation to the overall asset.

They are likely to refer to the cost of the component as a proportion of the overall cost of the asset (including the new component) rather than an absolute amount. This bulletin has been updated to highlight that it is essential that the assessments are made as at the same date. This may mean

  – estimating the current-day build cost of the asset and comparing the cost of the new component against that cost; or
  – discounting back the cost of the new component to the date when the asset was initially recognised and comparing that adjusted cost against the original cost of the asset.

- attribute values of items of PPE to significant components. When an asset is separated into different components, authorities will need to consider whether the revaluation reserve balance for the asset should be allocated across the various components.

18. Auditors should refer to this guidance when considering whether authorities have identified and properly accounted for significant asset components.

Service expenditure analysis

Guidance on community safety expenditure

19. The Local Authority (Scotland) Accounts Advisory Committee has issued guidance on accounting for community safety expenditure and income from 2014/15. Guidance on the classification of community safety expenditure explains that local authorities provide a wide range of community safety services including

- crime reduction, e.g. fees paid to police forces to secure extra police officers for a particular area or providing crime prevention advice
- community based CCTV cameras, i.e. those that do not fall within the definition of a specific service (e.g. cameras at a school should fall within the education service rather than community safety)
- safety services, e.g. provision of safety railing.

20. From 2014/15, the guidance recommends that expenditure on community safety is to be classified within the service expenditure analysis as general fund housing (within the private sector housing renewal sub division).

21. Restatement of 2013/14 comparatives will be required where there is a material change in the classification of community safety expenditure and income.

22. This change in treatment excludes community safety expenditure that

- specifically benefits, and is to be funded by, HRA tenants
- falls within the definition of any other specific service classification
- impacts on the amount of expenditure or income previously recorded for trading standards or environmental health. This is to avoid it affecting grant aided expenditure

used to distribute government grant. Authorities are instead required to submit details of the impact to LASAAC and, if material, disclose it in their financial statements.

23. Auditors should refer to this guidance when considering whether authorities have properly accounted for community safety expenditure and income from 2014/15.

Group financial statements

Guidance on accounting for collaborations

24. CIPFA has issued guidance called *Accounting for collaboration in local government* which is intended to help local authorities review their collaborative arrangements and account appropriately for them in accordance with the new group accounting standards from 2014/15.

25. Collaborative arrangements take many forms and involve various parties, including other public bodies, voluntary organisations and commercial entities. The guidance examines the accounting consequences of collaborations in local government. Auditors should refer to this guidance when considering whether authorities have properly accounted for their collaborative arrangements.

26. The five main accounting outcomes that might arise from collaborative arrangements are as follows

- Preparation of group accounts including the relevant transactions and balances from an authority's interest in other entities in accordance with the adoption of the relevant standards by the 2014/15 Code. This is the case where the other entity meets the definition of a subsidiary, associate or joint venture.
- Inclusion of transactions and balances relating to the arrangements in the authority's single-entity financial statements. This is the case where the arrangements meet the definition of a joint operation or recognition is required under other accounting standards.
- Recognition of an investment in the authority's single-entity balance sheet. This is the case where the arrangements are a financial instrument for the authority.
- Accounting for particular transactions with another party. This is the case where the relationship is with an independent other party, e.g. service provider.
- No recognition is required as the arrangements do not involve the authority entering into any transactions or acquiring any rights that need to be accounted for.

27. Determining which outcome applies to a particular arrangement is sometimes straightforward, e.g. where an authority holds 100% of the shares in a company. In more complex circumstances, the arrangements may not involve a separate legal entity over which the authority's control/influence can be assessed and the determination might involve judgements about contractual terms.

28. The guidance provides a useful chart at paragraph 3.8 which illustrates a process for separating out these different considerations.

Entities

29. Although it is a key element of the definition of a subsidiary, international financial reporting standards (IFRS) do not define precisely what is meant by the term 'entity'. The guidance offers the view that an entity would need to be capable of being treated legally like a person. However this is based on FRS 9 and is, in the TSU's view, inconsistent with the definition of entity in paragraph 9.1.2.25 of the Code which makes clear that use of the term is not limited to organisations that are corporate bodies in legal terms. Paragraph 397 of note for guidance 2014/11(LA) sets out the TSU's view that any committee or body to which section 106 of the 1973 Act applies should be considered an entity in this context.

30. The concept of structured entities can be relevant to any collaborative arrangement that operates through a separate entity. These entities are given prominence in the group accounts standards because of concerns that lack of information about off-balance sheet activities was a contributory factor to the global financial crisis. Consequently, focus is placed on arrangements where there is exposure to risk because an organisation has sought to secure control or influence over an entity through contractual arrangements while foregoing the traditional tool of voting power.

31. Structured entities are not subject to any special accounting treatment. However, the risk arising from an involvement in structured entities has been addressed by a requirement for specific disclosures for structured entities.

Materiality

32. Having identified that the authority is the parent of a group for the purposes of the Code or needs to account for collaborative arrangements, the next consideration is whether the relevant modifications to the financial statements would make a material difference to their usefulness for users.

33. Paragraph 9.1.1.6 of the Code states that authorities with interests in subsidiaries, associates and/or joint ventures should prepare group accounts in addition to their single entity financial statements, unless their interest is not considered material. The Code discussion on materiality at paragraph 2.1.2.9 makes the following points

- The focus of materiality is on the potential effect on the decisions or assessments of users of the accounts. Consideration of materiality therefore needs to take into account users and their interests.
- Potential omissions need to be considered collectively as well as individually. It may be that none of the interests that an authority has in other entities are material individually, but cumulatively they are material.
- It is not only the size of an item that is important, but also its nature. Qualitative factors can be as significant as quantitative factors.

34. Authorities should start from a presumption that the Code’s provisions should be followed, until it can be established that a different approach does not risk a misreading of the

authority's overall financial position or performance that might be significant to users of the accounts.

35. The process that should be undertaken in assessing materiality is as follows

- An initial assessment of qualitative factors should be made to determine whether group accounts should be prepared, irrespective of the quantitative impact that consolidation might have on the authority's results and financial position. Authorities will need to consider the circumstances that surround their involvement in companies and other group entities and collaborative arrangements. For example, an authority will need to consider whether it depends significantly on these entities for the continued provision of its statutory services.
- If there are no definitive qualitative factors, authorities should consider quantitative matters and assess the likely impact of consolidation.
- If the quantitative assessment does not confirm absolutely that group accounts would be immaterial, authorities should revisit the qualitative factors to make sure that there are none that would decisively tip the balance of opinion away from producing group accounts.

Control

36. Paragraph 8.2 of the guidance provides a useful diagram which lists the factors to be considered when determining control.

Group accounts

37. The Code sets out the accounting treatment for group accounts and details the presentation and disclosure requirements.

38. Where group accounts are required, authorities are required to prepare accounts for the authority and for the group. However, these two separate sets of accounts can be presented alongside each other in a columnar approach. The guidance recommends side-by-side presentation of the financial statements, as it allows clearer comparison of the authority-only and the group financial results.

39. Chapter 13 contains two worked examples, one for line by line consolidation of a subsidiary and one on equity accounting for an associate.

Non-group arrangements

40. The chart at paragraph 15.6 of the guidance shows how to categorise arrangements that do not fall into subsidiaries, associates or joint arrangements. For example it considers whether

- there are contractual arrangements to support the collaborative activity (if not, there are no accounting implications)
- the contractual arrangements take the form of a financial instrument, and therefore should be accounted for as such

- the contractual arrangements give the authority rights or obligations that require to be recognised.

41. Even where there are no accounting implications, there may still be a requirement for disclosures where the arrangement is a structured entity.

Guidance on transition to new standards

42. CIPFA has issued guidance on the transition to the new group accounting standards in 2014/15 in LAAP bulletin 102 Accounting for collaboration-transition issues. The bulletin highlights that the revised definition of control in *IFRS 10 Consolidated financial statements* may result in new entities being brought within the scope of group accounts. As this would be the result of a change in accounting policy, this would normally require a full retrospective restatement.

43. Paragraph 9.1.2.66 of the Code sets out the steps to be taken for an entity that is to be consolidated that was not previously treated as a subsidiary. This involves measuring the assets, liabilities and minority interests in the entity on 1 April 2014 as if it had been consolidated from the date when the authority obtained control under the Code's requirements for IFRS 10

44. The Code however contains concessions that recognise practicable difficulties in potentially going back many years to calculate the prior period restatements. The concessions are based on restatements not being required where they are impracticable (i.e. an authority is unable to apply a requirement after making every reasonable effort to do so).

45. Paragraph 9.1.2.67 of the Code states that if measuring a subsidiary's assets, liabilities and minority interests is impracticable, an authority should use the beginning of the earliest period for which application is practicable as a deemed acquisition date. This means going back to the date when all of the following apply

    - Information is available to allow the effects of retrospective application to be determined and measured reliably, without having to make unreasonable efforts to obtain that information.
    - There is no requirement in preparing figures to make assumptions about what management's intent was at the time.
    - it is possible when making significant estimates to separate out (without introducing subjective judgements) the information that provides evidence of circumstances that existed on the date that amounts are to be recognised and would have been available when the financial statements for that year were authorised for issue.

46. The bulletin also provides guidance on

    - entities that would have been subsidiaries under the IFRS 10 test but control was lost before 1 April 2014
    - the steps to be taken for an entity that was consolidated in the group accounts prior to 2014/15 but does not meet the new definition of a subsidiary

- moving from proportionate consolidation to equity accounting for jointly controlled entities
- adjustments needed where a jointly controlled entity becomes a joint operation so that the arrangement is no longer accounted for using the equity method

47. The bulletin also highlights that the only specific concession in relation to the Code's adoption of the requirements of *IFRS 12 Disclosure of interests in other entities* allows the new disclosures in relation to unconsolidated structured entities to be restricted to 2014/15 (i.e. no comparatives required for 2013/14).

48. Auditors should refer to this guidance when auditing the group financial statements in the 2014/15 annual accounts.

Remuneration reports

Amended regulations on elected members

49. The principal 2007 regulations that provide for the remuneration of elected members have been updated with effect from 1 April 2015.

50. The Local Governance (Scotland) Act 2004 (Remuneration and Severance Payments) Amendment Regulations 2015 (SSI 7) substitute increased annual amounts for different categories of remuneration to members.

Pension funds

Note for guidance on auditing 2014/15 local authority pension fund annual accounts

51. The TSU has published Note for guidance 2014/13(LA) Audit of 2014/15 local authority annual accounts (pension funds) to provide auditors with guidance on planning and performing the audit of the 2014/15 LGPS pension fund annual accounts.

52. The note for guidance provides guidance on the areas that the TSU considers represent a generic risk of material misstatement in the 2014/15 financial statements to inform auditors' own risk assessments. The note also provides guidance on auditors' responsibilities to

    - audit and express an opinion on elements of the remuneration report
    - express an opinion on the consistency of the management commentary with the financial statements
    - report on other matters such as the annual governance statement.

53. Auditors should use this note for guidance when planning and performing the audit of the 2014/15 LGPS annual accounts.

2014/15 example accounts and disclosure checklist

54. CIPFA has published guidance that illustrates the 2014/15 financial statements of LGPS pension funds. The publication also includes a disclosure checklist that identifies the Code's requirements in relation to pension funds. The 2014/15 *Local government pension scheme*

example accounts and disclosure checklist provides an example set of accounts that meet the minimum requirements of the Code.

55. It sets out a fund account and a net assets statement as well as information to be disclosed in the notes. Some key information required to be disclosed in the notes are discussed in the following paragraphs. Auditors should refer to this publication when auditing the 2014/15 LGPS pension fund financial statements.

56. The note on critical judgements in applying accounting policies (as required by Code paragraph 3.4.2.81) highlights the highly subjective nature of determining the fair value of private equity investments. It also explains the calculation of the pension fund liability and the fact that the estimate is subject to significant variances based on changes to the underlying assumptions.

57. The note on assumptions about the future and other sources of estimation uncertainty (as required by Code paragraphs 3.4.2.83 and 3.4.2.84) considers the items in the net assets statement for which there is a significant risk of material adjustment in the forthcoming year e.g. actuarial present value of promised retirement benefits, private equity and hedge funds.

58. The note of events after the reporting date (as required by Code paragraph 3.8.4.1) gives as an example of a non-adjusting event the marked decline in the global stock markets which would impact on the market value of the fund's investments were they to be valued as at the date the accounts were authorised for issue.

59. As a change from the previous edition, the note on management expenses follows the CIPFA guidance *Accounting for local government pension scheme management costs* (see technical bulletin 2014/3 - paragraph 95) and analyses the costs of managing the fund between administrative costs, investment management expenses, and oversight and governance costs. It also separately discloses performance related fees and transaction costs.

60. The note on the nature and extent of risks arising from financial instruments (as required by Code paragraphs 7.4.3.1 to 7.4.3.10) provides illustrative wording for explaining market risk, credit risk and liquidity risk.

61. The note on related party transactions (as required by Code paragraph 6.5.5.1r) describes the relationship between the administering council and the pension fund, including the costs incurred and reimbursed in administering the fund and the amount paid as contributions. It also gives details of the members of the pension fund committee who are in receipt of pension benefits, and the employees of the administering council who hold key positions in the financial management of the fund.

62. The note on related party transactions follows Code paragraph 3.9.4.3 by stating that the disclosure requirements for key management personnel are satisfied by the disclosures for officer remuneration. However, as explained at paragraph 190 of note for guidance 2014/13(LA), this is based on the assumption that there are such disclosures in the same financial statements. The inclusion of a remuneration report in the authority's own financial statements does not satisfy the disclosure requirements for key management personnel in the pension fund financial statements.

TSU guidance on agency disclosures

63. Subsequent to the publication of the 2014/15 example accounts referred to at paragraph 54 (and note for guidance 2014/13[LA]), the TSU has been in discussion with CIPFA regarding the requirement to disclose an agency arrangement in respect of administering payments for 'added years'.

64. LGPS pension funds often administer added years payments as agents of employing authorities in respect of staff who have had their pension augmented under *The Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998*. Paragraph 3.4.4.1 of the Code requires authorities to disclose the nature and amount of any significant agency income or expenditure.

65. Although this disclosure is not included in the 2014/15 example accounts, CIPFA has indicated agreement with the TSU's views that disclosure of the agency arrangement for added years is required in 2014/15, and that the 2015/16 example accounts will be amended. It is the income and expenditure associated with running the payrolls that is relevant for disclosure purposes, rather than the payroll cash flows themselves.

66. Auditors should confirm that the 2014/15 LGPS pension fund financial statements disclose the agency arrangement in respect of administering payments for 'added years'.

Establishment of pension boards

67. Regulations have been made which provide for the establishment of a pension board from 1 April 2015 for each authority that administers the LGPS. The Local Government Pension Scheme (Governance) (Scotland) Regulations 2015 (SI 60) make each pension board responsible for assisting the administering authority secure compliance with

- *The Local Government Pension Scheme (Scotland) Regulations 2014* (as explained in technical bulletin 2014/2 - paragraph 198) and other legislation relating to the governance and administration of the LGPS
- requirements imposed in relation to the LGPS by the Pensions Regulator.

68. A pension board is required to comprise four representatives appointed by scheme employers and four by relevant trade unions. The board may consider any matter concerning pensions it deems relevant to the activities of the relevant fund including

- any reports produced for the pension committee
- fund performance and administration
- actuarial reports and valuations
- funding strategy.

Auditing developments

69. The Accounts Commission has issued a report based on the findings from local government audit work during 2014, including the audit of the annual accounts. An overview of local government in Scotland 2015 was prepared by Audit Scotland and provides elected members with an independent view on how councils are managed and perform.

70. For example, the report highlights that councils had a total of £1.8 billion of useable reserves at 31 March 2014, which represents a decrease of 2% in 2013/14. General fund balances accounted for over half of this amount. Councils allocated most of their general fund balances (69%) for specific purposes, such as modernisation initiatives and local development projects. The remainder was unallocated and held as a contingency to help deal with unforeseen events such as rising interest rates, relieving the pressure on demand-led services, or other unplanned spending.

71. Councils need to consider both their level of reserves, and how they plan to use them, when developing financial plans and setting annual budgets. The proper officer is responsible for advising the council on the level of reserves it should hold and ensuring that there are clear procedures for keeping and using reserves. Auditors reported, however, that not all councils carried out a formal risk analysis to determine the appropriate level of reserves. Most councils had a policy to maintain unallocated general fund reserves at around 2 to 4% of their net spending on services.

Other developments

Housing benefits

2014/15 subsidy claims

72. The Department for Work and Pensions (DWP) has issued *Notes on completion of form MPF720B - final subsidy claim 2014/15* and a letter relating to the completion of the housing benefit subsidy claim for 2014/15.

73. The deadlines for receipt of the

- pre-certified claim to the DWP and external auditors is 30 April 2015
- the certified claim by the DWP is 30 November 2015.

2014/15 HB COUNT modules

74. The Audit Commission has issued the following modules of the 2014/15 HB COUNT approach

- Module 2 contains a checklist to help auditors ensure that the authority's system is using the correct benefit parameters to calculate benefit entitlement and for the authority to claim the correct amount of subsidy.
- Module 3 comprises workbooks to be completed for detailed testing, incorporating step-by-step guidance and a test result summary.

75. Module 1 has also been issued and provides an overview of the approach, but this is superseded in Scotland by guidance from the TSU.

76. For 2014/15, the key changes to HB COUNT are to reflect DWP changes to the regulations and subsidy order. The most significant of these are

- from 3 March 2014 the removal of the spare room subsidy (RSRS) applies to pre 1 January 1996 cases
- clarification of benefit cap exemptions for managed properties, refuges and hostels.

77. The Audit Commission has also developed an e-learning package setting out the principles of the HB COUNT approach to the certification of HB subsidy claims for 2014/15.

Removal of the spare room subsidy

78. The DWP has issued HB urgent bulletin U6/2014 Upper tribunal decisions CSH/41/14 and CSH/42/14 to provide details of decisions made by the Upper Tribunal relating to the determination as to whether a room is a bedroom for the purposes of the removal of the RSRS policy.

79. The Upper Tribunal found that the space standards set out in the *Housing (Scotland) Act 1987* are not determinative as to whether a room is a bedroom for the purposes of the RSRS policy in the social rented sector. The starting point for the determination is the landlord's description of the property. Local authorities should consider factors such as the size, configuration and overall dimensions of the room, as well as access, lighting, ventilation and privacy.

80. Rooms capable of being a bedroom should be classed as such, regardless of what it is actually being used for by the tenant.

Guidance for NFI HB matches

81. The DWP issued a letter regarding the *National fraud initiative's* (NFI) housing benefit data matches in order to provide guidance to those authorities that have transferred responsibility for fraud investigations to the DWP.

82. All NFI housing benefit data matches will continue to be released to the relevant local authority. Authorities are then required to carry out an initial sift of the data matches to identify those which show potential fraudulent activity and refer them to the DWP.

Miscellaneous

83. The DWP has issued the following circulars

- HB circular A18/2014 Housing benefit: Uprating 2015/16 and HB circular A2/2015 War pensions: uprating 2015/16 to advise of the benefits rates from April 2015.
- HB circular A4/2015 Pension flexibilities to advise how greater flexibility introduced to the pension system from 6 April 2015 will impact on housing benefit claims.

- HB circular S11/2014 New burdens payment for real time information bulk data matching initiative to announce funding to meet the costs of the *Real time information* bulk data matching initiative.
- HB circular S1/2015 Discretionary housing payments government contribution for 2015/16 confirming UK government funding for discretionary housing payments (DHPs) in 2015/16. There are no limits on DHP overall expenditure for Scottish local authorities.

84. The Housing Benefit &Housing Benefit (Persons who have attained the qualifying age for state pension credit)(Income from earnings)(Amendment) Regulations 2015 (SI 6) have been issued to clarify how local authorities should calculate housing benefit claimants' income.

Integration joint boards

Guidance for integration financial assurance

85. The Scottish Government has issued guidance on providing financial assurance for health and social care integration. Guidance for integration financial assurance states that the assurance process should enable the integration authority (integration joint board [IJB] or lead agency) and the delegating local authority (and health board) to identify the resources to be delegated and the risks associated with the integrated functions.

86. The process should be proportionate to the potential risks involved and cover the whole transition period. It should be possible for partners to avoid some of the document reviews involved in a formal process of financial assurance by placing reliance on assurances from each other.

87. IJBs will not be able to formally participate in the financial assurance process until they are established during 2015/16. It is recommended that until then

- the shadow chief officer and chief financial officer should work with the local authority (and health board) in carrying out the assurance work
- the shadow IJB should receive regular reports on the assurance work.

88. The guidance also recommends that the local authority (and health board) internal auditors should provide reports on the assurance process to the respective audit committees. In the TSU's view, the reports provided to the audit committee should be considered in the preparation of the 2014/15 governance statement. Where assurance reports have not been provided to the audit committee, this should be considered for inclusion within the governance statement. Auditors should confirm that is the case when reading the information in the 2014/15 governance statement.

89. The initial sums delegated to the IJB should be based on existing budgets, actual spend and the financial plans for delegated services. The budget should be assessed against the actual expenditure over the previous two to three year period and should include non-recurring funding and expenditure and savings and efficiency targets. Partners may find it helpful to treat the first year as a transitional year and agree to a risk sharing arrangement with allocations being adjusted in subsequent years.

90. There should be a post integration review undertaken by the respective audit committees and the results shared with the Scottish Government.

Integration scheme regulations

91. Integration schemes are required by the *Public Bodies (Joint Working)(Scotland) Act 2014* to set out for each local authority area the agreed arrangements for joint working. The following regulations have been issued in respect of integration schemes

- The Public Bodies (Joint Working) (Scotland) Act 2014 (Prescribed Local Authority Functions, etc) (Scotland) Regulations 2014 (SSI 345) sets out the prescribed functions to be delegated through an integration scheme. The functions can generally be described as adult social care services.
- The Public Bodies (Joint Working) (Integration Scheme)(Scotland) Regulations 2014 (SSI 341) prescribe the information to be included in an integration scheme. They require the information to include
  - governance arrangements, including the number of members and arrangements for the appointment of the chairperson
  - arrangements for the preparation of a strategic plan and overseeing operational delivery of integration functions
  - the process and timescale for the preparation of performance targets and improvement measures, and the reporting arrangements
  - the process to agree and amend payments to the integration authority and to deal with variances in spending on integration functions
  - the risk management strategy, arrangements for information sharing, dispute resolution and complaints handling.

92. Local authorities are required to have regard to the national health and wellbeing outcomes prescribed by The Public Bodies (Joint Working) (Scotland) Act 2014 (National Health and Wellbeing Outcomes) (Scotland) Regulations 2014 (SSI 343) when preparing the integration scheme.

Finance

Changes to council tax reduction scheme

93. Changes have been made to the council tax reduction scheme. The Council Tax Reduction (Scotland) Amendment Regulations 2015 (SSI 46)

- uprate figures that are used to calculate the amount of council tax reduction claimants are entitled to receive
- amend the definition of 'couple' to take account of same sex marriages
- extend the classes of persons who do not need to be habitually resident in the UK in order to qualify for a council tax reduction
- amend the definition of persons who are not entitled to council tax reduction.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 3 in respect of recharges to the HRA?			
2 Have you carried out the action recommended at paragraph 5 in respect of the application of the new accounts regulations to section 106 bodies?			
3 Have you carried out the action recommended at paragraph 11 in respect of the removal of charities from the register?			
4 Have you carried out the action recommended at paragraph 18 in respect of significant asset components?			
5 Have you carried out the action recommended at paragraph 23 in respect of community safety expenditure?			
6 Have you carried out the action recommended at paragraph 25 in respect of collaborative arrangements?			
7 Have you carried out the action recommended at paragraph 48 in respect of the transition to the new group accounts standards?			
8 Have you used the note for guidance referred to at paragraph 51 when planning and performing the audit of 2014/15 LGPS pension fund accounts?			
9 Have you carried out the action recommended at paragraph 55 in respect of the audit of 2014/15 LGPS pension fund accounts?			
10 Have you carried out the action recommended at paragraph 66 in respect of agency disclosures in 2014/15 LGPS pension fund accounts?			
11 Have you carried out the action recommended at paragraph 88 in respect of 2014/15 governance statements?			

TSU contacts for local authority chapter

94. The contacts in the TSU for this chapter are

- Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or pobrien@audit-scotland.gov.uk.
- Tim Bridle, Manager - Local Government (Technical) - 0131 625 1793 or tbridle@audit-scotland.gov.uk.
- Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or acairns@audit-scotland.gov.uk.

Central government chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks that are relevant to the central government sector.

It should be read by external auditors with appointments in the central government sector. It should also be read by auditors with appointments in the health sector and further education sector as most of the articles also apply to those sectors. Auditors should also read the cross-sectoral chapter.

Guidance from the TSU on emerging risks

Carry forward of grant in aid

95. The TSU is aware that a number of non-departmental public bodies (NDPBs) are reporting unspent grant in aid (GIA) for capital projects. The *Scottish public finance manual* (SPFM) section on grant and GIA states that unspent balances held at the end of the financial year are not liable to surrender to the Scottish Government. However, the Scottish Government may take back the GIA at the year end and make a new award of grant in the following financial year.

96. Auditors should confirm that NDPBs have discussed the treatment of any unspent GIA at 31 March 2015 with the Scottish Government and have accounted for it appropriately.

Accounting developments

General accounting

Amendments to 2014/15 FReM

97. HM Treasury has issued a revised version of the 2014/15 Government financial reporting manual (the FReM). The main changes from the previous version are to section 6.2 in respect *of IFRS 7 Financial instruments disclosures*. Section 6.2 has been amended to

- encourage bodies to make appropriate disclosures relating to significant credit risk arising from debtors
- continue to require the disclosures on fair value measurements previously included at paragraphs 7.27 to 7.27B of IFRS 7. The requirements have been relocated to *IFRS 13 Fair value measurement* and (as explained at paragraph 102, that standard does not come into effect in the central government sector until 2015/16), the amendment to the FReM has been necessary to require the disclosures to be made in 2014/15.

98. Auditors should ensure they refer to amended 2014/15 FReM when auditing the 2014/15 annual report and accounts.

2014/15 disclosure checklists

99. The National Audit Office (NAO) has issued the Disclosure checklist for 2014/15 charitable NDPBs and the Disclosure checklist for annual reports 2014/15 which are designed to ensure that bodies covered by the FReM have prepared their 2014/15 annual report and accounts in the appropriate form and have complied with all disclosure requirements. The guide is cross-referenced to the 2014/15 FReM, individual financial reporting standards, and the *Companies Act 2006.*

100. While the guide is designed primarily for the NAO's internal use, auditors in Scotland may also find it helpful. Auditors may wish to use the checklist when auditing the 2014/15 annual report and accounts. Auditors will need to generate a tailored checklist by selecting the criteria that applies to their audited body.

2015/16 FReM

101. Treasury has issued the 2015/16 FReM. The two significant changes from 2014/15 are

- the adoption of *IFRS 13 Fair value measurement*
- restructuring the annual report.

Adoption of IFRS 13

102. IFRS 13 sets out requirements for assets measured at fair value and is applied in full by the FReM to

- assets that are not held for their service potential
- operational assets which are surplus to requirements where there are no restrictions on disposal which would prevent access to the market.

103. IFRS 13 does not apply to operational assets which are in use delivering front line services or back office functions. Adaptations have been added to section 6.2 to reflect this approach. In addition, existing adaptations have been amended to refer to current value in existing use, rather than fair value, where IFRS 13 is not applied.

104. The guidance on property, plant and equipment has also been amended, particularly at paragraphs 7.1.4 to 7.1.8 and by the addition of a flowchart at paragraph 7.1.14. Paragraph 7.1.6 provides guidance on determining whether an asset is surplus. It clarifies that an asset is not surplus where there is a clear plan to bring it back into future use as an operational asset.

105. Similar changes have also been made to the adaptation for IAS 38 in respect of intangible assets, and the guidance on donated assets and heritage assets.

106. In addition, paragraph 7.1.14 has been amended to require disclosures if depreciated historical cost is used as a proxy for current value in existing use or fair value, including

- the classes of assets where it has been used

- the reasons why
- information about any significant estimation techniques.

Restructuring of annual report

107. Chapter 5 has been extensively re-written to require the annual report and accounts to comprise
    - a performance report
    - an accountability report
    - the financial statements.

Performance report

108. The performance report should provide information on the body, including its main objectives and strategies and the principal risks that it faces. The requirements are based on the matters the *Companies Act 2006* requires to be dealt with in a strategic report, but bodies are only required to follow the requirements to the extent they are incorporated at section 5.2 of the FReM.

109. The performance report is required to provide a fair, balanced and understandable analysis of the body's performance. It is required to have the following two sections
    - The overview section should give a short summary that provides users with sufficient information to understand the organisation. The minimum requirements are set out at FReM paragraph 5.2.8 and include a performance summary.
    - The performance analysis section is for bodies to report on their most important performance measures. The minimum requirements are set out at FReM paragraph 5.2.10 and include a more detailed analysis and explanation of the development and performance of the body during the year.

110. The performance report should be signed and dated by the Accountable Officer or Chief Executive.

Accountability report

111. The requirements of the accountability report are based on the matters required by the *Companies Act 2006* to be dealt with in a directors' report and remuneration report but only need to be followed by bodies to the extent that they are incorporated into section 5.3 of the FReM.

112. The accountability report requires to be signed and dated by the Accountable Officer or Chief Executive. It should have sections for a
    - corporate governance report
    - remuneration and staff report
    - parliamentary accountability and audit report.

Corporate governance report

113. The corporate governance report is required to explain the body's governance structures and how they support the achievement of its objectives. As a minimum, the corporate governance report must include the

- directors' report which should disclose the information listed at FReM paragraph 5.3.9, including the composition of the management board
- statement of Accountable Officer's responsibilities, model examples of which are provided at Annex 1. Paragraphs 5.3.11 and 5.3.12 require the Accountable Officer to confirm that
  - there is no relevant audit information of which the external auditors are unaware, and that they have taken all the necessary steps to make themselves aware of any relevant audit information and to establish that the external auditors are aware of that information
  - the annual report and accounts as a whole is fair, balanced and understandable and that they take personal responsibility for the annual report and accounts and the judgments required for determining that it is fair, balanced and understandable.
- governance statement prepared in accordance with Scottish Government guidance.

Remuneration and staff report

114. The required disclosures for the remuneration and staff report are set out at FReM paragraphs 5.3.15 to 5.3.27. This includes disclosure of

- the policy on the remuneration of directors for the current and future years
- each component (e.g. salary, allowances, accrued pension benefit) and the overall single total remuneration figure for each director using the format and methodology set out by the Cabinet Office in the relevant employer pension notice
- pension entitlements for each director in the format set out in the relevant employer pension notice
- payment for compensation on early retirement or for loss of office
- payments to past directors
- the ratio between the median staff remuneration and the mid-point of the banded remuneration of the highest paid director.

115. The requirements for the staff report are set out at FReM paragraph 5.3.27 and include

- an analysis of staff numbers
- an analysis of the number of persons of each sex who were directors, senior civil servants and employees
- sickness absence data
- off-payroll engagements and expenditure on consultancy
- summary data on the use of agreed exit packages.

Parliamentary accountability and audit report

116. The parliamentary accountability and audit report is required to comprise information on

- regularity of expenditure
- fees and charges
- remote contingent liabilities
- long-term expenditure trends.

117. The FReM also requires it to comprise the certificate and report of the Comptroller and Auditor General. In Scotland, this is the independent auditor's report.

Other changes

118. Other changes include the following

- Paragraph 1.2.1 c) now states that additional commentary on items may be provided in the accounting policy note or next to an individual disclosure note.
- Paragraph 1.4.2 has been amended to reflect the introduction of two new charities SORPs.

119. Paragraph 2.2.7 has been added to state that the Accountable Officer should not approve the accounts unless they are satisfied that the accounts give a true and fair view.

Provisions

2014/15 discount rate

120. HM Treasury has issued PES(2014)9 to announce the discount rate for post-employment benefits liabilities and general provisions as at 31 March 2015.

121. The discount rate for post-employment benefits and early departure provisions will change from 1.8 % real to 1.3% real from 31 March 2015. The financial assumptions, based on market conditions, related to post employment benefit discount rates are set out in an annex. Funded schemes within central government should use a discount rate based on financial assumptions at 31 March each year, rather than these assumptions which are as at 30 November.

122. The real discount rates to be applied to provisions recognised in accordance with IAS 37 as at 31 March 2015 are as follows:

- The short term rate (for cash-flows up to 5 years from the statement of financial position date) is minus 1.5%.
- The medium term rate (between 5 and 10 years) is minus 1.05%.
- The long term rate (more than 10 years) is unchanged at 2.20%.

123. The change in discount rates could result in non-cash negative annually managed expenditure (AME) arising from interest income. This income can only be used for expenditure relating to provisions, or for depreciation of capital assets that have been donated.

124. Auditors should refer to this announcement when auditing provisions in the 2014/15 annual report and accounts.

Auditing developments

Notes for guidance on auditing 2014/15 central government annual report and accounts

125. The TSU has published Note for guidance 2015/1(CG) Audit of 2014/15 central government annual report and accounts and Note for guidance 2015/2(CG) Audit of 2014/15 central government annual report and accounts (charitable NDPBs) to provide auditors with guidance on planning and performing the audit of the 2014/15 central government annual report and accounts.

126. The notes for guidance provide guidance on the areas that the TSU considers represent a generic risk of material misstatement in the 2014/15 financial statements to inform auditors' own risk assessments. The note also provides guidance on auditors' responsibilities to

- audit the regularity of expenditure and income
- audit part of the remuneration report
- consider the consistency of the management commentary/trustees' annual report with the financial statements
- review other matters such as the governance statement and any summarised financial statements.

127. Auditors should use the appropriate note for guidance when planning and performing the audit of the 2014/15 central government annual report and accounts.

2014/15 Government Banking Service account information

128. The TSU will obtain information on account balances at 31 March 2015 for central government bodies and health boards from the Government Banking Service (GBS) and distribute them to relevant auditors. The GBS operates accounts with the Royal Bank of Scotland and Citibank.

129. The GBS has confirmed that the arrangements for 2014/15 are unchanged, and therefore they will require bodies with new GBS accounts to submit an *Auditor authorisation form* to allow disclosure of account balances to auditors.

130. Auditors should confirm the account details at their bodies have not changed from 2013/14 and that, where required, their bodies have submitted an *Auditor authorisation form* to the GBS.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 96 in respect of unspent GIA at the year?			
2 Have you carried out the action recommended at paragraph 98 in respect of the 2014/15 FReM?			
3 Have you considered the action suggested at paragraph 100 in respect of the disclosure checklists?			
4 Have you carried out the action recommended at paragraph 124 in respect of changes to the discount rate for provisions?			
5 Have you used the appropriate note for guidance referred to at paragraph 125 when planning and performing the audit of the 2014/15 central government annual report and accounts?			
6 Have you carried out the actions requested at paragraph 130 in respect of the GBS account information?			

TSU contacts for central government chapter

131. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or ncameron@audit-scotland.gov.uk.
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Health chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that affect the health sector.

It should be read by external auditors with appointments in the health sector. Auditors should also read the central government chapter and cross-sectoral chapter.

Guidance from TSU on emerging risks

Governance requirements for social care integration

132. The guidance from the TSU at paragraph 88 in the local authority chapter on reporting to audit committees in respect of integration joint boards also applies to the health sector.

Accounting developments

General accounting

2014/15 accounts manual

133. The Scottish Government Health and Social Care Directorates (SGHSCD) has issued the *2014/15 NHS board accounts manual for the annual report and accounts* (the accounts manual) to interpret the accounting guidance contained in the FReM for the NHS in Scotland.

134. Auditors should refer to the accounts manual when auditing the 2014/15 annual report and accounts.

135. The terminology throughout the accounts manual has been amended to make it consistent with the FReM. For example, the full title of the manual has been amended to refer to the annual report rather than the directors' report. The main changes to the accounts manual from 2013/14 are in respect of the

- foreword, which are aimed at improving the quality of the published annual accounts
- management commentary and remuneration report, which reflect guidance issued for 2013/14.

Foreword

136. A paragraph has been added to page 5 of the accounts manual to remind boards that the annual report and accounts should be prepared to the highest standards and presented in a way that is helpful and informative to the user.

137. It also states that, although the consolidation template may be used as a basis for preparing their published annual accounts, it should be tailored to suit the individual board's

circumstances. Disclosure is not required if an item is not material or does not apply to the board's circumstances.

138. Clarification has been added that, although the manual covers Scottish financial returns (SFRs) which are required to be submitted to the SGHSCD, SFRs should not be included in the published annual report and accounts.

Management commentary

139. The operating and financial review has been retitled the management commentary, which now comprises a directors' report and a strategic report. The 2014/15 accounts manual has been updated to reflect guidance which advised boards of changes to the FReM in respect of the directors' report and strategic report which applied from 2013/14 but which had not been reflected in the 2013/14 accounts manual.

Strategic report

140. Pages 8 to 11 of the manual set out the disclosures for the strategic report. These include the following

- A brief history of the board and its statutory background.
- The main trends and factors likely to affect the future development, performance and position of the board.
- An analysis using financial and key performance indicators.
- Sustainability reporting requirements.
- Information on social, community and human rights policies.
- A description of the strategy and business model.
- A breakdown showing the number of persons of each gender who were directors, senior managers and employees of the board as at the end of the financial year.

141. Some disclosures previously included under the directors' report, including a note that the accounts have been prepared under an accounts direction, have been moved to the strategic report.

Directors' report

142. Pages 12 to 14 of the manual set out the disclosures for the directors' report. Changes from the 2013/14 manual include the requirements for disclosure of

- sickness absence data
- published personal data related incidents
- how often members attended board meetings.

143. The wording under the heading 'date of issue' at paragraph 8 has been amended to clarify that this refers to the date that the board approved the financial statements. The Chief Executive is still required to sign the directors' report on the date the annual report and accounts are authorised for issue.

Remuneration report

144. The guidance on page 18 regarding the remuneration report has been updated to reflect the guidance issued by the SGHSCD in 2013/14 on the requirement to disclose the single total remuneration figure for each director.

145. The single total remuneration figure should include (in addition to salary, performance related pay and benefits in kind) pension benefits accrued during the year. This should be calculated as

- the real increase in pension multiplied by 20
- plus the real increase in any lump sum
- less the contributions made by the individual.

146. The real increase excludes increases due to inflation or any increase or decrease due to a transfer of pension rights.

147. The definition of remuneration has also been amended to remove employers superannuation and other pension contributions.

Other changes

148. Other changes include the following

- The guidance on page 24 includes a table setting out which sections of the annual report and accounts should be signed and by whom.
- Page 104 has been updated to reflect that the discount rate for post-employment benefits set out in PES(2014)9 (referred to at paragraph 120).
- A table has been added to the timetable section to clarify the required number of paper and electronic copies of the annual report and accounts, e.g. Audit Scotland requires two signed copies.

2014/15 capital accounting manual

149. The SGHSCD have issued the *2014/15 NHS capital accounting manual* to interpret the accounting guidance contained in the 2014/15 FReM on capital accounting issues in the NHS. The main changes from the previous version are as follows

- Chapter 6 has been updated to include the loss or damage to assets in the normal course of business in the list of impairments that can be funded by non-cash departmental expenditure limits. The normal course of business includes all loss or damage resulting from management or staff action or inaction, including theft.
- Chapter 12 has been amended to reflect the FReM guidance that service concession arrangement infrastructure assets should be recognised when the IAS 16 recognition criteria are met.
- Guidance has been added to chapter 12 setting out the arrangements for the payment of design fees for hub projects, i.e.

- For capital funded projects, existing capital resource limit (CRL) funding should be used.
- For revenue funded projects, the board should request additional CRL from SGHSCD to provide a repayable loan to the hubco (i.e. the joint venture company that is developing and delivering community infrastructure projects).

150. Auditors should refer to the accounts manual when auditing the 2014/15 annual report and accounts.

Provisions

Guidance on clinical negligence claims from 2014/15

151. The SGHSCD has issued guidance on the revised accounting treatment and presentation of the *Clinical negligence and other risks indemnity scheme* (CNORIS) from 2014/15. *Guidance on accounting for clinical negligence and other risks indemnity scheme* explains that CNORIS is a mechanism for pooling risk in respect of legal claims related to clinical negligence. Boards contribute to the CNORIS pool each financial year at a pre-agreed contribution rate based on their associated risks. If a claim is settled, the board is reimbursed for the value of the settlement less a £25k 'excess' fee.

152. When a legal claim is made against a board, it assesses whether a provision requires to be recognised based on information provided by the Central Legal Office. If a provision is required, the board also recognises an associated debtor to reflect reimbursement from the scheme. This provision and associated debtor have been recognised in previous years and continue to be required.

153. From 2014/15, boards are also required to recognise a second provision for their contributions to the scheme in future years. This means there should be two related, but distinct, provisions recognised as a result of participation in the scheme. The second provision will be funded from AME budget cover.

154. The second provision should have been recognised in previous years and therefore a prior year restatement is required. The Scottish Government will provide the figures required for this restatement.

155. The guidance provides wording at Appendix A for a disclosure note that should be included in the financial statements. This takes the various CNORIS-related disclosures in the statements and includes them in one note to provide a comprehensive explanation of how CNORIS works.

156. Auditors should refer to this guidance when auditing the CNORIS provision in the 2014/15 annual report and accounts.. Auditors should ensure boards consider the nature, as well as the amount, of the transaction when considering materiality.

Auditing developments

Notes for guidance on auditing 2014/15 health annual report and accounts

157. The TSU has published [Note for guidance 2015/3(H) Audit of 2014/15 health annual report and accounts] to provide auditors with guidance on planning and performing the audit of the 2014/15 health annual report and accounts.

158. The note for guidance provides guidance on the areas that the TSU considers represent a generic risk of material misstatement in the 2014/15 financial statements to inform auditors' own risk assessments. The note also provides guidance on auditors' responsibilities to

- audit the regularity of expenditure and income
- audit part of the remuneration report
- consider the consistency of the management commentary with the financial statements
- review other matters such as the governance statement, consolidation templates, and any summary financial information.

159. Auditors should use the note for guidance when planning and performing the audit of the 2014/15 health annual report and accounts.

Corporate governance developments

2014/15 guidance on governance statements

160. The SGHSCD have issued *Guidance on governance statements 2014/15* to help Chief Executives prepare their board's governance statement. The Chief Executive is responsible for reviewing the adequacy and effectiveness of the system of internal control. The review should comprise an assessment of the effectiveness of overall corporate governance and risk management arrangements, and be supported by internal and independent assurances.

161. The governance statement should comply with guidance in the SPFM, be accurate and complete, and fairly report the known facts. It is for the Chief Executive to decide how to organise the governance statement but the guidance provides a suggested proforma. Features of the proforma that must be included in the statement are disclosures of

- the governance framework, including information on the committee structure
- an assessment of the board's compliance with the SPFM, with explanations where a different approach has been adopted
- details of the operation of the board
- the board's assessment of its own performance. Boards may include a link to an online copy of their assessment rather than duplicating the details in the governance statement
- an assessment of the board's risk management arrangements and risk profile
- any significant control weaknesses. The guidance sets out factors to be considered when assessing significance. It requires boards to give specific consideration to any reports

from inspection agencies, and the board's performance in relation to treatment time guarantees.

162. As indicated at paragraph 88, in the TSU's view, governance issues around the assessment work carried out in preparation for health and social care integration should be considered for inclusion in the governance statement.

163. The audit committee has a specific responsibility for reviewing the disclosures included in the governance statement. It should consider the information it needs, which may include the supporting information provided to the Chief Executive.

164. A letter of assurance from the Chair of the audit committee is required to be sent to the Chair of the Scottish Government Health and Wellbeing Audit and Risk Committee to

- provide assurances on the governance of the board
- advise of any governance matters that require to be brought to the attention of the Scottish Government Audit Committee.

165. Auditors should refer to this guidance when reading the information in the 2014/15 governance statement.

Other developments

Pay and workforce planning

2014 consultants' distinction awards

166. The Scottish Advisory Committee on Distinction Awards (SACDA) has published its Annual report 2014 which sets out the results of the 2014 awards round for distinction awards to consultants in NHS Scotland.

167. The report includes a list of all distinction award holders as at 30 September 2014.

Planning and performance management

2015/16 local delivery plan guidance

168. The Scottish Government has issued NHSScotland local delivery plans 2015/16 to provide guidance on the preparation of local delivery plans (LDPs) for 2015/16. Boards are to develop plans focused on strategic priority areas, including prevention, health inequalities, primary care, and integration.

169. Health and social care partners are required to take account of the health and social care outcomes set out in legislation (referred to at paragraph 92) when developing their plans. Once established, integration authorities will lead on the delivery of these outcomes.

Social care integration

Guidance on hospital set aside budgets

170. The Scottish Government has issued guidance on establishing the amount to be set aside by health boards for integrated health and social care services delivered in a large hospital. Guidance on financial planning for large hospital services and hosted services recommends that this should be determined by analysis of hospital activity and cost information.

171. Hospital patient administration systems should be used to identify the hospital activity and capacity used by patients for each integration authority. It is recommended that data used for the first strategic plan should be based on an average of the previous three years of activity. However, decisions on capacity and service redesign may result in subsequently result in different consumption patterns.

172. Performance against the plan for hospital capacity requires to be reported to allow the strategic plan to be adjusted and remedial action taken in year if necessary. Any adjustments to the set aside resource to reflect variances in performance should be made through annual adjustments to the strategic plan.

173. The methodology for costing this activity is a local decision, but a consistent methodology should be applied across all integration authorities in a health board area. The same methodology should be applied to hosted services provided in hospital.

Other integration scheme regulations and guidance

174. Regulations and guidance relevant to social care integration are included at paragraphs 78 to 85 of the local authority chapter.

175. In addition, regulations have been issued which prescribe the health board functions to be delegated through an integration scheme. The Public Bodies (Joint Working) (Scotland) Act 2014 (Prescribed Health Board Functions) (Scotland) Regulations 2014 (SSI 344) sets out

- the functions that may be delegated at Schedule 1
- the functions that must be delegated at Schedule 2
- the health board services related to these functions at Schedule 3.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 134 in respect of the 2014/15 accounts manual?			
2 Have you carried out the action recommended at paragraph 150 in respect of the 2014/15 capital accounting manual?			

	Yes/No/N/A	Initials/date	W/P ref
3 Have you used the note for guidance referred to at paragraph 157 when planning and performing the audit of the 2014/15 health annual report and accounts?			
4 Have you carried out the action recommended at paragraph 165 in respect of 2014/15 guidance on governance statements?			
5 Have you carried out the actions requested at paragraph 130 in respect of the GBS account information?			

TSU contacts for health chapter

176. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or ncameron@audit-scotland.gov.uk.
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Further education chapter

Introduction

This chapter contains technical developments and guidance on emerging risks in the quarter that are relevant to further education colleges.

It should be read by external auditors with appointments in the further education sector. Auditors should also read the central government chapter and the cross-sectoral chapter.

Accounting developments

Briefing note on review of resource returns

177. Colleges Scotland has issued a briefing note on proposals for external auditors to review the annual resource returns. The Office of National Statistics reclassification briefing note on change of accounting year end is intended to explain to board members, principals and other college senior managers the impact of moving the financial year end from 31 March to 31 July from 2014/15.

178. A key issue is that Scottish Government funding is still provided on a fiscal year basis, i.e. ending 31 March. The Scottish Funding Council (SFC) has proposed that the resource returns at 31 March (which are submitted to the SFC to monitor how funding was spent) should be reviewed by external auditors to provide assurance on the financial information contained in the returns.

179. The objective of the review engagement would be to enable an auditor to state whether anything has come to their attention that causes them to believe that the financial returns are not prepared in accordance with the applicable financial reporting framework (i.e. limited or 'negative' assurance). The TSU has agreed to arrange a review engagement in principle, subject to acceptance by the Scottish Government.

180. The TSU will provide guidance to auditors on performing and reporting on the review engagement in due course once the SFC has obtained confirmation from the Scottish Government that the approach is acceptable.

Corporate governance developments

New governance code

181. The SFC has issued a Code of good governance for Scotland's colleges which sets out standards of good governance for all college boards with effect from 1 August 2014. It has also issued an accompanying guidance note Good practice in college governance which advises that the code represents the SFC's view of good practice in governance.

182. It is therefore a condition of grant that colleges comply with the code. It is expected that regional strategic bodies (RSBs) will also follow the code, where relevant. Each college is required to report compliance with the code in its corporate governance statement. In addition, the chair is encouraged to report personally as to how the principles have been applied by the board.

183. The principles of the code are set out in five sections as follows

- Section A covers leadership and strategy including stating that the board is responsible for the college's strategic direction, and ensuring a performance measurement system is in place. For an assigned college, the board is required to have regard to the strategy determined by the RSB.
- Section B covers the quality of the student experience.
- Section C sets out the accountability requirements including the responsibilities of the board and committees.
- Section D deals with effectiveness including the responsibilities of the board Chair, members and the principal to ensure the board operates effectively.
- Section E deals with relationships and collaboration between colleges, RSBs, staff and students.

184. Where a college's practice is not consistent with any principle of the code, it is required to make this known immediately to the SFC or RSB. In the event of the latter, the RSB is required to provide the SFC with details. An explanation for the inconsistency requires to be clearly stated in the college's corporate governance statement. Colleges will be expected to offer a clear rationale for exceptions in the context of their operational model and to identify mitigations.

185. Auditors should use the code when reading the information in the 2014/15 corporate governance statement.

New financial memorandum

186. The SFC has issued a new Financial memorandum with fundable bodies in the college sector which applies from 1 December 2014. It is a condition of the grants from the SFC that that colleges and RSBs comply with the requirements of the memorandum.

187. The memorandum is set out in four parts as follows

- Part 1 deals with the relationship between the SFC and institutions, and the responsibilities of each for the proper stewardship of public funds.
- Part 2 imposes a number of general requirements on all institutions including the requirement to repay grant if a requirement is not complied with.
- Part 3 applies additional requirements to RSBs, regional colleges and regional boards. Regional colleges and regional boards are required to follow the requirements of the SPFM except where special actions or agreed derogations are set out in the memorandum.

188. Auditors should confirm their colleges are aware of the memorandum and have arrangements in place to ensure they comply with it.

Other developments

Finance

Use of depreciation funding in 2014/15

189. The SFC has issued guidance on the release of 2014/15 funding, which was previously earmarked for depreciation, for other purposes. Financial adjustments for student support and other purposes in financial year 2014/15 explains that prior to reclassification as central government bodies, colleges used available funds to cover depreciation charges on their fixed assets.

190. Following reclassification, colleges have been given a cash budget to cover their costs (including depreciation) and a separate budget for fixed assets. As depreciation is not a cash cost, there is additional budget available which can be used to meet other revenue expenditure, including student support.

191. As colleges are required to spend the full amount of their cash budgets, this additional revenue expenditure may result in an operational deficit in colleges' 2014/15 income and expenditure accounts equivalent to their net depreciation charges. The SFC will adjust for these deficits when assessing colleges' financial health.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 185 in relation to the code of good governance?			
2 Have you carried out the action recommended at paragraph 188 in relation to the financial memorandum?			

TSU contact for further education chapter

192. The contact in the TSU for this chapter is Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Cross-sectoral chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to all sectors.

It should be read by all external auditors. Information on developments and guidance from the TSU in the quarter that are relevant to only one sector are covered in the relevant sector-specific chapter.

Guidance from TSU on emerging risks

Auditor's responsibilities for management commentary

193. The TSU has received some enquiries from auditors regarding their responsibilities in respect of the management commentary included in the annual report and accounts. Auditors are required to read the management commentary and express an opinion in the auditor's report as to whether it is consistent with the financial statements.

194. In this context, an inconsistency is anything in the management commentary that contradicts information contained in the audited financial statements. Inconsistencies include

- differences between amounts or narrative appearing in the financial statements and the management commentary
- differences between the bases of preparation of related items where the figures are not directly comparable and the different bases are not disclosed
- contradictions between figures in the financial statements and the narrative explanation of those figures in the management commentary.

195. Auditors should also read the management commentary to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by auditors in the course of performing the audit. If revision of the management commentary is necessary, and the audited body refuses to make the revision, auditors should include in the auditor's report an 'other matter' paragraph describing the matter.

196. Further guidance is included in the notes for guidance from the TSU on auditing the 2014/15 annual report and accounts. Auditors should read the management commentary and report in accordance with this guidance.

Holiday pay and overtime

197. A recent ruling from the Employment Appeal Tribunal states that compulsory overtime is part of an employee's normal remuneration and therefore should be included in the calculation of pay for holiday leave taken. The position on voluntary overtime is less clear.

198. Public bodies have not previously included overtime in their calculations of holiday pay owed to employees. Although this decision may yet be subject to appeal, auditors should confirm that audited bodies are considering whether the criteria for recognising a provision are met, including obtaining legal advice.

New requirement to report to Pension Regulator

199. The TSU has identified that auditors of public service pension schemes are required to report certain breaches of the law to the Pension Regulator from 1 April 2015 under section 70 of the Pensions Act 2004. The application of section 70 was extended to cover public service schemes by Schedule 4 of the Public Service Pensions Act 2013.

200. Section 70 imposes the duty to report on a number of individuals including a member of the pension board of a public service scheme and a professional adviser to such a scheme. The term professional adviser is defined in section 47 the Pension Act 1995 and includes the auditor appointed by the trustees. Although section 47 refers specifically to occupational pension schemes, and auditors in the public sector are not appointed by the trustees, the TSU has confirmed with the Pension Regulator that they expect the duty to nevertheless apply to auditors of public service pension schemes.

201. Auditors are therefore required to provide a written report to the Pension Regulator from April 2015 if they have reasonable cause to believe that a legal duty relevant to the administration of the scheme has not been complied with, and that failure is likely to be of material significance to the regulator. Auditors should contact the TSU for advice if such a situation arises in practice.

Corporate governance developments

New code on fraud and corruption

202. CIPFA has issued a code of practice and guidance notes to provide the basis for counter fraud arrangements across the public sector. The *Code of practice on managing the risk of fraud and corruption* consists of the following five groups of principles that set out a body's responsibilities for establishing good counter fraud practice and the form that will take

- The governing body should acknowledge its responsibility for ensuring that the risks associated with fraud and corruption are managed effectively across all parts of the organisation.
- Fraud risk identification is essential to understand specific exposures to risk, changing patterns in fraud and corruption threats and the potential consequences to the organisation and its service users.
- An organisation needs a counter fraud strategy setting out its approach to managing its risks and defining responsibilities for action.
- The organisation should make arrangements for appropriate resources to support the counter fraud strategy.

- The organisation should put in place policies and procedures to support the counter fraud and corruption strategy and take action to prevent, detect and investigate fraud.

203. The guidance notes consider the implementation of the code and share examples of good practice. This includes interpretations to highlight where sectoral differences should be taken into account.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you read the management commentary in accordance with the guidance at paragraph 196?			
2 Have you carried out the action recommended at paragraph 198 in respect of holiday pay?			
3 Have you carried out the action required at paragraph 201 in respect of reporting to the Pension Regulator?			

TSU contact for cross-sector chapter

204. The contact in the TSU for this chapter is Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or pobrien@audit-scotland.gov.uk.

Technical Services Unit

Audit Scotland's Technical Services Unit (TSU) informs the professional judgement of appointed external auditors on technical matters and encourages the proper exercise of professional scepticism to improve the quality of the audit delivered to the Accounts Commission and Auditor General for Scotland. The TSU provides authoritative guidance and practical assistance to support appointed auditors in carrying out their responsibilities under the *Code of audit practice* to

- provide an opinion on audited bodies' financial statements and, where required, the regularity of transactions
- review and report on other information published with the financial statements, including governance statements and remuneration reports
- examine and report on approved grant claims and other returns submitted by local authorities
- review and report on whole of government accounts returns.

Contact details for relevant TSU staff are included at the end of each chapter.

Feedback on technical bulletins is encouraged and should be sent to

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AUDIT SCOTLAND

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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

Foreword

Technical bulletins are prepared by Audit Scotland's Technical Services Unit (TSU), and approved by the Assistant Auditor General, to provide external auditors appointed by the Accounts Commission and Auditor General for Scotland with

- information on the main public sector technical developments in the quarter that are relevant to their audit appointment
- guidance from the TSU on any emerging risks identified in the quarter.

Technical bulletins are available to external auditors from Audit Scotland's *Technical reference library,* and published on the Audit Scotland website so that audited bodies and other stakeholders can access them.

It is important that auditors read this technical bulletin promptly so they are familiar with the information and guidance provided. The auditor action checklist section at the end of each chapter should be completed by a senior member of the audit team.

The articles on technical developments are intended to highlight the key points that the TSU considers external auditors require to be aware of. It may still be necessary for auditors to read the source material where greater detail is required. The documents referred to in the articles can be obtained by using the hyperlinks, where available. They are also available to external auditors from Audit Scotland's *Technical reference library*.

While auditors act independently, and are responsible for their own conclusions and opinions, the TSU has a role in ensuring that those conclusions and opinions are reached on the basis of informed judgement. Consistency in similar circumstances is important and **Audit Scotland's *Code of audit practice* therefore states that auditors should normally follow TSU guidance.** Auditors should advise the TSU promptly if they intend not to follow guidance provided in this technical bulletin on an emerging risk.

The TSU encourages feedback on this technical bulletin. Comments should be sent to pobrien@audit-scotland.gov.uk.

More in-depth and extensive guidance is provided in separate technical guidance notes published by the TSU. Technical guidance notes published in the quarter are referred to in this technical bulletin, and can be obtained by using the hyperlinks to the Audit Scotland website.

Headlines

This chapter provides brief headlines for the articles on technical developments and guidance in this technical bulletin, classified by the audit year to which it relates, and referenced to the paragraphs containing the main article.

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Cross-sectoral chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to all sectors, and a summary of cases of fraud.

It should be read by all external auditors. Information on developments and guidance from the TSU in the quarter that are relevant to only one sector are covered in the relevant sector-specific chapter.

Auditing developments

Extended auditor reporting from 2014/15

1. The Financial Reporting Council (FRC) has issued a report containing the results of a survey on the implementation of extended auditor reporting required from 1 October 2012 for companies subject to the *UK Corporate governance code*.

2. The extended reporting requirements were explained in technical bulletin 2013/2 (paragraph 20). In summary, revisions to *ISA 700 (UK&I) The independent auditor's report on financial statements* require auditors to include the following in their independent auditor's reports
   - A description of those assessed risks of material misstatement identified as having the greatest effect on the overall strategy, the allocation of resources, and directing the efforts of the audit team.
   - An explanation of how the auditor applied the concept of materiality.
   - A summary of the audit scope, including an explanation of how the scope was responsive to the assessed risks of material misstatement and the concept of materiality.

3. As advised in technical bulletin 2014/4 (paragraph 1), auditors are required to include the above matters, as well as the findings in respect of each risk, in their annual audit reports (rather than independent auditor's reports) from 2014/15. Auditors should refer to the findings from this survey when preparing their 2014/15 annual audit reports.

4. The survey findings set out in Extended auditor's reports - a review of experience in the first year confirm that auditors appeared to have met the new reporting requirements, although some improvements were identified. For example, the narrative should be related more directly to the specific circumstances of the audited body rather than using generic or abstract explanations expressed in standardised language.

5. Table 3 of the report analyses the number of assessed risks of material misstatement reported by each audit firm, highlighting the highest (10) and lowest (1) numbers reported. Table 5 provides an analysis of the types of risk reported, with impairment of assets being the most frequently recurring.

6. Some auditors had included the significant risks defined in auditing standards (i.e. fraud in revenue recognition, and management override of controls) in the risks of material misstatement. However, the report clarifies that it was not the FRC's intention that these risks should be included as a matter of course.

7. The survey covers the inclusion of a description of the findings for each identified risk, and illustrates this on page 24 of the report. The report warns that care needs to be taken with the inclusion of such findings so as not to inappropriately include discrete opinions on separate elements of the financial statements.

8. All of the auditor's reports in the survey met the requirement to explain how the auditor applied the concept of materiality, including specifying the threshold used by the auditor as materiality for the financial statements as a whole. However, most reports also stated the benchmark used in determining materiality and described the percentage that was applied to the benchmark in order to determine materiality. In some cases, the reasoning behind the choice of the benchmark was also explained.

9. Just over half of the reports provided a comprehensive explanation of how the scope of the audit addressed the assessed risks of material misstatement and the auditor's application of materiality. However, the remainder seemed to meet the requirement in form but not in substance, and provided a description that was detached from the discussion of risks and materiality.

Corporate governance developments

New counter fraud strategy

10. The Scottish Government has issued Protecting public resources in Scotland which sets out a strategic approach to countering fraud, bribery and corruption. The approach includes objectives to

- raise awareness
- improve systems and controls
- work well across organisations
- conduct effective investigations
- maintain robust whistle-blowing procedures
- punish fraudsters effectively.

Other developments

Pension funds

New governance code

11. The Pensions Regulator has issued a code of practice that sets out the legal requirements for public service pension schemes established under the Public Service Pensions Act 2013. The

Act introduced a framework for the governance and administration of public service pension schemes (including those for local government, civil servants, health and teachers) and provides for an extended regulatory oversight by the regulator.

12. Code of practice 14 Governance and administration of public service pension schemes is particularly directed at scheme managers and the members of pension boards. It provides them with practical guidance and sets out standards of conduct and practice expected.

13. Auditors should refer to this code when considering a pension fund's corporate governance arrangements.

Fraud cases

14. The following is a summary of fraud cases arising at audited bodies that have recently been reported by auditors to the TSU. Auditors should consider whether the weaknesses in internal control that facilitated each fraud may apply at their audited bodies and take the appropriate action.

Expenditure

Unauthorised ordering of goods

15. A teacher based at a football learning centre defrauded £5,000 from a council by ordering tickets from the related football club for personal use. Key features of the fraud include the following

- The fraud was discovered by the football club’s internal auditor during a routine audit.
- The fraud was possible as invoices were approved by the perpetrator, and accepted by the education service without proper supporting documentation.
- Processes have been reviewed and controls are being strengthened.

Overpayments of social care payments

16. A council overpaid £9,000 for the provision of social care as payments continued to be made to the provider for nine months after a customer had died. Key features include the following

- The overpayments were possible due to no internal controls being in place to ensure payments were only made for appropriate customers. The council relied on the provider to check remittance advices and inform the council of any discrepancies.
- Internal audit has undertaken a review of payments, and overpaid amounts have been recovered from subsequent payments to the supplier.

Fraudulent new supplier

17. A childcare development officer defrauded over £37,000 from a council by submitting a fraudulent new supplier form for training course provision. Subsequently, fraudulent invoices were paid. Key features include the following

- The fraud was facilitated by

  - no independent confirmation that the supplier was legitimate being obtained prior to being added to the accounts payable system
  - invoices being authorised for payment without any checks being carried out on their validity
  - the perpetrator keeping the value of invoices below £1,000 to avoid detection and charging invoices to cost centres which were underspent against budget.
- The fraud was discovered when a colleague received an order for training courses and discovered that the address on the order was that of the perpetrator.
- Internal audit undertook an investigation and have developed an action plan in order to address the control weaknesses. A police investigation is ongoing.

Theft

Theft of vehicle

18. A perpetrator stole a refuse collection vehicle from a council site and then caused significant damage to other vehicles. The key features include the following
    - The theft was possible as the keys were left in the ignition.
    - The theft was discovered when a member of the public reported seeing the vehicle being driven erratically.
    - A number of cars and public property were hit by the stolen vehicle, with repair costs estimated at £11,000.
    - The perpetrator has been charged.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 3 in respect of the study on extended auditor reporting?			
2 Have you carried out the action recommended at paragraph 13 in respect of the pension fund code of practice?			
3 Have you carried out the action required at paragraph 14 in respect of the reported fraud cases?			

TSU contact for cross-sector chapter

19. The contacts in the TSU for this chapter are

- Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or pobrien@audit-scotland.gov.uk.
- Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or acairns@audit-scotland.gov.uk (for fraud cases).

Local authority chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to the local authority sector.

It should be read by external auditors with appointments in the local authority sector. Auditors should also read the cross-sectoral chapter.

Accounting developments

General accounting

Guidance on 2014/15 financial statements

20. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued LAAP bulletin 103 Closure of the 2014/15 accounts and related matters to provide further guidance on the 2014/15 financial statements.

21. Much of the bulletin content either does not apply to Scotland or merely highlights other guidance. The main item that applies to Scottish local authorities is covered at paragraphs 55 to 58 of the bulletin. This highlights the Employment Appeal Tribunal ruling that holiday pay should include non-guaranteed overtime (i.e. overtime which is not guaranteed by the employer, but which the worker is obliged to work if it is offered).

22. The bulletin highlights that the ruling may have implications for local authorities where their employees are required to work overtime as a regular part of their job. The backdated claims have, however, been limited, as the tribunal ruled that workers can only make claims if it is less than three months since their last incorrect payment. The claim can, however, be backdated until such time as there is a three month break between underpayments.

23. Authorities need to assess the likely impact of the ruling and consider whether a provision is required to be recognised under the *IAS 37 Provisions, contingent liabilities and contingent assets*.

24. Auditors should refer to the guidance in this bulletin when auditing the 2014/15 annual accounts.

2015/16 accounting code

25. The CIPFA/LASAAC Local Authority Code Board (CIPFA/LASAC) has issued the *Code of practice on local authority accounting in the UK 2015/16* (accounting code) which sets out local authority accounting requirements for 2015/16.

26. The accounting code's financial reporting framework is based on international financial reporting standards (IFRS) as adopted by the European Union, adapted for the local authority

context where necessary. The 2015/16 code has been prepared on the basis of accounting standards and other pronouncements in effect for accounting periods commencing on or before 1 January 2015.

27. The main changes in this edition of the accounting code are to reflect the adoption of *IFRS 13 Fair value measurement*. Fair value is defined at paragraph 4.1.2.11 as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. an exit price). This reflects the definition in IFRS 13 without any adaptation.

28. Section 2.10 has been added to set out the measurement and disclosure requirements for items where the accounting code requires or permits fair value measurement. These items are listed at paragraph 2.1.2.33 and include surplus assets, revenue, investment property, assets held for sale, and financial instruments. The requirements apply prospectively from 1 April 2015 (i.e. there is no retrospective adjustment).

29. The measurement requirements for fair value are set out at paragraphs 2.10.2.18 to 2.10.2.29 and include the following

- When measuring fair value, authorities should take into account the characteristics of the asset, such as its condition and location and any restrictions on its sale or use.
- Authorities are required to use valuation techniques consistent with one or more of the three main approaches to measuring fair value (i.e. the market approach, the cost approach and the income approach), the main aspects of which are summarised in paragraphs B5 to B11 of IFRS 13.
- Local authorities are required to follow the fair value hierarchy prescribed by paragraphs 76 to 90 of IFRS 13 which categorises into three levels the valuation techniques used to measure fair value. These include
  - quoted prices in active markets for identical assets or liabilities (level 1)
  - inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly (level 2)
  - unobservable inputs (level 3).

30. The disclosure requirements are set out at section 2.10.4. They are required for all assets and liabilities measured at fair value in the accounting code, with the exception of those excluded by paragraphs 2.10.2.15 and 2.10.2.16 (e.g. leases, and pension scheme assets). Disclosures are required to help users assess

- for assets and liabilities that are measured at fair value after initial recognition, the valuation techniques and inputs used to develop those measurements
- for recurring fair value measurements using significant unobservable inputs (level 3), the effect of the measurements on surplus or deficit on the provision of services or other comprehensive income and expenditure for the period.

31. There is also an additional disclosure requirement in respect of impairment at paragraph 4.7.4.2 if the recoverable amount is fair value less costs of disposal.

32. Other than surplus assets, there are no changes to the measurement requirements for property, plant and equipment as a result of adopting IFRS 13. However, there has been a change in terminology with references to fair value in the 2014/15 accounting code replaced with references to current value. Current value is defined at paragraph 4.1.2.4 as having the following four measurement bases

- Existing use value for assets providing service potential to the authority where an active market exists.
- Existing use value – social housing for operational council dwellings.
- Depreciated replacement cost (DRC) for assets where there is no market or the asset is specialised.
- Fair value for surplus assets.

33. There is a new requirement at paragraph 4.1.4.2 for authorities to disclose information within the accounting policies that helps users to understand the valuation techniques used to develop the current value measurements for significant categories of property, plant and equipment.

34. In addition to the changes arising from the adoption of IFRS 13, other changes in this edition of the accounting code are summarised in the following paragraphs.

35. Appendix D of the accounting code sets out disclosure requirements for the 2015/16 financial statements as a result of the change in accounting policy for measuring highways infrastructure assets in the 2016/17 code. The measurement basis will change from historical cost to current value. Authorities should disclose the following (to the extent that the information is known or reasonably estimable)

- Narrative explaining that highways infrastructure assets are to be recognised as a separate class of property, plant and equipment and measured for the first time at DRC in the 2016/17 financial statements, in accordance with the *Code of practice on transport infrastructure assets* (the infrastructure code).
- The carrying amount of assets expected to be reclassified as highways infrastructure assets, i.e. the original 1 April 2015 measurement at depreciated historical cost.
- The expected amount of any revaluation gains and losses to be recognised on reclassification and remeasurement.
- The expected change in depreciation, impairment, revaluation etc to be recognised in 2015/16 comparatives in the 2016/17 financial statements.

36. Clarification has been added to paragraph 4.1.2.38 regarding what a ‘short period’ means for the measurement of classes of property, plant and equipment. This relates to a sentence in that paragraph that states that a class of assets may be revalued on a rolling basis provided revaluation is completed within a short period. The paragraph has been amended to explain that a ‘short period’ normally means once every five years.

37. There are some changes to section 4.10 on heritage assets to reflect that FRS 30 has been replaced by FRS 102. Confirmation has been added at paragraph 4.10.14 that the

measurement of heritage assets should continue to be made by any method that is appropriate and relevant. There has also been some reduction in disclosure requirements, e.g. disclosures required by paragraph 4.10.4.4 in respect of transactions are only required for the current and preceding period rather than each of the previous four accounting periods.

38. Other changes include the following

- Amendments have been made throughout the accounting code to reflect the requirements of *The Local Authority Accounts (Scotland) Regulations 2014* (the accounts regulations). This includes a footnote to explain that references to 'statement of accounts' in the code should be read as 'annual accounts' for Scottish authorities.
- There is an amendment at paragraph 1.5.1 to highlight the importance of considering materiality when preparing disclosures. It states that CIPFA/LASAAC is of the view that local authorities should only include disclosures that are material to the presentation of a true and fair view and to the understanding of users of the financial statements.
- Clarification has been added to paragraph 3.4.2.40 in respect of disclosures that support the movement in reserves statement. It states that the analysis for lines g) (i.e. adjustments between accounting basis and funding basis) and i) (transfers to or from reserves) should not obscure useful information by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics.

Property, plant and equipment

New guidance notes on highways infrastructure assets

39. CIPFA has issued guidance notes to provide practical assistance to local authorities when implementing the infrastructure code's measurement requirements.

40. The infrastructure code requires highways infrastructure assets (including carriageways, footways, cycletracks, structures, street furniture, street lighting, traffic management systems and land) to be measured on a DRC basis. DRC is a method of valuation that provides the current cost of replacing an asset with its modern equivalent asset (MEA) less deductions for all physical deterioration and all relevant forms of obsolescence.

41. Section 5 of the guidance notes explains the principles of a DRC valuation. The DRC value is calculated by subtracting the accumulated depreciation from the gross replacement cost (GRC).

42. The GRC is the cost of replacing the asset with its MEA. The MEA should give the same service and performance as the existing asset, but should use modern materials and technology. It should include any modern safety design requirements, but should not include redesign of the asset.

43. To calculate GRC for any of the infrastructure asset types, it is necessary to know the dimensions of the asset and the relevant unit cost rate to replace the asset. For example, for a carriageway the required dimensions would be length and width, and the rate would be £ per

m2. The rate used to calculate GRC should be the cost to replace the asset with an MEA based on the complete replacement of the network.

44. For some highways infrastructure assets, including carriageways, there are central GRC rates that local authorities can use when they do not have their own rates. Guidance on the calculation of specific asset classifications is provided at sections 6 to 11 of the guidance notes.

45. Paragraph 6.1 explains that the GRC valuation for carriageways can be calculated using the *Valuation toolkit*, which is provided centrally as part of the supporting materials on the CIPFA website. The toolkit incorporates centrally provided rates.

46. Accumulated depreciation for carriageways is estimated using the current replacement cost for the depreciable surface layers of a carriageway to estimate the amount of the asset's value that has been consumed.

47. The *United Kingdom Pavement management system* (UKPMS) is the national standard for management systems for the assessment of local road network condition and for the planning of investment and maintenance. A local authority's UKPMS will hold detailed information in relation to the road network inventory and condition data and can be used to estimate the depreciation elements of the DRC valuation. The condition of a road is used as a proxy for its age, which is then used to estimate where a carriageway is on its life cycle and therefore the proportion of its value that has been consumed.

48. Paragraph 6.2 advises that, for financial reporting purposes, it is anticipated that the accounting code will require highways infrastructure assets to be reported as one figure in the balance sheet. CIPFA/LASAAC has agreed the principle that carriageways should be deemed a single asset.

49. Section 13 provides guidance on the required accounting disclosures. The requirements for 2015/16 and 2016/17 are outlined in paragraphs 13.2 and 13.3. The financial statements for 2015/16 will also require to be restated in accordance with paragraph 13.3 for 2016/17.

50. Paragraph 13.4 explains that the valuation at 1 April is the opening GRC value of the asset at the start of the year. This is the same as the previous year's closing GRC balance. This differs from other property, plant and equipment assets valued on a DRC basis, where this figure is normally the DRC valuation or certified amount. When these other property, plant and equipment assets are revalued, the accumulated depreciation is written out of the accounts and the DRC valuation is held and subsequently depreciated until the next revaluation. For highways infrastructure assets, a different approach is being considered by CIPFA/LASAAC which would mean that the accumulated depreciation was not written out on revaluation.

51. Paragraph 13.6 explains that the revaluation reserve for infrastructure assets will only come into existence on 1 April 2015 (when the 2015/16 balances are restated for the 2016/17 accounts) and will initially hold all revaluation increases that take the asset from historical cost to its DRC valuation. These increases will be the sum of GRC and accumulated depreciation differences.

52. Auditors should refer to these guidance notes when considering local authorities' arrangements for valuing highways infrastructure assets on a DRC basis from 2016/17.

Provisions

New statutory guidance on equal pay and severance costs from 2014/15

53. The Scottish Government has issued statutory guidance which provides local authorities with financial flexibility to assist with meeting the costs associated with equal pay and severance. The statutory guidance in Finance circular 4/2015 Equal pay and severance provides flexibility by permitting authorities to

- delay the financial impact of equal pay and severance until a cash payment is made
- use capital receipts to fund equal pay back pay settlements and severance payments.

54. The statutory guidance applies from 1 April 2014 and will expire on 1 April 2018. The statutory flexibility is not mandatory but, where an authority chooses to use the flexibility, the following new statutory accounts are required

- Equal pay provision statutory adjustment account.
- Severance provision statutory adjustment account.

55. In each financial year covered by the statutory guidance, a statutory adjustment may be made to exclude the following when determining the movement on the general fund for the year

- A new or increased provision for severance.
- The equal pay back payment element of any new or increased provision.

56. The statutory adjustment should be debited to the relevant new statutory account, with a corresponding credit to the general fund. When payments are made or the amount of the provision is reduced, the relevant statutory account should be credited, with a corresponding debit to the general fund. By 31 March 2019, the debits to each statutory account should be matched by corresponding credits.

57. Capital receipts may be used to fund equal pay back payments and severance costs. However, authorities are required to act prudently which means

- they should not rely exclusively on the use of capital receipts but should meet this cost from revenue or revenue reserves where possible
- assets should not be sold purely to fund equal pay or severance.

58. There are further conditions on the use of capital receipts to fund severance costs as they may only be used

- where the severance costs arise from service redesign which is properly aligned to delivering on the preventative agenda and engagement with community planning partners. There is no approval process but the alignment is to be evidenced through a local authority's committee reporting structure
- to fund the statutory elements

- to fund lump sums due either to the individual or a pension fund and not any future recurring payments.

59. Capital receipts may not be used to fund severance costs if these costs relate to teachers.

60. The statutory guidance varies the accounting treatment of capital receipts set out in the accounting code as follows

    - The requirement to credit the capital fund with an amount equal to the disposal proceeds (i.e. capital receipt) is replaced with the option to credit the new statutory accounts.
    - The value of the disposal proceeds which may be credited may not exceed the debit value of the statutory adjustment. This means that disposal proceeds may not be credited in anticipation of future increases in a provision.
    - When a payment is made, the relevant statutory account should be debited with a corresponding credit to the general fund. This should be presented separately from the provisions adjustment in the movement in reserves statement, i.e. the analysis should not be for the net movement in the statutory accounts.
    - Any disposal proceeds not applied to a provision as at 31 March 2019 should be credited to the statutory capital fund.

61. Auditors should confirm compliance with this statutory guidance for authorities choosing to use the flexibility when testing equal pay and severance costs as part of the audit of the 2014/15 financial statements.

Management commentary

New preparation guidance from 2014/15

62. The Scottish Government has issued guidance on the preparation of a management commentary which the accounts regulations require to be included in the annual accounts from 2014/15. Finance circular 5/2015 The Local Authority Accounts (Scotland) Regulations 2014 - management commentary comprises the following two parts

    - Part 1 provides non-statutory guidance.
    - Part 2 provides statutory guidance which requires the management commentary to reflect those matters quoted companies are required by the *Companies Act 2006* to disclose in a strategic report, interpreted for local authorities.

63. The content of a strategic report required by the *Companies Act* is summarised in a table at paragraph 7 of part 1. The statutory guidance at paragraph 6 sets out the interpretation of these requirements for local authorities. In summary, a management commentary should include the following

    - A fair review of the local authority's business, which should be a balanced and comprehensive analysis of
        - the development and performance of the business during the financial year

  - the position of the authority's business at the end of the year, consistent with the size and complexity of the business.
- A description of the principal risks and uncertainties facing the authority.
- Financial key performance indicators, as well as any non-financial performance indicators that management consider relevant. These do not necessarily need to include information relating to environmental matters or employee matters which would be required by the *Companies Act*.
- The main trends and factors likely to affect the future development, performance and position of the authority's business.
- A description of the authority's strategy and business model.
- References to, and additional explanations of, amounts included in the authority's annual accounts.

64. Paragraph 7 of the statutory guidance requires that the content elements should not be treated as a list of disclosures and addressed in isolation. The management commentary should recognise, highlight, and explain the relationships and interdependencies between elements and other disclosures in the annual accounts.

65. The statutory guidance at paragraph 2 requires local authorities to prepare a management commentary having regard to Guidance on the strategic report issued by the FRC. Specifically, a local authority is required by paragraph 5 to apply the communication principles set out in that guidance. They are reproduced at paragraph 12 of part 1 and include, for example, requirements for the management commentary to

- be fair, balanced, understandable, and comprehensive but concise
- have a forward-looking orientation
- provide information that is entity-specific
- highlight and explain linkages between pieces of information presented within the management commentary and in the annual accounts more broadly.

66. Only information that is material in the context of the management commentary should be included within it. When considering materiality, a local authority is required by paragraph 8 to have regard to the principles set out in paragraphs 5.4 and 5.5 of the FRC guidance.

67. There is no prescription regarding the format of the management commentary. Part 1 of the circular refers to guidance issued by Deloitte which provides a suggested framework which can be followed. Key aspects from the guidance have been reproduced at paragraph 27 in the circular.

68. There is no requirement for a local authority to prepare a directors' report. However, local authorities are required to include in the management commentary those matters required to be disclosed in a directors' report by the *Companies Act* (summarised at paragraph 8 of part 1) if they are relevant and considered to be of strategic importance.

69. The statutory guidance at paragraph 9 sets aside the accounting code's requirement for an explanatory foreword. However, paragraph 22 of part 1 requires authorities to consider whether any items required to be included in the explanatory foreword should be included in the management commentary. The explanation of the financial statements, their purpose and relationship between them should not be included in the management commentary.

70. Auditors should refer to this guidance when reading and reporting on the 2014/15 management commentary. Guidance on auditors' responsibilities for the management commentary is provided at paragraphs 606 to 612 of note for guidance 2014/11(LA). The issue of this finance circular supersedes paragraph 607.

Pension funds

Guidance on application of accounts regulations

71. The Scottish Government has issued guidance on the application of the accounts regulations to pension funds from 2014/15. Finance circular 6/2015 Local authority pension fund annual report and accounts replaces finance circular 1/2011 and comprises the following two parts

- Part 1 provides the new non-statutory guidance.
- Part 2 provides the statutory guidance on pension fund accounting requirements generally, and is unchanged from circular 1/2011. The statutory guidance states that the annual accounts within the pension fund annual report are a separate abstract of accounts and are subject to the arrangements set out in the *Local Government (Scotland) Act 1973* and the accounts regulations.

72. A report about the management and financial performance of the pension fund continues to be required by *The Local Government Pension Scheme (Administration) (Scotland) Regulations 2008* (the administration regulations). Paragraph 8 of part 1 of the guidance recommends that the management commentary required by the accounts regulations should meet both sets of requirements.

73. Guidance on auditors' responsibilities for the management commentary is provided at paragraphs 205 to 213 of note for guidance 2014/13(LA). The issue of this finance circular supersedes paragraph 206.

74. The accounts regulations also introduce the requirement for the annual accounts to include an annual governance statement, while the administration regulations continue to require the inclusion of a governance compliance statement. Paragraph 13 of part one recommends that an administering authority includes either

- a single governance statement with two sections, with the first being the annual governance statement, and the second the governance compliance statement; or
- two separate statements, with the annual governance statement followed immediately by the governance compliance statement.

75. Guidance on auditors' responsibilities for the annual governance statement and governance compliance statement is provided at paragraphs 214 to 232 of note for guidance 2014/13(LA). The issue of this finance circular supersedes paragraph 217.

76. The accounts regulations set out the signatories to the various statements required to be included in the annual accounts. For pension funds, paragraph 5 of part 1 considers that the convenor of the pension committee should be nominated to sign the relevant statements instead of the Leader of the Council.

77. Auditors should refer to this guidance when auditing the 2014/15 annual accounts.

Guide on new pension flexibilities

78. The Local Government Pension Scheme (LGPS) has issued a guide to provide information on reforms to workplace pensions from 6 April 2015. The reforms offer greater flexibility (referred to as *Freedom and choice*) in the way individuals over 55 can access their defined contribution (DC) pension savings. Members of DC schemes have the flexibility to purchase an annuity or take cash sums, either at different stages or all at one time.

79. The new flexibilities do not apply to the LGPS. However, some indirect changes impact upon any members of the LGPS who are considering transferring the value of their accrued LGPS pension rights to a DC arrangement offering 'flexible benefits'.

80. Any member wanting to transfer to a DC arrangement is required to obtain appropriate advice from an authorised independent adviser. Where the number of transfers may result in a risk to the LGPS pension fund, the amount of the transfer value can be reduced.

Auditing developments

2014/15 model independent auditor's reports

81. The TSU has issued 2014/15 Independent auditor's report (local authorities) - technical guidance note 2015/3(LA) to provide auditors with the model independent auditor's reports which should be used for the 2014/15 annual accounts of local authorities. The technical guidance note also provides application guidance on their use.

82. In the interests of consistency, auditors are required to use the model wording in the appendices to the technical guidance note as a condition of their audit appointment. The only exception is any amendments required to tailor the terminology to reflect local circumstances. It should be noted that the requirement to follow the model wording in the appendices applies to the 'Bannerman' paragraph. The previous dispensation which allowed minor wording changes no longer applies from 2014/15.

83. Any proposed modifications to any audit opinion or conclusion in the model reports, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with the TSU in advance of finalising the report.

84. Auditors should use this technical guidance note when reporting on 2014/15 audits. They should complete the checklist at Appendix 4 which provides a list of the key auditor actions.

Other developments

Whole of government accounts

2014/15 guidance for preparers

85. The Scottish Government has emailed Scottish local authorities to advise that they should follow guidance from the Treasury when completing their 2014/15 data collection templates (DCTs) for whole of government accounts (WGA).

86. WGA guidance for local authorities (England) on completing the 2014/15 DCT pack explains that WGA bodies are required to submit a cycle 1 DCT (before review by auditors) and a cycle 2 DCT (after auditors' review). The cycle 2 DCT is the cycle 1 version updated for audit adjustments and CPID corrections.

87. The Scottish Government has agreed different submission deadlines to those set out in the Treasury guidance. Local authorities are required to submit

- a locked cycle 1 DCT to their auditor and to the Scottish Government by 24 July
- a locked cycle 2 DCT to the Scottish Government by 30 September 2015.

88. Auditors should refer to this guidance when reviewing the 2014/15 DCTs of local authorities.

2014/15 guidance for auditors

89. The TSU has published Auditor assurance on 2014/15 WGA returns (local authorities) - technical guidance note 2015/4(LA) to provide guidance on the review of the 2014/15 WGA DCTs. The approach set out in the technical guidance note has been agreed with the National Audit Office (NAO), who have responsibility for the overall audit approach to WGA in the UK, and is based on their group audit instructions.

90. The NAO has prescribed a threshold for auditor review. A review is required where either gross assets (excluding property, plant and equipment, heritage assets, intangibles, investment properties, and assets held for sale), or gross liabilities (excluding pension liabilities), or gross income or gross expenditure is above £350 million.

91. No testing is required for bodies below the threshold but, in a change from previous years, auditors are required to complete the first section of the assurance statement and submit it to the NAO.

92. Auditors of local authorities over the threshold are responsible for

- planning the review of the DCTs and arranging timetables for completion of the work within the required timeframes
- completing the appropriate test procedures (see sections 4 and 5)

- making judgements on the accuracy of the information within the DCT, and obtaining the authority's agreement regarding any adjustments that are required (see section 6)
- reporting the results on completion of the review in an assurance statement submitted to the NAO.

93. Auditors should expect to receive the draft DCT by 24 July 2015. Auditors should follow the guidance in the technical guidance note when reviewing the DCTs. Action that auditors are required to undertake is included at sections 4 to 6. Actions include initial gateway tests, fieldwork tests, and required completion procedures. They are summarised in an auditor action checklist at Appendix 1 which auditors should complete.

94. Auditors should plan to lock the DCT and pass it to the authority and submit it to the NAO by 30 September 2015.

Housing benefits

Guidance on certifying 2014/15 subsidy claims

95. The TSU has published Auditor certification of the 2014/15 housing benefit subsidy claim – technical guidance note GN/HBS/15 to provide guidance to auditors on certifying 2014/15 housing benefit (HB) subsidy claims.

96. Auditors should follow this technical guidance note when reviewing and reporting on 2014/15 HB subsidy claims.

2014/15 HB COUNT

97. The Audit Commission has issued Module 5 of the 2014/15 HB COUNT which is the software diagnostic tool.

98. The module contains a control matrix that requires to be completed by auditors when certifying 2014/15 HB subsidy claims.

Subsidy claims best practice guide

99. The Department for Work and Pensions (DWP) has issued a best practice guide on the preparation of HB subsidy claims. The Housing benefit subsidy claims- local authority best practice guide provides details of practices councils may adopt across seven error categories including overpayment misclassification, reconciliations, overpaid/underpaid benefits and auditor certification. The guide also includes a section on good practice identified by auditors during the certification process.

Overpayments guide 2015

100. The DWP has issued a revised Housing benefit overpayment guide 2015 to provide guidance on overpayments of HB. Overpayment is defined in the guide as an amount of HB which has been paid to a claimant to which there was no entitlement.

101. Part 2 explains that an overpayment is recoverable normally when the claimant either caused or contributed to the mistake or could reasonably have been expected to realise they were being overpaid. Even if an overpayment is deemed recoverable, a council does not have to recover it.

102. Auditors should refer to this guide when certifying the 2014/15 HB subsidy claim.

Impact of pension flexibilities

103. The DWP has issued further guidance on how the greater flexibility introduced to the pension system from 6 April 2015 explained at paragraph 78 will impact on HB claims.

104. HB circular A7/2015 Pension flexibilities – further guidance advises that

- where a claimant takes either ad hoc withdrawals or the whole sum, the amounts withdrawn should be treated as capital
- where amounts are withdrawn on a regular basis, they should be treated as income.

105. If the claimant is of pension credit qualifying age, notional income equivalent to 100% of the annuity should be assumed. Where the claimant also withdraws income, the higher of the notional income or actual amount withdrawn should be treated as income.

Funding

106. The DWP has issued the following circulars announcing various funding for local authorities

- HB circular S2/2015 New burdens payment for real time information bulk data matching initiative provides details of funding in order to action *Real time information* referrals, which matches HB claimant details against HM Revenues and Customs data to identify cases where claimants have under-declared income.
- HB circular S3/2015 Fraud and error reduction incentive scheme 2015/16 funding and HB General information bulletin G5/2015 set out details of *Fraud and error reduction incentive scheme* funding in 2015/16.
- HB circular S4/2015 Additional funding to meet the costs of implementing welfare reform changes in 2015/16 announces additional funding to support the costs of implementing welfare reform changes in 2015/16.
- HB circular S5/2015 New burdens payment for migrant access to benefits announces funding to meet new burdens incurred by local authorities following restrictions to HB for European Economic Area nationals.

Finance

Government 2014/15 and 2015/16 funding

107. The Scottish Government has issued a circular to provide a summary of the general revenue grant (GRG) and distributable non domestic rates income (NDRI) for 2015/16 set out in The Local Government Finance (Scotland) Amendment Order 2015.

108. Annex B of Finance circular 2/2015 Local government finance amendment order 2015 sets out the distribution of the total revenue funding allocation between councils and the allocation of the different elements for each council for 2015/16.

109. Annex D sets out the final distribution of the total revenue funding allocation between councils and the allocation of the different elements for each council for 2014/15. Individual local authority changes are set out in Annex E.

110. Auditors should refer to this circular when testing funding figures in the 2014/15 annual accounts.

Community charge debt

111. The Community Charge Debt (Scotland) Act 2015 has been passed to extinguish all community charge liabilities, including civil penalties, interest and surcharges, on 1 February 2015. Summary warrants and decrees became unenforceable on that date.

112. Auditors should refer to this Act when auditing the council tax income account as part of the audit of the 2014/15 annual accounts.

Integration joint boards

Guidance on finance matters

113. The Scottish Government has issued guidance on financial matters in respect of the implementation of health and social care integration. *Health and social care integration finance guidance* explains that integration joint boards (IJBs) are legal entities that fall within section 106 of the *Local Government (Scotland) Act 1973*. They are therefore required to produce annual accounts in accordance with the accounting code and accounts regulations, which will be audited by auditors appointed by the Accounts Commission.

114. Annual accounts will be required for 2015/16 regardless of the date of commencement of joint service delivery where the IJB has reportable transactions, e.g. operating costs. A set of illustrative financial statements is included in the guidance. IJB annual accounts will be expected to present

- gross local authority and health contributions
- IJB operating costs, which will include the cost of support services provided by the partners
- the cost of any commissioned services.

115. It is anticipated that local authorities and health boards will include financial information regarding the IJB in their annual accounts. The necessary information will be required by a mutually agreed date that allows health boards to meet their statutory obligations.

116. The guidance advises that where an IJB comprises one local authority and one health board *IFRS 11 Joint arrangements* will apply on the assumption that 'joint control' exists. The presumed default classification of an IJB is a joint venture.

117. Auditors should refer to this guidance when considering the arrangements for health and social care integration.

Revised guidance for integration financial assurance

118. Technical bulletin 2015/1 (paragraph 85) advised that the Scottish Government had issued guidance on providing assurance that an IJB will receive adequate resources to carry out its functions. The guidance recommended that, until IJBs are established, the local authority (and health board) internal auditor should report to the respective audit committees on the assurance process that has been carried out by the partners.

119. The Scottish Government has issued revised *Guidance for integration financial assurance* which requires the arrangements for obtaining assurance to be set out in the governance statements of the local authority and IJB (and health board) for the year prior to and the year of the delegation of functions and resources.

120. Auditors should refer to this guidance when considering the financial assurance arrangements for integration and confirm they are set out in the 2014/15 governance statement.

Treasury management

Audit Scotland report

121. The Accounts Commission has issued a report on Borrowing and treasury management in councils. The report was prepared by Audit Scotland and focuses on whether councils openly and clearly demonstrate the affordability and sustainability of borrowing decisions over the term of the borrowing. It also looks at whether councils' approach to borrowing, as outlined in their treasury management strategy, reflects their corporate priorities and aims.

122. Councillors have a key role in holding officers to account and the report evaluates the councillor's role in considering borrowing and treasury management reports.

123. Key messages include the following

- Councils are following the general principles of the relevant codes of practice in demonstrating short-term affordability (i.e. the next couple of years), but they are not always highlighting the strategic importance of borrowing and treasury management or clearly analysing and reporting the long-term affordability and sustainability of their borrowing.
- Councils need to develop detailed analysis to support borrowing decisions and to demonstrate they represent best value for the council.
- Councils need to improve scrutiny of borrowing and treasury management. This is a complex and technical subject and officers need to provide wider training and support to councillors, and also provide clearer, more accessible reports.
- The current governance structures in some councils could be improved to support more effective scrutiny.

Grant claims

2014/15 guidance for auditors

124. The TSU has issued Certification of 2014/15 approved local authority grant claims and returns - Technical guidance note GN/GEN/15 to provide general guidance to auditors on the certification of 2014/15 local authority grant claims and returns and to explain the approach and procedures to be adopted. The technical guidance note

- explains the arrangements for the certification of grant claims and other returns
- provides a list of grant claims and other returns which external auditors are required to certify in 2014/15 under their audit appointment
- considers the roles and responsibilities of grant-paying bodies, local authorities, the TSU and appointed auditors
- sets out the overall approach to be adopted by auditors
- provides guidance on auditor reporting.

125. The TSU also separately publishes a technical guidance note on each significant approved claim to provide auditors with specific guidance on certifying that claim. In addition to Auditor certification of the 2014/15 housing benefit subsidy claim - Technical guidance note GN/HBS/15 referred to at paragraph 95, the following have been published for 2014/15

- Auditor certification of the 2014/15 safety camera programme grant claims - Technical guidance note GN/FPN/15
- Auditor certification of the 2014/15 education maintenance allowance grant claims - Technical guidance note GN/EMA/15
- Auditor certification of the 2014/15 Bellwin scheme claims - Technical guidance note GN/BEL/15
- Auditor certification of the 2014/15 criminal justice social work services financial returns - Technical guidance note GN/CJS/15.

126. Auditors should follow these technical guidance notes when reviewing and reporting on 2014/15 grant claims.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 24 in respect of the bulletin from CIPFA on the 2014/15 financial statements?			
2 Have you carried out the action recommended at paragraph 52 in respect of the arrangements for measuring highways infrastructure assets?			
3 Have you carried out the action recommended at paragraph 61 in respect of the statutory guidance on equal pay and severance costs?			
4 Have you carried out the action recommended at paragraph 70 in respect of the guidance on the management commentary?			
5 Have you carried out the action recommended at paragraph 77 in respect of the guidance on pension funds?			
6 Have you carried out the action required at paragraph 84 in respect of the 2014/15 independent auditor's report?			
7 Have you carried out the action recommended at paragraph 93 in respect of reviewing 2014/15 WGA DCTs?			
8 Have you carried out the action required at paragraph 96 in respect of reviewing 2014/15 HB subsidy claims?			
9 Have you carried out the action recommended at paragraph 110 in respect of government funding?			
10 Have you carried out the action recommended at paragraph 112 in respect of community charge debt?			
11 Have you carried out the action recommended at paragraph 117 in respect of health and social care integration?			

	Yes/No/N/A	Initials/date	W/P ref
12 Have you carried out the action recommended at paragraph 120 in respect of the 2014/15 governance statement?			
13 Have you carried out the action required at paragraph 126 in respect of reviewing 2014/15 grant claims?			

TSU contacts for local authority chapter

127. The contacts in the TSU for this chapter are

- Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or pobrien@audit-scotland.gov.uk.
- Tim Bridle, Manager - Local Government (Technical) - 0131 625 1793 or tbridle@audit-scotland.gov.uk.
- Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or acairns@audit-scotland.gov.uk (for housing benefit).

Central government chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks that are relevant to the central government sector.

It should be read by external auditors with appointments in the central government sector. It should also be read by auditors with appointments in the health sector and further education sector as most of the articles also apply to those sectors. Auditors should also read the cross-sectoral chapter.

Guidance from TSU on emerging risks

Status of non-executive members

128. The TSU has become aware of a potential emerging risk in respect of the employment status of non-executive members of public bodies.

129. The Public sector pay policy for senior appointments technical guide states that chairs and board members are not employees and do not receive a salary. It recommends that care is taken in drafting letters of appointment to avoid references to salary or employment, as there may be tax and other implications.

130. However, the Scottish public finance manual (SPFM) requires chairs and members who qualify as 'employees' for tax purposes to be paid their fees through the payroll system with tax deducted at source.

131. The TSU understands that HM Revenue and Customs has advised a public body that statutory maternity pay is payable in respect of an non-executive board member as they hold the office of a member of a public body and this meets the definition of an employee under the *Social Security Contributions and Benefits Act 1992*.

132. The TSU has raised this issue with the Scottish Government Pay Policy Unit and is awaiting a response. Further guidance will be provided in due course.

Summary financial information in NAO disclosure checklist

133. The TSU has identified that the section of the 2014/15 FReM disclosure checklist on summary financial information issued by the National Audit Office (NAO) does not appear to reflect The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013.

134. The 2013 regulations amended section 426 of the *Companies Act 2006.* As explained in technical bulletin 2014/2 (paragraph 216), paragraph 5.1.7 of the *Government financial reporting manual* (FReM) states that a body that wishes to publish a separate annual report additional to its annual report and accounts that it describes as containing summary financial

information should comply with the requirements of section 426. The 2013 regulations replaced the previous references to summary financial information in section 426 with a requirement for a copy of the strategic report. The TSU has raised this issue with the NAO.

135. Auditors should refer to the guidance at paragraphs 356 to 365 of note for guidance 2015/1(CG) in respect of the required disclosures and audit requirements.

Accounting developments

General accounting

Guidance on IFRS not yet effective

136. HM Treasury has issued a guide to new international financial reporting standards (IFRS) that have been issued but are not yet effective in 2014/15, and therefore require disclosure in accordance with *IAS 8 Accounting policies, changes in accounting estimates and errors*.

137. Review of new IFRS issued and/or effective during the 2014/15 clarifies that the standards that have been issued but are not yet effective are

- *IFRS 13 Fair value measurement* which has been issued to provide consistent guidance on fair value measurement. As explained in technical bulletin 2015/1 (at paragraph 102), it will be included in the 2015/16 FReM without adaptation. However, adaptations to other standards limit the circumstances in which a valuation is required under IFRS 13.
- *IAS 36 Impairment of assets on recoverable amount disclosures (amendment)* modifies some of the disclosure requirements regarding measurement of the recoverable amount of impaired assets. It is also expected to apply from 2015/16.

138. Auditors should consider this guide when auditing the disclosure of standards issued but not yet effective in the 2014/15 annual accounts.

139. The guide also provides information on standards under development. Treasury has recently began assessing the impact on the public sector of the following standards

- *IFRS 15 Revenue from contracts with customers* which establishes the application principles required for entities to report useful information on the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers. It is expected to be included in the 2017/18 FReM.
- *IFRS 9 Financial instruments* which applies a single classification and measurement approach to all financial assets, and is expected to be included in the 2018/19 FReM.

Remuneration report

Preparation guidance for 2014/15

140. The Cabinet Office has issued EPN 430 2014/15 Disclosure of salary, pension and compensation information to provide guidance on the preparation of a remuneration report for 2014/15. An example remuneration report is provided at Annex 13C.

141. Remuneration reports are required to disclose

- information on the pay and pension packages of the senior management team
- the median remuneration of all staff and the ratio between this and the mid-point of the banded remuneration of the highest paid director
- the number of exit packages for all staff by cost band, broken down by the number of compulsory redundancies and the number of other departures agreed
- compensation payments made to senior management.

142. Changes to the disclosures required for pensions from 2014/15 are as follows

- If a member has a preserved award from a previous civil service employment that they have not opted to aggregate with the pension from their current service, this should not be included in the disclosure.
- Where a member has opted out of the scheme for the whole year, no pension figure should be disclosed and a footnote should be added noting that fact.
- If a member's pension has been subject to a pension sharing order on divorce, the gross pension should be included in the disclosure.

143. Auditors should refer to this guidance when auditing the remuneration report in the 2014/15 annual report and accounts.

Auditing developments

2014/15 model independent auditor's reports

144. The TSU has issued 2014/15 Independent auditor's report (central government) - technical guidance note 2015/2(CG) to provide auditors with the model independent auditor's reports which should be used for the 2014/15 annual accounts. The technical guidance note also provides application guidance on their use.

145. In the interests of consistency, auditors are required to use the model wording in the appendices to the technical guidance note as a condition of their audit appointment. The only exception is any amendments required to tailor the terminology to reflect local circumstances. It should be noted that the requirement to follow the model wording in the appendices applies to the 'Bannerman' paragraph. The previous dispensation which allowed minor wording changes no longer applies from 2014/15.

146. Any proposed modifications to any audit opinion or conclusion in the model reports, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with the TSU in advance of finalising the report.

147. Auditors should use this technical guidance note when reporting on 2014/15 audits. They should complete the checklist at Appendix 6 which provides a list of the key auditor actions.

Corporate governance developments

Revised guidance for board members

148. The Scottish Government has published a revised edition of On board – a guide for board members of public bodies in Scotland which provides information on the role of board members in public bodies in Scotland. The guidance applies to non-departmental public bodies, although board members of other bodies may find sections of the guidance helpful.

149. The main changes to the guide are to reflect developments since the previous edition such as recent revisions to the *Model code of conduct for members of devolved public bodies*. There is a new annex on induction guidance and training.

150. Section 2 of the guide covers the principles of corporate governance and how these translate into the conduct and management of public business. It is referred to in the SPFM as relevant guidance when assessing corporate governance for the purposes of the governance statement.

151. Auditors should consider this guidance when reviewing the 2014/15 governance statement.

Other developments

Whole of government accounts

2014/15 guidance for preparers

152. The Scottish Government has emailed Scottish central government bodies to advise that they should follow guidance from the Treasury when completing their 2014/15 data collection templates (DCTs) for whole of government accounts (WGA).

153. Guidance to the whole of government accounts - year ended 31 March 2015 from the Treasury explains that WGA bodies are required to submit a cycle 1 DCT (before review by auditors) and a cycle 2 DCT (after auditors' review). The cycle 2 DCT is the cycle 1 version updated for audit adjustments and CPID corrections.

154. The Scottish Government has agreed different submission deadlines to those set out in the Treasury guidance. Bodies are required to submit

- a locked cycle 1 DCT to their auditor and to the Scottish Government by 24 July
- a locked cycle 2 DCT to the Scottish Government by 30 September 2015.

155. Auditors should refer to this guidance when reviewing the 2014/15 DCTs.

2014/15 guidance for auditors

156. The TSU has published Auditor assurance on 2014/15 WGA returns (central government) - technical guidance note 2015/5(CG) to provide guidance on the review of the 2014/15 WGA DCTs. The approach set out in the technical guidance note has been agreed with the

National Audit Office (NAO), who have responsibility for the overall audit approach to WGA in the UK, and is based on their group audit instructions.

157. The NAO has prescribed a threshold for auditor review. A review is required where either gross assets (excluding property, plant and equipment, heritage assets, intangibles, investment properties, and assets held for sale), or gross liabilities (excluding pension liabilities), or gross income or gross expenditure is above £350 million.

158. No testing is required for bodies below the threshold but, in a change from previous years, auditors are required to complete the first section of the assurance statement and submit it to the NAO.

159. Auditors of bodies over the threshold are responsible for

- planning the review of the DCTs and arranging timetables for completion of the work within the required timeframes
- completing the appropriate test procedures (see sections 4 and 5)
- making judgements on the accuracy of the information within the DCT, and obtaining the body's agreement regarding any adjustments that are required (see section 6)
- reporting the results on completion of the review in an assurance statement submitted to the NAO

160. Auditors should expect to receive the draft DCT by 24 July 2015. Auditors should follow the guidance in the technical guidance note when reviewing the DCTs. Action that auditors are required to undertake is included at sections 4 to 6. Actions include initial gateway tests, fieldwork tests, and required completion procedures. They are summarised in an auditor action checklist at Appendix 1 which auditors should complete.

161. Auditors should plan to lock the DCT and pass it to the body and submit it to the NAO by 30 September 2015.

Budgeting

2015/16 budgeting guidance

162. HM Treasury has issued Consolidated budgeting guidance on accounting for budgets in the *National accounts* for 2015/16. The *National accounts* are prepared in accordance with the internationally agreed framework *European system of accounts 2010*, and are the responsibility of the Office for National Statistics.

163. The *National accounts* treat some transactions differently from the financial statements as budgets have different objectives.

164. The main changes in the guidance from 2014/15 are

- the guidance on impairments in chapter 3 has been updated to better align descriptions and terminology with the FReM

- the guidance on pensions in chapter 12 has been updated to provide clarity on the budgeting treatment of the various pension schemes.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action required at paragraph 135 in respect of summary financial information?			
2 Have you carried out the action recommended at paragraph 138 in respect of standards issued not yet effective?			
3 Have you carried out the action recommended at paragraph 143 in respect of the 2014/15 remuneration report guidance?			
4 Have you carried out the action required at paragraph 147 in respect of the 2014/15 independent auditor's report?			
5 Have you carried out the action recommended at paragraph 151 in respect of the 2014/15 governance statement?			
6 Have you carried out the action required at paragraph 160 in respect of reviewing 2014/15 WGA DCTs?			

TSU contacts for central government chapter

165. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or ncameron@audit-scotland.gov.uk.
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Health chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that affect the health sector.

It should be read by external auditors with appointments in the health sector. Auditors should also read the central government chapter and cross-sectoral chapter.

Accounting developments

Provisions

Further guidance on clinical negligence claims in 2014/15

166. Technical bulletin 2015/1 (paragraph 151) advised that the Scottish Government Health and Social Care Directorates (SGHSCD) had issued guidance on the revised accounting treatment and presentation of the *Clinical negligence and other risks indemnity scheme* (CNORIS) from 2014/15.

167. The SGHSCD has subsequently issued further guidance on the required retrospective restatement which sets out standard wording to be disclosed in the affected notes under IAS 8.

168. The SGHSCD undertook an exercise to identify the amount of the restatement required for 2012/13 and 2013/14. The amounts that apply to each board are included at Appendix B and are based on the CNORIS contribution rates advised by the NHS Central Legal Office.

169. The TSU has reviewed the work that the SGHSCD undertook to provide the figures for the provision. There were no issues identified in respect of the methodology followed or the amounts provided.

170. Auditors should refer to this guidance when auditing the CNORIS provision in the 2014/15 financial statements.

Guidance on equal pay

171. The SGHSCD has issued a letter advising boards to recognise a provision for equal pay in 2014/15. Boards will be advised separately of the amount to be recognised, and funding will be provided.

172. The letter sets out a form of wording that should be disclosed in the provisions note, i.e. other provisions include an amount of £x in respect of the board's estimated liability arising from equal pay claims.

173. Auditors should refer to this guidance when auditing provisions in the 2014/15 annual accounts.

Auditing developments

2014/15 model independent auditor's reports

174. The TSU has issued 2014/15 Independent auditor's report (health) - technical guidance note 2015/1(H) to provide auditors with the model independent auditor's reports which should be used for the 2014/15 annual accounts. The technical guidance note also provides application guidance on their use.

175. In the interests of consistency, auditors are required to use the model wording in the appendices to the technical guidance note as a condition of their audit appointment. The only exception is any amendments required to tailor the terminology to reflect local circumstances. It should be noted that the requirement to follow the model wording in the appendices applies to the 'Bannerman' paragraph. The previous dispensation which allowed minor wording changes no longer applies from 2014/15.

176. Any proposed modifications to any audit opinion or conclusion in the model reports, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with the TSU in advance of finalising the report.

177. Auditors should use this technical guidance note when reporting on the audit of the 2014/15 annual reports and accounts. They should complete the checklist at Appendix 3 which provides a list of the key auditor actions.

Other developments

Planning and performance management

Revised guidance on separate annual report

178. The SGHSD has issued a letter to update existing guidance on the required content of the separately published annual reports from 2014/15. The guidance required the inclusion of summary financial information in the separate annual report which consequently required an auditor's statement as to whether the information was consistent with the board's full financial statements.

179. As a result of changes to the *Companies Act 2006* explained at paragraph 134, the inclusion of summary financial information would have required the report to include a copy of the strategic report.

180. The letter therefore amends the guidance by removing the expectation that financial information should be included in the separate annual report. This would mean that a strategic report would not be required, there would be no auditor involvement with the separate annual report, and the report could be published in advance of the annual accounts being laid in Parliament.

181. Auditors should confirm that their boards do not include summary financial information in their separate annual report from 2014/15. However, paragraphs 411 to 419 of note for guidance 2015/3(H) provide guidance for auditors in cases where boards nevertheless choose to continue to include summary financial information.

Pay and workforce planning

2014/15 executive and senior management pay arrangements

182. The SGHSCD has issued a circular announcing the mandatory executive and senior management pay arrangements for 2014/15. PCS(ESM)(2015)1 advises that the minimum and maximum point of pay ranges for grades A to I have been increased by 1%. The pay ranges are set out at paragraph 1 of the schedule to the direction that accompanies the circular.

183. All staff grade A to I will receive the uplift, unless performance is rated as unacceptable.

184. The consolidated pay progression should be applied with effect from 1 April 2014, based on 2013/14 performance. Employees will not receive more than the maximum consolidated salary for their pay range. The increases based on individual manager's performance are set out at paragraph 4 of Schedule 1.

Social care integration

Guidance on finance matters

185. The Scottish Government has issued guidance on financial matters in respect of the implementation of health and social care integration. It is anticipated that health boards will include financial information regarding the IJB in their annual accounts. The necessary information will be required by a mutually agreed date that allows boards to meet their statutory obligations.

186. The guidance advises that where an integration joint board (IJB) comprises one local authority and one health board *IFRS 11 Joint arrangements* will apply on the assumption that 'joint control' exists. The presumed default classification of an IJB is a joint venture.

187. Auditors should refer to this guidance when considering the arrangements for health and social care integration.

Revised guidance on integration financial assurance

188. Technical bulletin 2015/1 (paragraph 85) advised that the Scottish Government had issued guidance on providing assurance that an IJB will receive adequate resources to carry out its functions. The guidance recommended that, until IJBs are established, the health board (and local authority) internal auditor should report to the respective audit committees on the assurance process that has been carried out by the partners.

189. The Scottish Government has issued revised *Guidance for integration financial assurance* which requires the arrangements for obtaining assurance to be set out in the governance

statements of the health board and IJB (and local authority) for the year prior to and the year of the delegation of functions and resources.

190. Auditors should refer to this guidance when considering the financial assurance arrangements for integration and confirm they are set out in the 2014/15 governance statement.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action requested at paragraph 170 in respect of CNORIS provisions?			
2 Have you carried out the actions requested at paragraph 173 in respect of equal pay?			
3 Have you carried out the action required at paragraph 177 in respect of the 2014/15 independent auditor's report?			
4 Have you carried out the action required at paragraph 181 in respect of the separate 2014/15 annual report?			
5 Have you carried out the actions requested at paragraphs 187 and 190 in respect of health and social care integration?			

TSU contacts for health chapter

191. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or ncameron@audit-scotland.gov.uk.
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Further education chapter

Introduction

This chapter contains technical developments and guidance on emerging risks in the quarter that are relevant to further education colleges.

It should be read by external auditors with appointments in the further education sector. Auditors should also read the central government chapter and the cross-sectoral chapter.

Accounting developments

Update on review of resource returns

192. Technical bulletin 2015/1 (paragraph 177) advised that a briefing note from Colleges Scotland had proposed that the resource returns at 31 March (which are required to monitor how funding was spent) should be reviewed by external auditors to provide assurance on the financial information contained in the returns.

193. The Scottish Funding Council (SFC) has subsequently advised the TSU that a review will not be required for 2014/15. Guidance on the position for future years will be provided in due course.

Change of financial year end

194. The Colleges of Further Education (Financial Year)(Scotland) Order 2015 has moved the financial year end of colleges back to 31 July.

195. As the financial year end for 2013/14 was 31 March, the order states that the financial year for 2014/15 covers the period from 1 April 2014 to 31 July 2015.

Auditing developments

Audit Scotland report on colleges

196. The Auditor General has issued a report that comments on the various reforms underway in the sector, and provides an update on its financial standing. Scotland's colleges 2015 was prepared by Audit Scotland and key messages include the following

- Planning for mergers was generally good and all of the merged colleges were established on time.
- While mergers have contributed to significant efficiency savings, the Scottish Government and the SFC have not specified how they will measure some of the expected wider benefits.
- Colleges transferred £99 million to arm's-length independent foundations in 2013/14.

- While most severance was managed in accordance with good practice, auditors found significant weaknesses in how two colleges processed senior staff severance payments, while another four fell short of good practice.

Other developments

Finance

Use of depreciation funding in 2014/15

197. Technical bulletin 2015/1 (paragraph 189) advised that the SFC had issued guidance on the release of funding, previously earmarked for depreciation, for other purposes in 2014/15. The SFC has subsequently issued a letter to colleges responding to concerns about the governance implications of following the guidance, particularly where this results in a deficit in the 2014/15 accounts.

198. The letter confirms that the SFC will treat any deficit as a technical deficit for financial monitoring purposes, as it does not represent a risk to a college's financial sustainability. The position will be communicated to stakeholders to minimise the risk of a deficit being misinterpreted.

199. A standard form of words is being developed for affected colleges to explain the position in their 2014/15 annual accounts.

TSU contact for further education chapter

200. The contact in the TSU for this chapter is Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Technical Services Unit

Audit Scotland's Technical Services Unit (TSU) informs the professional judgement of appointed external auditors on technical matters and encourages the proper exercise of professional scepticism to improve the quality of the audit delivered to the Accounts Commission and Auditor General for Scotland. The TSU provides authoritative guidance and practical assistance to support appointed auditors in carrying out their responsibilities under the *Code of audit practice* to

- provide an opinion on audited bodies' financial statements and, where required, the regularity of transactions
- review and report on other information published with the financial statements, including governance statements and remuneration reports
- examine and report on approved grant claims and other returns submitted by local authorities
- review and report on whole of government accounts returns.

Contact details for relevant TSU staff are included at the end of each chapter.

Feedback on technical bulletins is encouraged and should be sent to

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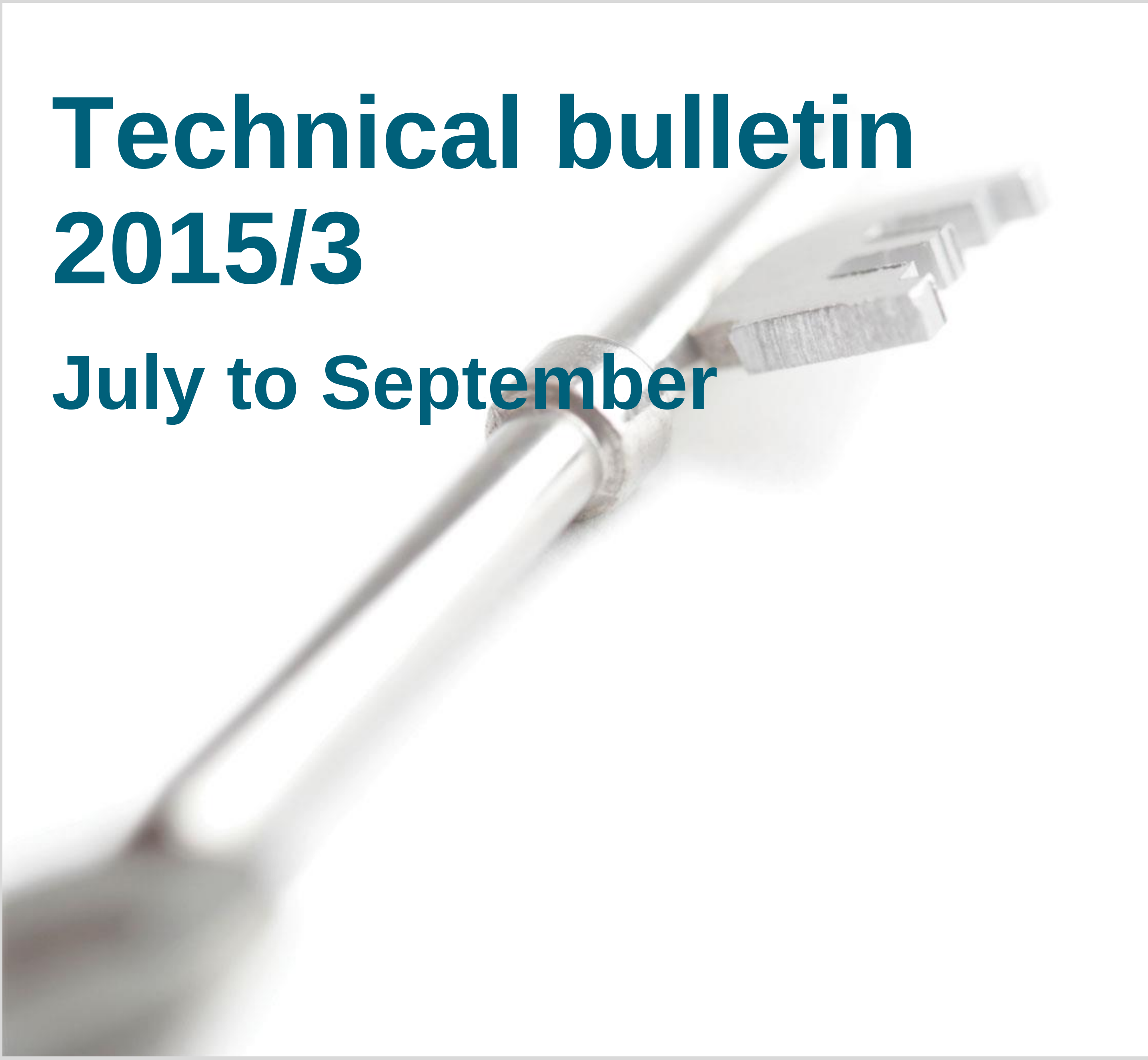

Prepared by the Technical Services Unit
11 September 2015

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

Foreword

Technical bulletins are prepared by Audit Scotland's Technical Services Unit (TSU), and approved by the Assistant Auditor General, to provide external auditors appointed by the Accounts Commission and Auditor General for Scotland with

- information on the main public sector technical developments in the quarter that are relevant to their audit appointment
- guidance from the TSU on any emerging risks identified in the quarter.

Technical bulletins are available to external auditors from Audit Scotland's *Technical reference library,* and published on the Audit Scotland website so that audited bodies and other stakeholders can access them.

It is important that auditors read this technical bulletin promptly so they are familiar with the information and guidance provided. The auditor action checklist section at the end of each chapter should be completed by a senior member of the audit team.

The articles on technical developments are intended to highlight the key points that the TSU considers external auditors require to be aware of. It may still be necessary for auditors to read the source material where greater detail is required. The documents referred to in the articles can be obtained by using the hyperlinks, where available. They are also available to external auditors from Audit Scotland's *Technical reference library*.

While auditors act independently, and are responsible for their own conclusions and opinions, the TSU has a role in ensuring that those conclusions and opinions are reached on the basis of informed judgement. Consistency in similar circumstances is important and **Audit Scotland's *Code of audit practice* therefore states that auditors should normally follow TSU guidance.** Auditors should advise the TSU promptly if they intend not to follow guidance provided in this technical bulletin on an emerging risk.

The TSU encourages feedback on this technical bulletin. Comments should be sent to pobrien@audit-scotland.gov.uk.

More in-depth and extensive guidance is provided in separate technical guidance notes published by the TSU. Technical guidance notes published in the quarter are referred to in this technical bulletin, and can be obtained by using the hyperlinks to the Audit Scotland website.

Headlines

This chapter provides brief headlines for the articles on technical developments and guidance in this technical bulletin, classified by the audit year to which it relates, and referenced to the paragraphs containing the main article.

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Local authority sector

Introduction

This chapter contains information on the main technical developments, and guidance from the TSU on any emerging risks, in the quarter that are relevant to the local authority sector.

It should be read by external auditors with appointments in the local authority sector.

Accounting developments

General accounting

Draft 2016/17 accounting code

1. The CIPFA/LASAAC Local Authority Code Board (CIPFA/LASAAC) has issued a consultation paper that sets out proposed amendments to the *2016/17 Code of practice on local authority accounting in the UK* (the draft code). It comprises an invitation to comment (ITC) as well as exposure drafts of the code (ED1 to ED 8) with the proposed amendments set out.

2. The main proposed amendments in the draft code are to reflect
   - the move to measuring the highways network asset at depreciated replacement cost (DRC) in accordance with the measurement methodologies specified in the *Code of practice on transport infrastructure assets* (the transport code)
   - a review of the pension funds section of the code
   - a number of narrow scope amendments to international financial reporting standards (IFRS)
   - the issue of the *Conceptual framework for general purpose financial reporting by public sector entities*
   - changes to legislation.

3. The ITC is also asking for comments on the application of *IFRS 9 Financial instruments* and *IFRS 15 Revenue recognition for contacts with customers* to future editions of the code.

4. The TSU will be preparing a response to the consultation on behalf of Audit Scotland. Auditors should advise the TSU if they have any comments on the proposals that they wish to be included in the response. Responses require to be submitted to code.responses@cipfa.org by 9 October 2015.

Highways network asset

5. The proposed amendments in respect of measuring the highways network asset at DRC are discussed at paragraphs 16 to 39 of the ITC and set out in ED 2. The proposed new requirements are included principally in a new section 4.11. There are also consequential

amendments to section 4.1 (on property, plant and equipment) which extend the current adaptation of *IAS 16 Property, plant and equipment* to withdraw the option to measure the carrying amount of the highways network asset at historical cost.

6. Paragraph 4.11.21 explains that the highways network asset comprises
   - carriageways including urban roads and rural roads
   - footways and cycletracks
   - structures including bridges, signs, retaining walls, and subways
   - street lighting
   - street furniture including traffic signs, safety fences, bollards, and bus shelters
   - traffic management systems including traffic signals, pedestrian signals, zebra crossings, and safety cameras
   - land.

7. It is proposed that the highways network asset should be treated as a single asset for financial reporting purposes, and presented as a separate class of assets on the face of the balance sheet.

8. Proposals include a requirement for annual depreciation of the highways network asset to be measured in accordance with the transport code which is different to the normal approach. The transport code requires annual depreciation to be calculated by estimating the aggregate cost of all the capital replacements/reinstatements needed to restore service potential over the life cycle, spread over the estimated number of years in the cycle.

9. Information on the condition of the asset is important in the calculation as it is used as a proxy for age in order to estimate accumulated depreciation. The actual deterioration of the asset between years is not compared to the annual depreciation. If the estimated age of the asset changes by more than expected, this would be treated as a revaluation movement rather than as a direct annual charge to the comprehensive income and expenditure statement (CIES).

10. This differs from the normal approach where changes in condition would be reflected in the formal revaluations and thus be included as part of a depreciation charge to the CIES. Further changes in condition would not be reflected until the next formal valuation unless indications of impairment exist.

11. There is also a proposed change to the normal treatment of accumulated depreciation and impairment. Local authorities normally follow the option in IAS 16 to eliminate accumulated depreciation and impairment when an asset is revalued. CIPFA/LASAAC considers that the information generated for the measurement of the highways network asset will be better presented following the option in IAS 16 where accumulated depreciation and impairment are adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account accumulated impairment losses.

12. There is a proposal (at paragraph 4.11.2.14) that the requirements for derecognition should follow the requirements of the accounting code for property, plant and equipment. In addition,

the cost of a replaced part (e.g. surface of a road) should be used as an estimate of the value of the part it has replaced. Authorities would be required to assume that on replacement the asset has reached the end of its useful life, unless they can demonstrate that this is not the case.

13. The change to DRC is a change in accounting policy which the ITC states will require full retrospective application. Local authorities will need to establish the difference between the depreciated historical cost for the highways network asset and the carrying amount at DRC from 1 April 2015. The exposure draft proposes a transitional approach at paragraph 4.11.2.16 which allows authorities to use any reasonable estimation process to split the depreciated historical cost of the original infrastructure class of assets between the residual infrastructure assets and the highways network asset.

Accounting and reporting by pension funds

14. CIPFA/LASAAC has carried out a review of the reporting requirements of section 6.5 of the code on the accounting and reporting of pension funds. The review was timed to coincide with the issue of the new *Financial reports of pension schemes - a statement of recommended practice 2015* (the 2015 pension SORP).

15. The proposed amendments arising from the review are discussed at paragraphs 40 to 57 of the ITC and set out in ED 3. They include

- changes at paragraph 6.5.3.6 to the fund account and net assets statement to reflect changes in the pension SORP, e.g. an updated analysis of investment income and investment assets, and new classifications for transfers from other pension funds and payments to and account of leavers
- the application of the disclosure requirements of *IFRS 13 Fair value measurement* to pension fund investments
- proposed recommended disclosure requirements at paragraph 6.5.5.1 v) in respect of management expenses. The disclosures are
  - the total amount of direct transaction costs of all significant asset classes (i.e. investment types) disclosed under the investments reconciliation table
  - an explanation of the nature of the transaction costs and how they arise.
- an annex that provides an overview of how the other sections of the code apply to pension funds.

Narrow scope amendments to IFRS

16. Proposed amendments to the code arising from narrow scope amendments to IFRS are discussed at paragraphs 58 to 89 and Appendix A of the ITC, and are set out in ED 1.

17. They include proposed amendments to

- paragraph 3.4.2.26 to clarify that an authority must not reduce the understandability of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions.

- paragraph 3.4.2.27 to clarify that materiality considerations still apply when a standard requires a specific disclosure including cases where the standard uses the term 'as a minimum'.
- paragraph 3.4.2.83 to give examples of ordering the notes to the financial statements systematically. These include
  - giving prominence to the areas of its activities that the authority considers to be most relevant to an understanding of its financial performance and financial position, such as grouping together information about particular activities
  - grouping together information about items measured similarly such as assets measured at current value
  - following the order of the line items in the CIES and the balance sheet.
- paragraph 3.4.2.60 to clarify that line items in the balance sheet may be disaggregated. It also been amended to require that any subtotals should be presented in accordance with paragraph 55A of *IAS 1 Presentation of financial statements*, i.e. the subtotals should
  - be comprised of line items made up of amounts recognised and measured in accordance with IFRS
  - be presented and labelled in a manner that makes the line items that constitute the subtotal clear and understandable
  - be consistent from period to period
  - not be displayed with more prominence than the sub-totals and totals required in IFRS.
- paragraph 3.4.2.90 to require authorities to disclose the factors that are used to identify the reportable operating segments when they have been aggregated.

18. ED 2 sets out the proposed amendment to paragraph 4.1.2.33 which removes the option to proportionately restate any accumulated depreciation or impairment at the date of valuing property, plant and equipment (other than for the highways network asset).

19. ED 4 sets out a proposed amendment to paragraph 3.9.2.7 that clarifies that a management entity that provides key management services to an authority is deemed to be a related party. The disclosure requirements for the amounts incurred by an authority for key management personnel services have been inserted in new paragraph 3.9.4.2.

Conceptual framework

20. The proposed amendments arising from the issue of the conceptual framework for public sector entities are discussed at paragraphs 90 to 96 of the ITC and set out in ED 6.

21. Amendments include paragraph 2.1.2.18 which states that
    - some complex economic phenomena are difficult to represent in local authority financial statements

- all efforts should be undertaken to represent the phenomena in a manner that is understandable to a wide range of users
- some users may need to seek the aid of an advisor to assist in understanding the phenomena
- information should not be excluded from financial statements solely because it may be too complex or difficult for some users to understand without assistance.

Changes to legislation

22. As a result of regulations that apply to English local authorities, the requirement in section 3.1 for an explanatory foreword has been replaced with the requirement for a narrative report. As Scottish authorities are required to produce a management commentary instead, this will not have a direct impact.

23. However, a separate concurrent consultation (covered at paragraph 24) is proposing the inclusion of a new funding analysis in the narrative report/management commentary.

Consultation on improving financial statements presentation

24. CIPFA/LASAAC has issued a consultation paper on proposed improvements to the presentation of local authority financial statements. The proposals are intended to reconnect the financial statements of authorities with the way in which they are organised and funded. *Telling the story - consultation on improving the presentation of local authority financial statements* comprises an ITC and separate appendices that illustrate the impact on the financial statements. ED 1 sets out the proposed changes to the accounting code.

25. Paragraphs 12 to 15 of the ITC and Appendix 7 consider a number of options for changes in the way local authority financial statements are presented. The preferred option proposed in the consultation paper is to introduce a requirement for a funding analysis to be included in the management commentary that provides a direct reconciliation between the CIES and amounts based on how local authorities are funded and budget. The funding analysis would be supported by a streamlined movement in reserves statement (MiRS) and replace the current segmental reporting note.

26. The TSU will be preparing a response to the consultation on behalf of Audit Scotland. Auditors should advise the TSU if they have any comments on the proposals that they wish to be included in the response. Responses require to be submitted to financial.reporting@cipfa.org by 9 October 2015.

Funding analysis

27. The funding analysis is discussed at paragraphs 16 to 23 of the consultation paper, with an exemplification provided in Appendix 2. The funding analysis brings together local authority performance reported on the basis of proper accounting practice with statutorily defined charges to the general fund, including the housing revenue account (HRA).

28. The funding analysis reconciles the CIES to

- the net expenditure chargeable to the general fund and HRA
- the statutory position on the general fund balance, which may then be split between the general fund and HRA balances. Views are sought, however, on whether a separate funding analysis should be provided for the HRA.

29. Appendix 3 illustrates an explanation of the nature of the adjustments between the funding analysis and the CIES.

30. It is proposed that the funding analysis should be included as a mandatory component of the management commentary. However, in order to meet the reporting requirements of *IFRS 8 Operating segments*, CIPFA/LASAAC considers the funding analysis should nevertheless be considered a part of the financial statements.

Comprehensive income and expenditure statement

31. The proposals in respect of the CIES are discussed at paragraphs 9 to 11 and 24 to 26 of the consultation paper, with an illustration at Appendix 4.

32. There are proposals that

- service information included in the net cost of services in the CIES should be presented in a format that is consistent with the organisational structure under which the authority operates and not the service expenditure analysis *in Service reporting code of practice* (SeRCOP)
- the costs of corporate departments treated as separate segments should be included on a direct cost basis rather than being apportioned to other services on the total cost basis set out in SeRCOP.

Movement in reserves statement

33. The proposals in respect of the MiRS are discussed at paragraphs 27 to 32 of the consultation paper, with an illustration at Appendix 5. The proposals include presenting the movements from the CIES on one line, i.e. total comprehensive income and expenditure.

34. There would remain the requirement for a line in the MiRS which includes the adjustments from income and expenditure charged under accounting requirements to that required by statutory funding requirements. Appendix 6 provides an illustration of the analysis of the adjustments that requires to be disclosed, making use of appropriate levels of aggregation.

Segmental analysis

35. Proposals regarding the segmental analysis are discussed at paragraphs 33 to 38 of the consultation paper. It is considered that generally the funding analysis and the CIES under the new proposals will meet the segmental analysis requirements of IFRS 8.

36. However, a proposed new code paragraph 3.4.2.42 is set out in ED 1 to meet the requirements of IAS 1 to disclose information regarding the nature of expenses.

Transitional arrangements

37. The consultation paper is seeking views on the timetable for changes to the code. Specifically, it asks whether

- the adoption should apply from the 2016/17 code
- early adoption should be permitted in 2015/16. If early adoption is permitted, it would need to be on a comprehensive basis rather than piecemeal.

Governance statements

Draft revisions to good governance framework

38. The CIPFA/SOLACE Joint Working Group on Good Governance in Local Government has issued a consultation paper on a revised draft framework for governance in local government. The draft framework in Delivering good governance in local government - consultation is based on the core principles and sub principles set out in the International framework: good governance in the public sector.

39. The principles from the international framework have been adapted for the local government context and translated into a series of expected behaviours and outcomes which demonstrate good governance in practice. The principles in the consultation draft are intended to form a shared understanding of what constitutes good governance across local government.

40. The draft framework includes the following two overarching principles for acting in the public interest

- Behaving with integrity, demonstrating strong commitment to ethical values, and respecting the rule of law.
- Ensuring openness and comprehensive stakeholder engagement.

41. In addition, achieving good governance in the local government also requires effective arrangements for

- defining outcomes in terms of sustainable economic, social, and environmental benefits
- determining the interventions necessary to optimize the achievement of the intended outcomes
- developing the authority's capacity, including the capability of its leadership and the individuals within it
- managing risks and performance through robust internal control and strong public financial management
- implementing good practices in transparency, reporting, and audit to deliver effective accountability.

42. Each local authority should be able to demonstrate that its governance structures are consistent with the core and supporting principles contained in this framework. It should therefore develop and maintain a local code of governance reflecting the behaviours and outcomes set out.

43. The TSU will be preparing a response to the consultation on behalf of Audit Scotland. Auditors should advise the TSU if they have any comments on the proposals that they wish to be included in the response. Responses should be submitted to kerry.ace@cipfa.org by 28 September 2015.

New guidance on financial management of self-directed support

44. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued guidance on the financial management of self-directed support (SDS) for social care. Under SDS, local authorities are responsible for developing an appropriate support plan based on how each person wishes to receive support and the estimated cost of securing it. The guidance is in three parts

- Part I provides an overview of SDS
- Part II identifies the financial management implications arising from SDS
- Part III provides a self-evaluation framework.

45. Support options under SDS include

- the local authority making direct payment to the supported person
- either the local authority or the supported person selecting the support, and the authority making the arrangements for the provision of it.

46. A central financial management aspect of SDS is the need for an authority to determine the amount (referred to as the relevant amount) that it considers is a reasonable estimate of the cost of securing the provision of support. There is no set specified method that must be used for determining the relevant amount, and authorities are expected to develop an appropriate methodology.

47. Authorities should undertake regular verification of the relevant amount calculation to ensure that it is reliable and the factors affecting actual costs incurred are reflected in the calculation. The table at paragraph 43 of part II of the guidance outlines a potential approach.

48. Financial management monitoring arrangements are described in this guidance as obtaining evidence that the relevant amount has been used for the intended service purpose. The arrangements should be proportionate and appropriate to the risks to which public resources are exposed to.

49. There a number of financial management risks arising under SDS, and the following are discussed as paragraphs 110 to 144 of part II

- demand forecasting
- cost information
- budget methodology
- financial failure of third parties
- the supported person from fraud and corruption
- authorisation of payments.

50. Auditors should refer to this guidance when considering the financial management of self-directed support.

Pension funds

New framework for pension board members

51. CIPFA has issued a framework that sets out the knowledge and skills required for public service pension schemes' pension board members. The objectives of the *Local pension boards - a technical knowledge and skills framework* are to

- improve the knowledge and skills in all the relevant areas of activity of a pension board
- assist board members in achieving the degree of knowledge appropriate for the purposes of enabling them to properly exercise the functions of a member of the pension board.

52. The framework is intended to complement the *Pensions Regulator's Code of practice No 14: Governance and administration of public service pension schemes*.

53. Auditors should refer to this guidance when considering the pension fund governance statements.

Housing benefits

2014/15 HB COUNT

54. The Public Sector Audit Appointments Limited has issued the analytical review module of the 2014/15 HB COUNT. The tool enables auditors to review housing benefit (HB) subsidy claim forms by comparing 2014/15 information with 2013/14 and with other authorities. It provides a number of useful worksheets including the following two which require to be completed

- The year-to-year worksheet where 2013/14 claim data is entered manually for comparison against 2014/15 data. Any significant variances identified should be explained in column I
- The key ratios worksheet that allows comparison with other authorities. Any ratios highlighted in grey, pink or purple should be reviewed to establish the reason.

55. The information is for auditor use only. If auditors wish to provide authorities with outputs, they should ensure that the data for other authorities is anonymised.

Guidance on supporting evidence for subsidy claims

56. The Department for Work and Pensions (DWP) has issued a bulletin to provide general information on various HB matters.

57. HB General information bulletin G8/2015: subsidy certification provides advice on alternative types of evidence that demonstrate that a claim was received when original HB claim forms are not available. These include

- letters from the claimant about changes in circumstances
- copies of information supporting income, capital or rent levels

- copies of records of reviews of the claim.

58. The bulletin also advises that notifications arising from *Real time information* (RTI) referrals which contain sufficient information to process a change to HB entitlement provide acceptable evidence to support that change in entitlement.

Guidance on effective dates

59. The DWP has issued clarification on the impact on effective dates when changes to non-social security income coincide with the April uprating of applicable amounts. HB circular A10/2015 April uprating: Clarification of effective dates for housing benefit advises that

60. where rent is charged on a weekly basis, April uprating and changes in the claimant's income normally take effect from the first Monday in April

61. Where rent is charged on a non-weekly basis and
    - there is a change in the claimant's rental liability during the first week in April, both changes take effect from the date of the rent increase
    - there is no change in the claimant's rental liability, uprating takes effect from 1 April and the increase in income takes effect from the first day of the benefit week following the date on which the increase to the income actually occurs.

Guidance on residence status for EEA nationals

62. The DWP has issued guidance on permanent residence status for European Economic Area (EEA) nationals. HB circular A8/2015 European Economic Area right to reside - permanent residence status explains that an EEA national who has permanent residence status does not need to satisfy any other right to reside conditions for HB purposes.

63. Since April 2006, EEA nationals and their family members acquire a right of permanent residence in the UK if they have resided in the UK
    - legally for a continuous period of 5 years
    - as a worker or self-employed person, or in other specified cases such as a student.

64. The guidance covers matter such as
    - absences during the 5 year qualifying period
    - circumstances where individuals can acquire a right to reside in the UK permanently with less than 5 years residence
    - cases where a benefit is sanctioned or disallowed.

Guidance on benefits for persons from abroad

65. CIPFA has published guidance on determining HB awards for persons from abroad. These are claimants who do not satisfy the required residency tests and are not normally entitled to receive HB or any other income-related benefit. There are however many exceptions this rule including

- people with leave to remain in the UK
- workers who are members of an EEA state
- people with refugee status.

2015/16 funding

66. The DWP has issued the following circulars announcing funding for local authorities in 2015/16
    - HB circular S7/2015 New burdens payment for the real time information bulk data matching initiative announces additional funding to continue to action RTI referrals.
    - HB circular S8/2015 Payment of new burdens relating to the Single Fraud Investigation Service for 2015/16 – revised announces additional funding to meet the costs of the introduction of the Single Fraud Investigation Service in 2015/16.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 50 in respect of the financial management of self-directed support?			
2 Have you carried out the action recommended at paragraph 53 in respect of pension fund governance statements.			

TSU contacts for local authority chapter

67. The contacts in the TSU for this chapter are
    - Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or pobrien@audit-scotland.gov.uk.
    - Tim Bridle, Manager - Local Government (Technical) - 0131 625 1793 or tbridle@audit-scotland.gov.uk.
    - Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or acairns@audit-scotland.gov.uk (for housing benefit).

Further education sector

Introduction

This chapter contains information on the main technical developments, and guidance on any emerging risks, in the quarter that are relevant to further education colleges.

It should be read by external auditors with appointments in the further education sector.

Guidance from TSU on emerging risks

Valuation of tangible fixed assets

68. Technical bulletin 2014/2 (paragraph 280) advised that, in accordance with the Government financial reporting manual (FReM), tangible fixed assets would be valued on current value basis from 2014/15.

69. The *2007 Statement of recommended practice: Accounting for further and higher education* (SORP) allows colleges to

- adopt a policy of revaluation; or
- hold assets at historical cost; or
- hold assets at their book amount on transition to *FRS 15 Tangible fixed assets*.

70. Where colleges have in previous years adopted either the second or third option allowed by the SORP, they will be required to move to a policy of revaluation (i.e. current value basis) in 2014/15. As this is a change in accounting policy, the move should be accounted for as a prior year adjustment in accordance with *FRS 3 Reporting financial performance*.

71. Auditors should confirm that colleges have valued their tangible fixed assets in accordance with the FReM, and have accounted for a prior year adjustment where required.

Accounting developments

General accounting

2014/15 accounts direction

72. The Scottish Funding Council (SFC) has issued their accounts direction for colleges for 2014/15. As in previous years, the direction requires colleges to comply with the SORP in preparing their financial statements. As a change in 2014/15, the direction confirms that colleges are also required to comply with the FReM in those areas not covered by the SORP. In cases where there is a conflict, the SORP will take precedence.

73. Colleges are required to prepare their annual report and accounts with a 31 July year end. This change means that the 2014/15 annual report and accounts will cover a 16 month period for most colleges. The comparative figures will relate to the 8 month period to 31 March 2014.

74. Specific mandatory disclosure requirements for colleges are set out in Appendix 2 to the direction. The most significant additional disclosure as a result of complying with the FReM is the need for a remuneration report. Appendix 4 includes an example remuneration report and colleges are also referred to the FReM and Employers pension notice 430 for additional guidance. The amounts disclosed should include a pro-rata annual equivalent.

75. Also in accordance with the FReM, Appendix 2 also requires details of the estates strategy to be disclosed in the operating and financial review (OFR).

76. The direction requires an explanation to be disclosed where a college has incurred a deficit as a result of spending cash funding originally provided to cover depreciation. An illustrative form of wording is provided at Appendix 5.

77. Colleges are required to include a statement covering the responsibilities of their governing body in relation to corporate governance. Appendix 3 sets out the required disclosures and refers colleges to the guidance in the Scottish public finance manual.

78. The first page of direction should be included as an appendix to the financial statements.

Guidance on 2014/15 financial statements

79. The SFC has issued guidance to supplement the 2014/15 accounts direction. Detailed notes for guidance on completion of the 2014/15 financial statements covers key disclosures in the financial statements, including model disclosure notes set out at Annexes A to H. In certain cases, the additional disclosures are required to reflect the situation in Scotland.

80. The guidance notes remain largely the same as 2013/14, but reflect the 16 month accounting period, and compliance with the FReM.

81. In addition, paragraph 21 has been amended to reflect the SFC's view that the requirement under *IAS 19 Employee benefits* to accrue for untaken annual leave at the year end applies to colleges in 2014/15.

Provisions and contingencies

Guidance for early retirement provision

82. The SFC issued Guidance for early retirement provision spreadsheet completion to advise that the suggested net interest rate for early retirement pension calculations in 2014/15 has been changed to 1.00%.

83. Auditors should confirm their colleges have used an appropriate discount rate when calculating their early retirement provision, and have paid due regard to the rate suggested by the SFC.

Auditing developments

Technical guidance notes

Audit of 2014/15 annual report and accounts

84. The TSU has published Audit of 2014/15 annual report and accounts (further education) - technical guidance note 2015/6(FE) to provide auditors with guidance on performing the audit of the 2014/15 further education annual report and accounts.

85. The technical guidance note comprises a number of modules that

- highlight what the TSU considers to be the main risks of misstatement in each financial statement area, explains the correct treatment, and sets out actions for auditors to consider.
- provides guidance on auditors' responsibilities in respect of auditing the regularity of transactions, the OFR, the remuneration report, and the governance statement.

86. Auditors should use the technical guidance note when performing the audit of the 2014/15 further education annual report and accounts.

2014/15 model independent auditor's reports

87. The TSU has published 2014/15 Independent auditor's report (further education) - technical guidance note 2015/7(FE) to provide auditors with the model independent auditor's reports which should be used for the 2014/15 annual accounts. The technical guidance note also provides application guidance on their use.

88. In the interests of consistency, auditors are required to use the model wording in the appendices to the technical guidance note as a condition of their audit appointment. The only exception is any amendments required to tailor the terminology to reflect local circumstances. It should be noted that the requirement to follow the model wording in the appendices applies to the 'Bannerman' paragraph. The previous dispensation which allowed minor wording changes no longer applies from 2014/15.

89. Any proposed modifications to any audit opinion or conclusion in the model reports, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with the TSU in advance of finalising the report.

90. Auditors should use this technical guidance note when reporting on the audit of the 2014/15 annual reports and accounts. They should complete the checklist at Appendix 3 which provides a list of the key auditor actions.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 83 in respect of the early retirement provision?			
2 Have you used the technical guidance note referred to at paragraph 86 when performing the audit of the 2014/15 further education annual report and accounts?			
3 Have you used the technical guidance note referred to at paragraph 90 when reporting on the audit of the 2014/15 further education annual report and accounts?			

TSU contacts for further education chapter

91. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or ncameron@audit-scotland.gov.uk.
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Fraud cases

This chapter contains a summary of fraud cases arising at audited bodies that have recently been reported by auditors to the TSU.

Auditors should consider whether the weaknesses in internal control that facilitated each fraud may apply at their audited bodies and take the appropriate action.

Expenditure

Invalid social care payments

92. A couple defrauded £464,000 in independent living social care payments from a council over a nineteen year period.

Key features

A woman claimed independent living payments since 1996 to pay her carer, who was a family friend, on the basis that her husband was pursuing a career in the Territorial Army.

A social worker reported their suspicions to the council corporate fraud team, whose investigation established that the husband had not been in the Territorial Army since 1999. It is suspected that the family friend did not provide any care and passed the wages on to the couple, possibly retaining a percentage.

The fraud was possible as no evidence was obtained that the husband was serving in the Territorial Army.

The fraud continued for such a long period as social workers were apparently unsure to whom within the council to report their suspicions. A publicity campaign is ongoing within the council to raise awareness of fraud and how to report suspicions to the corporate fraud team.

TSU contact for fraud chapter

93. The contacts in the TSU for this chapter is Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or acairns@audit-scotland.gov.uk.

Technical Services Unit

Audit Scotland's Technical Services Unit (TSU) informs the professional judgement of appointed external auditors on technical matters and encourages the proper exercise of professional scepticism to improve the quality of the audit delivered to the Accounts Commission and Auditor General for Scotland. The TSU provides authoritative guidance and practical assistance to support appointed auditors in carrying out their responsibilities under the *Code of audit practice* to

- provide an opinion on audited bodies' financial statements and, where required, the regularity of transactions
- review and report on other information published with the financial statements, including governance statements and remuneration reports
- examine and report on approved grant claims and other returns submitted by local authorities
- review and report on whole of government accounts returns.

Contact details for relevant TSU staff are included at the end of each chapter.

Feedback on technical bulletins is encouraged and should be sent to

pobrien@audit-scotland.gov.uk

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Audit Scotland
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Technical bulletin 2015/4

October to December

AUDIT SCOTLAND

Prepared by the Technical Services Unit
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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

Foreword

Technical bulletins are prepared by Audit Scotland's Technical Services Unit (TSU), and approved by the Assistant Auditor General, to provide external auditors appointed by the Accounts Commission and Auditor General for Scotland with

- information on the main public sector technical developments in the quarter that are relevant to their audit appointment
- guidance from the TSU on any emerging risks identified in the quarter.

Technical bulletins are available to external auditors from Audit Scotland's *Technical reference library,* and published on the Audit Scotland website so that audited bodies and other stakeholders can access them.

It is important that auditors read this technical bulletin promptly so they are familiar with the information and guidance provided. The auditor action checklist section at the end of each chapter should be completed by a senior member of the audit team.

The articles on technical developments are intended to highlight the key points that the TSU considers external auditors require to be aware of. It may still be necessary for auditors to read the source material where greater detail is required. The documents referred to in the articles can be obtained by using the hyperlinks, where available. They are also available to external auditors from Audit Scotland's *Technical reference library*.

While auditors act independently, and are responsible for their own conclusions and opinions, the TSU has a role in ensuring that those conclusions and opinions are reached on the basis of informed judgement. Consistency in similar circumstances is important and **Audit Scotland's *Code of audit practice* therefore states that auditors should normally follow TSU guidance.** Auditors should advise the TSU promptly if they intend not to follow guidance provided in this technical bulletin on an emerging risk.

The TSU encourages feedback on this technical bulletin. Comments should be sent to pobrien@audit-scotland.gov.uk.

More in-depth and extensive guidance is provided in separate technical guidance notes published by the TSU. Technical guidance notes published in the quarter are referred to in this technical bulletin, and can be obtained by using the hyperlinks to the Audit Scotland website.

Headlines

This chapter provides brief headlines for the articles on technical developments and guidance in this technical bulletin, classified by the audit year to which it relates, and referenced to the paragraphs containing the main article.

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CIPFA has published the 2015/16 edition of the *Local government pension scheme example accounts and disclosure checklist*.	36 - 39
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Cross-sectoral chapter

Introduction

This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to all sectors.

It should be read by all external auditors. Information on developments and guidance from the TSU in the quarter that are relevant to only one sector are covered in the relevant sector-specific chapter.

Auditing developments

Proposed changes to auditing and ethical standards

1. The Financial Reporting Council (FRC) has issued a consultation paper Enhancing confidence in audit which contains proposed changes to auditing and ethical standards. The proposals arise from
   - a new EU audit Regulation and Directive which require revisions to ethical and auditing standards
   - recent changes to International Auditing and Assurance Standards Board (IAASB) auditing standards.
2. The consultation paper discusses the proposed changes to auditing standards at section 3. A table showing the affected standards is provided at Appendix 2 to the paper, while Annex 2 sets out the proposed changes in detail.
3. The main proposals include the following
   - The adoption of the IAASB's *ISA 700 Forming an opinion and reporting on financial statements* to replace the current *ISA 700 (UK&I) Independent auditor's reports on the financial statements*.
   - The adoption of the IAASB's *ISA 701 Key audit matters* which requires auditors of listed entities to communicate those matters that the auditor views as most significant, with an explanation of how they were addressed in the audit. There is a proposal to extend the definition of key audit matters used by the IAASB to include those assessed risks of material misstatement which had the greatest effect on the overall audit strategy, the allocation of resources in the audit, and directing the efforts of the audit team.
   - The adoption of the IAASB's *ISA 720 The auditor's responsibilities relating to other information in documents containing audited financial statements*, with proposed additional requirements to obtain an understanding of the applicable reporting framework used to prepare the other information (e.g. management commentary and governance statement), consider whether there are material misstatements between the other

information and that framework, and report on the other information in accordance with legislation.

- Changes to *ISA (UK&I) 570 Going concern* to require auditors to report by exception on management's use of the going concern basis of accounting and whether material uncertainties have been identified but not disclosed.

4. The proposed auditing standards in Annex 2 have changes tracked from the latest published version with the exception of ISA 700, ISA 701 and ISA 720. For these three standards, the IAASB's revised standard has been included as the starting point and then UK specific changes have been incorporated.

5. Proposed changes to ethical standards are discussed at section 2 of the consultation paper, and set out in detail in Annex 1. It is proposed that the current five separate standards should be consolidated into one standard with sub-sections.

6. The standards are being revised to make the overarching principles and supporting ethical provisions more prominent and more clearly outcome based, and to place them at the front of the standard (see pages 17 to 21 of Annex 1). These outcomes must be met. Specific requirements and guidance designed to assist compliance with the principles and supporting provisions in particular circumstances are also included.

7. Comments should be made to ARDconsultation@frc.org.uk by11 December 2015.

TSU contact for cross-sector chapter

8. The contact in the TSU for this chapter is Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or pobrien@audit-scotland.gov.uk.

Local authority sector

Introduction

This chapter contains information on the main technical developments, and guidance from the TSU on any emerging risks, in the quarter that are relevant to the local authority sector.

It should be read by external auditors with appointments in the local authority sector.

Auditing developments

Technical guidance notes

Audit of 2015/16 annual accounts

9. The TSU has published Audit of 2015/16 annual accounts (local authorities) - technical guidance note 2015/8(LA) to provide auditors with guidance on planning and performing the audit of the 2015/16 local authority annual accounts.

10. The technical guidance note comprises a number of modules that
    - highlight the main risks of misstatement in each financial statement area, explains the correct treatment, and sets out actions for auditors to assess whether the authority has followed the required treatment
    - provides guidance on auditors' responsibilities in respect of the management commentary, the remuneration report, and the annual governance statement.

11. Following extensive consultation with all auditors, the technical guidance note represents an agreed position on a range of complex technical issues and is a key document as auditors plan and perform the audit of 2015/16 local authority annual accounts.

12. Auditors should read the technical guidance note so they are familiar with the guidance provided. It is important that auditors follow the actions set out to ensure that all auditors adopt a consistent approach to common risks.

Accounting developments

Borrowing and lending

Proposed new regulations

13. The Scottish Government has issued a consultation paper on proposed changes to the statutory arrangements for local authority borrowing, lending and the loans fund. The proposal is to repeal most paragraphs of Schedule 3 of the Local Government (Scotland) Act 1975 and replace them from 2016/17 with
    - The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016

- statutory guidance on the loans fund.

14. Regulations 2 to 4 of the draft regulations cover the borrowing of money by local authorities. A summary of key proposals are as follows
    - Regulation 2(1) sets out the purposes for which a local authority may borrow.
    - Regulation 2(1)(a) retains the existing power to borrow to finance capital expenditure but Regulation 1 defines capital expenditure by reference to proper accounting practices.
    - Regulation 2(1)(b) permits a local authority to borrow for treasury management activities. This provides a slightly wider power than Schedule 3 reflecting the treasury needs of an authority to refinance existing borrowing, use internal cash reserves, and borrow in advance or after capital expenditure is incurred.
    - Regulation 4 requires a local authority, when exercising its borrowing powers, to have regard to recognised codes of practice and guidance in relation to treasury management. The *Treasury management code* is considered to be recognised guidance.
15. Regulation 5 recognises credit arrangements (e.g. leases and private finance initiative) for the purposes of financing capital expenditure of the local authority.
16. Regulation 6 requires a local authority to determine, before the start of each financial year, how much external debt it can afford (known as the authorised limit) during that financial year and each of the subsequent two financial years. As a transitional measure, Regulation 23 requires the authorised limit for 2016/17 to be determined no later than 1 June 2016. The *Prudential code* includes long-term liabilities in the authorised limit, but the proposal in the Regulations is to also include short term liabilities.
17. Regulation 6(2) requires an authority to set a single authorised limit for external debt and to separately identify the amount of borrowing and the amount of credit arrangements. These are defined as the authority's 'debt amounts'. Regulation 6(3) allows a local authority to exceed either of its debt amounts (borrowing or credit arrangements) provided its authorised limit is not exceeded. Regulation 6(6)(a) requires the section 95 officer to report any debt amounts which have been exceeded.
18. Under Regulation 6(4), the determination of the authorised limit and any variation of that limit is a function of the authority itself and may not be delegated. This takes precedence over the *Prudential code*, which requires the setting or revising of prudential indicators to follow the same route as the budget of the local authority.
19. Regulations 7 to 10 set out the arrangements for the security of money borrowed. As a new provision, local government pension funds do not form part of the revenues of the authority in terms of providing security for borrowing. Similarly, under Regulation 13, money borrowed by a local authority for a pension fund is not to be treated as borrowing of the local authority. The temporary use by a local authority of money forming part of pension funds (other than for the purposes of the fund) is to be treated as borrowing by the authority under Regulation 14.

20. Regulation 16 provides local authorities with the new power to borrow and advance funds to a common good fund. However, this is only in respect of expenditure by the fund which would be capital expenditure of the local authority if incurred directly by the authority.

21. Regulation 17 requires local authorities to maintain a loans fund and to administer it in accordance with proper accounting practices and prudent financial management. Regulation 18(1) requires a local authority to determine, for each loan fund advance

- the period over which the advance is to be repaid
- the amount of repayment in each financial year in that period.

22. In making this determination, the repayment must be a prudent repayment. Statutory guidance will detail how a loans fund is to be administered. The draft statutory guidance sets out the meaning of prudent repayment at paragraphs 26 and 27. It explains that the broad aim of prudent repayment is to ensure that

- the advance is repaid over a period bearing some relation to the period over which the asset continues to provide a service
- the value of the instalment bears some relation to the consumption of the asset used to provide the service.

23. However, there may be circumstances where it is prudent to determine the period and amounts based on a funding or income stream.

24. Paragraphs 28 to 44 of the draft statutory guidance sets out the following four options that are considered to represent prudent repayment

- Option 1 allows a local authority to determine, for a transitional period of five years, that loans fund advances made from 1 April 2016 will be repaid as if the Schedule 3 had not been repealed.
- Option 2 equates the annual repayment of the loans fund advance with the amount of annual depreciation and any impairment charged for the asset the subject of the loans fund advance.
- Option 3 is based on the life of the asset, either using the equal instalments or annuity method.
- Option 4 allows the annual repayment of a loans fund advance to be calculated by reference to an income stream.

25. Paragraphs 50 to 55 of the draft statutory guidance requires a local authority to disclose in the annual accounts

- its policy for determining its loans fund advance repayment
- the value of outstanding advances at each financial period end, together with an analysis of the value of repayments due in future periods in five year periods.

26. The Regulations only apply to new loan fund advances made after 1 April 2016. Repayment of loan fund advances made before that date will continue to be made in accordance with Schedule 3.

27. Responses to the consultation should be made to Hazel.Black@gov.scot by 31 December 2015.

Health and social care integration

New financial reporting guidance

28. The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) has issued Additional guidance on accounting for the integration of health and social care 2015/16 to support the implementation of financial reporting for health and social care integration in both the integration joint board (IJB) and local authority annual accounts. Detailed guidance is provided on a number of areas including

- the 2015/16 accounting period for an IJB
- IJB operating costs
- remuneration reports
- the service expenditure analysis
- related party disclosures
- underspends.

2015/16 IJB accounting period and operating costs

29. Guidance is provided on the 2015/16 accounting period for IJBs at paragraphs 10 to 18, and on the operating costs at paragraphs 19 to 28.

30. For 2015/16, the accounting period will be from the establishment date specified in the order (at which point the shadow board will cease to operate) to 31 March 2016. This will be earlier than the statutory 'integration start day' when joint service delivery actually commences. Points covered in the guidance include the following

- Between the establishment date and the integration start day, it is anticipated that IJB operating costs will be incurred. These are the costs of running the IJB itself, rather than expenditure incurred on commissioning services. Typically IJB running costs will include the supply of staff and services by the local authority and NHS board partners.
- The date from which joint service delivery costs will be reflected in IJB accounts as commissioning expenditure, and in local authority accounts as commissioning income and service expenditure, will be the integration start day.
- Where a reduction in the partner contribution is agreed as a consideration for the provision by the local authority of staff or services to support the IJB, the authority's partner contribution in the IJB accounts should be grossed up and the cost of the services recognised separately. This would not be the case where there is clear evidence that the support is being provided free of charge.

Remuneration report

31. The guidance covers the remuneration report of both the IJB and local authority partner at paragraphs 29 to 53. Some key points are as follows

- The Chairperson and the Vice-Chairperson of the IJB should be included in the IJB remuneration report.
- It is considered that the IJB Chief Officer should be regarded as an employee of the IJB and included in the remuneration report.
- It is not anticipated that the IJB will recognise a pension liability for voting board members or the Chief Officer on the IJB balance sheet, unless the IJB has entered into a formal agreement to accept ongoing pension liabilities (rather than simply fund the current employer's contributions).
- Non-voting board members are not regarded as employees of the IJB. On this basis, they are not anticipated to feature in the remuneration report.

Service expenditure analysis

32. Guidance on the service expenditure analysis (SEA) is provided at paragraphs 54 to 67. IJBs are expected to analyse their expenditure and income in terms of the existing SEA set out in the *Service reporting code of practice*. In addition, a new line for health care expenditure will be required. Partner funding contributions should be presented as taxation and non-specific grant income and expenditure rather than service related income.

33. In the local authority's accounts, its contribution to IJB funding should be a distinct from commissioning income received and service expenditure incurred. The guidance includes a suggested presentation for the local authority SEA at paragraph 67.

Related party disclosure

34. The IJB will be a related party of the partner organisations and disclosure will therefore be required in each of the partner's accounts. Disclosures will also be required in the IJB accounts. Guidance, including anticipated disclosures, is provided at paragraphs 68 to 72.

Cash and cash equivalents

35. IJBs are not expected to operate bank accounts or hold cash balances. Where an IJB underspends, a general fund balance is expected to exist. Paragraph 78 of the guidance advises that the asset supporting the general fund balance should be presented as a debtor. As it is unlikely that the IJB will present a cash and cash equivalent figure on the balance sheet, there is unlikely to be a cash flow statement.

Pension funds

2015/16 example accounts and disclosure checklist

36. The Chartered Institute of Public Finance and Accountancy (CIPFA) has published the 2015/16 edition of the *Local government pension scheme example accounts and disclosure checklist*. The publication provides an example set of accounts that meet the minimum requirements of the *Code of practice on local authority accounting in the UK* (the Code). It sets out a fund account and a net assets statement as well as information to be disclosed in the notes. Auditors can access it from the *Technical reference library*.

37. The main change to the example accounts for 2015/16 is the addition of note 25 on agency services. It has been added to reflect that some pension funds provide agency payroll services to some scheme bodies for discretionary awards. This is a memorandum disclosure only as the sums involved are not recognised within pension fund accounts.

38. Note 24 on related party transactions describes the relationship between the administering council and the pension fund. As was the case in previous editions, the note follows Code paragraph 3.9.4.3 by stating that the disclosure requirements for key management personnel are satisfied by the disclosures for officer remuneration. However, this is based on the assumption that there are such disclosures in the same financial statements. The inclusion of a remuneration report in the authority's own financial statements does not satisfy the disclosure requirements for key management personnel in the pension fund financial statements.

39. The publication also includes a disclosure checklist that identifies the Code's requirements in relation to pension funds.

Housing benefits

Miscellaneous guidance

40. The Department for Work and Pensions (DWP) has issued the following bulletins and circulars in respect of housing benefit

- HB general information bulletin G11/2015 provides a reminder that documentary evidence used in support of housing benefit claims cannot be submitted electronically.
- HB circular A11/2015 Fraud and error reduction incentive scheme incentive payments: Clarity on the end of year adjustment provides clarification that local authorities can transfer any excess above the *Fraud and error incentive scheme* threshold in one quarter to other quarters where they are below the threshold in order to qualify for incentive payments for the year.
- HB urgent bulletin U1/2015 Clarification on the impact of sanctions on housing benefit provides clarification on the impact of *Jobseekers allowance* and *Incapacity benefit* sanctions on housing benefit claims. When a sanction is applied, entitlement to benefits continues but will not be payable for a fixed period of time. Claimants who are receiving passported housing benefit should continue to do so without interruption.
- HB circular A12/2015 Process to obtain appropriate claimant personal independence payment information not available via the customer information system provides updated guidance that incorporates all previous information on the process local authorities should adopt when obtaining *Personal independence payment* award details for housing benefit purposes.

Abolition of the family premium and changes to backdating housing benefit

41. The Housing Benefit(Abolition of the family premium and date of claim)(Amendment) Regulations 2015 have been issued to amend the principal 2006 housing benefit regulations. The amendments

- shorten the period over which housing benefit claims can be backdated from six months to one month with effect from 1 April 2016
- abolish the family premium for housing benefit claims from 1 May 2016. Transitional protection is in place for some existing housing benefit recipients.

Non domestic rates

New powers for local scheme

42. Section 140 of the *Community Empowerment (Scotland) Act 2015* empowers a local authority to establish a scheme to reduce or remit any rate levied by it in respect of lands and heritages from 2015/16. The scheme may apply to specified categories, areas or activities.

43. The Community Empowerment (Scotland) Act 2015 (Commencement No. 1) Order 2015 brought section 140 into force on 31 October 2015.

Charities

Common good register

44. Part 8 of the *Community Empowerment (Scotland) Act 2015* contains a requirement for local authorities to establish and maintain a register of property which they hold as part of the common good.

45. Once part 8 is commenced, before establishing a common good register, an authority will be required to

- publish a list of property that it proposes to include in the register
- notify community councils and other community bodies
- invite the community bodies to make representations in relation to whether the property is part of the common good.

46. Once the register is established, local authorities will be required to

- make arrangements to enable members of the public to inspect the common good, and make it available on a website
- publish details of any proposed property disposals or change of use
- have regard to any guidance issued by the Scottish Government in relation to these duties.

Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action required by paragraph 13 in respect of technical guidance note 2015/8(LA)?			

TSU contacts for local authority chapter

47. The contacts in the TSU for this chapter are

- Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or pobrien@audit-scotland.gov.uk.
- Tim Bridle, Manager - Local Government (Technical) - 0131 625 1793 or tbridle@audit-scotland.gov.uk.
- Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or acairns@audit-scotland.gov.uk (for housing benefit).

Central government sector

Introduction

This chapter contains information on the main technical developments, and guidance on any emerging risks, in the quarter that are relevant to central government bodies.

It should be read by external auditors with appointments in the central government sector.

Accounting developments

Provisions

2015/16 discount rates

48. HM Treasury has issued PES(2015)8 to announce the discount rate for post-employment benefits liabilities and general provisions as at 31 March 2016.

49. The discount rate for post employment benefits and early departure provisions will change from 1.3 % real to 1.37% real from 31 March 2016. The financial assumptions, based on market conditions, related to post employment benefit discount rates are set out in an annex. Funded schemes within central government should use a discount rate based on financial assumptions at 31 March each year, rather than these assumptions which are as at 30 November.

50. The real discount rates to be applied to provisions recognised in accordance with IAS 37 as at 31 March 2016 are as follows:

- The short term rate (for cash-flows up to 5 years from the statement of financial position date) is minus 1.55%.
- The medium term rate (between 5 and 10 years) is minus 1.00%.
- The long term rate (more than 10 years) is minus 0.80%.

51. The change in discount rates could result in non-cash negative annually managed expenditure (AME) arising from interest income. This income can only be used for expenditure relating to provisions, or for depreciation of capital assets that have been donated. It cannot be used to fund genuine AME cash expenditure.

52. Auditors should refer to this paper when reviewing the discount rates applied to provisions in 2015/16 financial statements.

Financial instruments

2015/16 discount rates

53. PES(2015)8 also sets out the discount rate to be applied to financial instruments at 31 March 2016 where future cash flows are discounted to measure fair value. The *Government financial*

reporting manual (FReM) requires bodies to use the higher of the rate intrinsic to the financial instrument and the real financial instrument rate set by Treasury. The paper advises that the rate set by Treasury to be applied at 31 March 2016 is 0.7

- Where the financial instrument is index linked to RPI, the rate as applied is RPI+0.7.
- Where it is not linked to an inflationary index, and a nominal rate is required, 3.7% may be used.

54. Non-cash gains or losses that score in budgets arising from this change in estimation should be scored to AME. Negative AME cannot be used to fund cash AME expenditure or lending.

55. Auditors should refer to this paper when reviewing the discount rates applied to financial instruments in 2015/16 financial statements.

TSU contacts for central government chapter

56. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or ncameron@audit-scotland.gov.uk.
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Further education sector

Introduction

This chapter contains information on the main technical developments, and guidance on any emerging risks, in the quarter that are relevant to further education colleges.

It should be read by external auditors with appointments in the further education sector.

Auditing developments

Technical guidance notes

2014/15 independent auditor's reports

57. The TSU has published 2014/15 Independent auditor's report (further education) - technical guidance note 2015/7(FE) - supplement to provide auditors with guidance on wording a potential qualification to the opinion in the independent auditor's report on whether the remuneration report within colleges' 2014/15 accounts complies with the accounts direction.

58. The accounts direction requires compliance with the FReM, and the supplement was prepared in response to a number of auditors advising the TSU that their colleges had not disclosed the information on pension rights necessary to meet the requirements of FReM paragraph 5.2.27.

59. Subsequent to publication of the supplement, it appears that at least one college has also not complied with the FReM requirement to include the value of pension benefits in the single total remuneration figure. Where this is the case, this should also be reflected in the independent auditor's report. Given that the non-compliance would then extend to both the pension rights and remuneration disclosures, auditors should consider whether it would be appropriate to express an adverse opinion (i.e. the remuneration report does not comply with the accounts direction) rather than an 'except for' qualified opinion. Auditors should contact the TSU if this is the case.

TSU contacts for further education chapter

60. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or ncameron@audit-scotland.gov.uk.
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or hcobb@audit-scotland.gov.uk.

Fraud cases

This chapter contains a summary of fraud cases arising at audited bodies that have recently been reported by auditors to the TSU.

Auditors should consider whether the weaknesses in internal control that facilitated each fraud may apply at their audited bodies and take the appropriate action.

Expenditure

Duplicate payment

61. A council overpaid over £1,000,000 to an external provider due to a lack of internal controls to prevent an invoice being paid more than once.

Key features

The provider sent the invoice to the local authority in both electronic and hard copy. The electronic invoice was processed automatically by one department while subsequently the hard copy was processed as a manual payment by another department. When the second invoice was passed to the Accounts Payable team, their checks did not identify the first invoice on the system.

The overpayment was not identified until it was highlighted by the provider and returned.

Arrangements have been put in place to improve clarity over which department is responsible for processing orders and invoices, and to ensure that additional checks on invoices to prevent duplicate payments are conducted, where appropriate.

Income

School funds

62. A school clerical assistant misappropriated over £15,000 of cash from a school fund.

Key features

The defaulter was responsible for the day-to-day operation of the school fund. She misappropriated some of the income and also wrote fraudulent cheques.

The fraud was identified when a supplier contacted the Head Teacher to request payment for an outstanding invoice. It was then identified that there were insufficient funds in the bank account to pay the invoice.

The fraud was possible as the Head Teacher did not ensure that the fund was regularly reconciled or review school fund documentation to verify the balance held. In addition school fund accounts had not been prepared, and this was not pursued by the relevant Team within the council.

Head Teachers have been reminded of the need to ensure compliance with the council's financial regulations in relation to school funds.

TSU contact for fraud chapter

63. The contact in the TSU for this chapter is Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or acairns@audit-scotland.gov.uk.

Technical Services Unit

Audit Scotland's Technical Services Unit (TSU) informs the professional judgement of appointed external auditors on technical matters and encourages the proper exercise of professional scepticism to improve the quality of the audit delivered to the Accounts Commission and Auditor General for Scotland. The TSU provides authoritative guidance and practical assistance to support appointed auditors in carrying out their responsibilities under the *Code of audit practice* to

- provide an opinion on audited bodies' financial statements and, where required, the regularity of transactions
- review and report on other information published with the financial statements, including governance statements and remuneration reports
- examine and report on approved grant claims and other returns submitted by local authorities
- review and report on whole of government accounts returns.

Contact details for relevant TSU staff are included at the end of each chapter.

Feedback on technical bulletins is encouraged and should be sent to

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9 December 2015