

# Midlothian Integration Joint Board

Year ending 31 March 2017

Annual Audit Plan

Audit and Risk Committee – 9 March 2017



Building a better  
working world

## Public sector audit framework

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The Code of Audit Practice (the Code) <http://www.audit-scotland.gov.uk/report/code-of-audit-practice-2016> sets out the responsibilities of audited bodies, in accordance with statute and other relevant guidance, in respect of the preparation of financial statements.

We issue our audit opinion on the 'truth and fairness' of the Midlothian Integration Joint Board's (the IJB) financial statements in accordance with management's timetable, and by 30 September 2017.

The nature of public sector audit means that the focus of audit work is broader than just the financial statements of the IJB. We report on the four dimensions of public sector audit as set-out jointly by the Accounts Commission and the Auditor General for Scotland. Judgements in respect of Best Value are formed from the findings in respect of each of the four dimensions.

## Understanding the Integration Joint Board

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Our audit approach responds to our understanding of the IJB, and the environment in which it operates. 2016/17 has seen establishment of the IJB's Strategic Plan. The IJB effects its activity through direction to its constituent authorities in relation to each of the delegated functions. The IJB also operates as a statutory member of the Midlothian Community Planning Partnership and contributes to the delivery of the strategic priorities.

Resources have been tight in 2016/17 and the IJB approved use of integration funding to meet financial pressures. The 2017/18 budget and beyond is expected to be extremely challenging, requiring major changes in how services are configured and delivered.

## Financial statements audit

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### Materiality

Planning Materiality for the audit has been determined at £1.8 million, representing 1.5% of estimated gross expenditure. Tolerable Error is set at £0.9 million. Our Summary of Audit Differences (SAD), the nominal amount (amount below which misstatements, whether individually or accumulated with other misstatements, would not have a material effect on the financial statements) is £90,000.

### Risk assessment

In line with auditing standards we identify significant risks in respect of fraud in expenditure recognition, and in respect of the risk of management override of controls.

At this stage of our audit planning, we have not identified any other significant financial statement risks. We will confirm our updated risk assessment as part of our Annual Audit Report.

### Audit approach

We obtain an understanding of the IJB's control environment and key accounting processes in operation.

Management has primary responsibility for the prevention and detection of fraud. We design appropriate audit procedures in response to identified fraud risk factors, for the purpose of detecting material misstatements.

There are no significant changes to the Accounting Code of Practice for 2016/17 although a new expenditure and funding analysis is required.

## Wider scope audit and other work

Pages 12-14

The wider scope audit as set out in the Code plays a key role in the public sector audit framework in Scotland.

We have identified two wider scope audit focus areas for 2016/17, being the areas where we will concentrate our audit work in the year. Firstly, we will consider the work undertaken by chief officers and the IJB to consider the achievement of Financial Sustainability in delivery of key priorities. Secondly, in respect of Governance and Transparency, we will consider the arrangements established to ensure effective governance and scrutiny and transparency in performance reporting.

Key to the assessment and judgement in the wider scope audit areas is the quality of the IJB's self-evaluation to be able to demonstrate the quality and effectiveness of their arrangements. In planning and performing our audit work, we take into account the Accounts Commission's Strategic Audit Priorities.

## Other audit responsibilities

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The extent of our other audit responsibilities is expected to develop as the IJB's operations mature. As the IJB is constituted under local authority regulations, we have regard to statutory responsibilities on local authority bodies in respect of compliance with the Following the Public Pound Code, to the extent it is applicable to the IJB's operations.

## Team, fees and deliverables

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Stephen Reid is your audit engagement partner, supported principally by Keith Macpherson and John Boyd.

As this is first year of the IJB audit, no central fee has been set by Audit Scotland for any integration authorities. We will agree the fee with chief officers on completion of our audit planning, and our understanding of the year-end audit requirements.

We have agreed a high level timetable with management to meet statutory and other guidance for reporting.

## Appendices

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We confirm our independence to act as your external auditor.

We provide you with details of the key communications we are required to provide you with in accordance with Auditing Standards.

### About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of Midlothian Integration Joint Board (the IJB) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

This report is for the benefit of the IJB and is made available to the Accounts Commission, the Controller of Audit and Audit Scotland (together the Recipients). This report has not been designed to be of benefit to anyone except the Recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

### Complaints

If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Russell Frith, Assistant Auditor General, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

# **1. Public sector audit framework**

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as Midlothian Integration Joint Board's (the IJB) external auditor for the five year period 2016/17 to 2020/21.

We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; relevant Auditing Standards and applicable Practice Notes issued by the Auditing Practices Board; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Plan, prepared for the benefit of IJB management and the Audit and Risk Committee, sets out our proposed audit approach for the audit of the financial year ending 31 March 2017, in accordance with the responsibilities placed on us through the public sector audit framework in Scotland.

## Financial statements audit

### *The IJB's responsibilities*

The IJB is responsible for the preparation of the financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation. The Code also sets out the IJB's responsibilities for maintaining accounting records and supporting working papers that have been prepared to an acceptable professional standard.

The IJB is also required to prepare and publish, along with the financial statements, an annual governance statement, management commentary and a remuneration report that are consistent with the disclosures within the financial statements.

Management, with the oversight of the Audit and Risk Committee, should ensure communication of relevant information to users about the IJB and its financial performance. Guidance on IJB performance reporting was provided by the Scottish Government in publication <http://www.gov.scot/Publications/2016/03/4544>.

### *Our responsibilities*

We are responsible for conducting an audit of the financial statements of the IJB. We will provide an opinion on the financial statements as to:

- whether they give a true and fair view of the financial position of the IJB as at 31 March 2017 and its expenditure and income for the year then ended; and
- whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2016/17 Code of Practice on Local Authority Accounting in the United Kingdom.

We also review and report on the consistency of the other information prepared and published by the IJB along with its financial statements.

### *The Local Authority Accounts (Scotland) Regulations 2014 (the Regulations)*

In accordance with the Regulations 2014, the signed unaudited annual financial statements should be submitted to the external auditor no later than 30 June 2017. Furthermore, the unaudited annual financial statements should be considered by an appropriate committee of the IJB by 31 August 2017.

The Regulations also set out the requirements for approval of the audited financial statements. The IJB, or relevant committee, is required to approve the audited annual financial statements for signature no later than 30 September 2017. In making their consideration, the Regulations require elected members to have regard to any report made, or advice provided by the proper officer of the IJB and the auditor.

To support those charged with governance in discharging these responsibilities, we will report the findings of our audit in our Annual Audit Report.

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## Key messages

The Code of Audit Practice (the Code) <http://www.audit-scotland.gov.uk/report/code-of-audit-practice-2016> sets out the responsibilities of audited bodies, in accordance with statute and other relevant guidance, in respect of the preparation of financial statements.

We issue our audit opinion on the 'truth and fairness' of the IJB's financial statements in accordance with management's timetable, and by 30 September 2017.

Together the Accounts Commission and the Auditor General for Scotland agreed the four dimensions set out in the Code which comprise the wider scope audit for public sector in Scotland. These are:

- financial sustainability;
- financial management;
- governance and transparency; and
- value for money.

In local government, audit work over the four dimensions leads to an overall assessment of Best Value.

## Wider scope audit


### The IJB's responsibilities

The Code sets out the broader responsibilities of the IJB in respect of ensuring proper financial stewardship of public funds. In particular the IJB should establish proper arrangements:

- for ensuring the proper conduct of its affairs, including the legality of activities and transactions and for monitoring the adequacy and effectiveness of these arrangements;
- for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct;
- to ensure that their financial position is soundly based having regard to, for example, balances and reserves including strategies about levels held and their future use and how they plan to deal with uncertainty in the medium and longer term; and
- for securing Best Value in accordance with the IJB's statutory duty, including the preparation and publication of performance information in accordance with directions issued by the Accounts Commission.

### Our responsibilities

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on the four dimensions of wider-scope public audit. Our audit work over the wider scope audit dimensions complements our financial statements audit.

 <b>Financial management</b>	 <b>Financial sustainability</b>	 <b>Governance and transparency</b>	 <b>Value for money</b>
<p>We conclude on the effectiveness of financial management arrangements. This includes considering whether there is sufficient financial capacity and resources, sound budgetary processes and whether the control environment and internal controls are operating effectively.</p>	<p>We consider the medium and longer term outlook to determine if planning is effective to support service delivery. This will focus on the arrangements to develop viable and sustainable financial plans.</p>	<p>We review the adequacy of governance arrangements. In particular, we consider and report on; whether these are appropriate and operating effectively and that there is effective scrutiny, challenge and transparency on decision-making.</p>	<p>We consider whether value for money can be demonstrated in the use of resources. This includes the extent to which there is an alignment between spend, outputs and outcomes delivered and that there is a clear focus on improvement.</p>

## Key messages

The nature of public sector audit means that the focus of audit work is broader than just the financial statements of the IJB.

We report on the four dimensions of public sector audit as set-out jointly by the Accounts Commission and the Auditor General for Scotland.

Judgements in respect of Best Value are formed from the findings in respect of each of the four dimensions.

## **2. Understanding the Integration Joint Board**

## 2. Understanding the Integration Joint Board

In accordance with the principles of the Code, our audit work is designed to be proportionate and risk based. It is based on an understanding of the strategic environment in which the IJB operates.

Through our knowledge and experience, plus our assessment of how the wider environment impacts on your activities, we tailor our approach to risk assessment.

Through discussion with senior management, and from review of corporate planning documents, we develop an understanding of your priorities and the specific challenges which the IJB faces.

### Strategic context

The IJB is an organisation at a relatively early stage of maturity, but having to operate in an increasingly challenging environment. Changes in population demographics across Scotland have increased both the need and the demand for certain services. There has, however, been continued pressure on both NHS resources and the local government finance settlements in recent years.

2016/17 represents the first full year of operation of integration authorities, such as the IJB, established to take forward the Scottish Government's programme of reform in respect of Integration and transformation of Health and Social Care.

In December 2016, the Scottish Government set out its nine priorities for integration authorities in a letter to Chief Officers. These form the context for the IJB to set its own strategic and budget planning going forward.

### Understanding the IJB's priorities

The IJB approved its three year Strategic Plan in December 2015 in advance of the commencement of its responsibilities for the planning, resourcing and the operational oversight of a wide range of health and social care services from 1 April 2016. The Strategic Plan was developed drawing on the findings of the Joint Strategic Needs Assessment, completion of which was a requirement of the Public Bodies (Joint Working) (Scotland) Act 2014.

The IJB effects its activity through direction to its constituent authorities in relation to each of the delegated functions. The IJB also operates as a statutory member of the Midlothian Community Planning Partnership and contributes to the delivery of the strategic priorities as contained in the Strategic Outcomes of the partnership.

There has been significant pressure on the 2016/17 IJB budget from the outset reflecting significant cost and demand pressures. We understand, however, that actions have been taken to address a major projected overspend in Adult Care. The partners have agreed to cover any 2016/17 overspends.

Midlothian Council approved its 2017/18 budget in February 2017, which included the allocation to the IJB. The IJB's budget for 2017/18 will be set in late March 2017, following agreement of the NHS budget position. Linked to this are the delivery plans for the IJB and how the strategic plan priorities will be delivered through a change programme which requires to balance transforming service delivery with the need to achieve significant efficiency savings and the challenges facing social care in seeking to remodel services to meet increasing demand.

The strength of partnership working arrangements will be a key factor in the ability of the IJB to deliver the significant change required in integrating health and social care to improve services while the overall resource envelope is severely constrained.

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### Key messages

Our audit approach responds to our understanding of the IJB, and the environment in which it operates. 2015/16 has seen establishment of the IJB's Strategic Plan. Delivery of strategic priorities is undertaken as a statutory member of the Midlothian Community Planning Partnership.

Resources have been tight in 2016/17 and the 2017/18 budget and beyond is expected to be extremely challenging, requiring major changes in how services are configured and delivered.



### **3. Financial statements audit**

We provide an opinion on the financial statements as to whether they give a true and fair view of the financial position of the IJB, and whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2016/17 Code of Practice on Local Authority Accounting in the United Kingdom. We also review and report on the consistency of the other information prepared and published by the IJB along with its financial statements.

We undertake our financial statements audit work in accordance with the four phases of EY's Global Audit Methodology: *Planning; Identification and assessment of risk; Design and execution of our response to those risks; and Conclude and communicate.*

## Planning our audit work

### **Initial planning, independence and quality assurance**

Our initial planning for any audit engagement includes client and engagement acceptance, which includes our documentation of the service requirements. We did not identify any specific audit risks arising from these procedures.

Part of these procedures are designed to ensure compliance with all relevant ethical standards, including independence which we assess for both EY as a firm and the individuals assigned to the audit. We set out more information on our independence in Appendix A.

We identify the team with primary responsibility for performance of the audit. Stephen Reid is the audit partner-in-charge.

### **Materiality**

In accordance with ISA 320 we apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion. Materiality is the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. We determine:

- Planning materiality (PM) – this is set for the financial statements as a whole, and is used to set the scope for our audit. We have determined this to be £1.8 million, representing 1.5% of estimated gross expenditure.
- Tolerable Error (TE) – materiality at an individual account balance, which is set so as to reduce to an acceptably low level that the aggregate of uncorrected and undetected misstatements exceeds PM. We have set this at 50% of PM, being £0.9 million.
- Summary of Audit Differences (SAD) Nominal amount – this is the amount below which misstatements, whether individually or accumulated with other misstatements, would not have a material effect on the financial statements. We have set this at £90,000.

Our evaluation requires professional judgement and so takes into account qualitative as well as quantitative considerations implied in the definition. Factors which we consider include the perspectives and expectations of users of the financial statements as well as our risk assessment as to the likelihood of material misstatements arising in the financial statements.

The amount we consider material at the end of the audit may differ from our initial determination. At the end of the audit we will form, and report to you, our final opinion by reference to all matters that could be significant to users of the financial statements, including the total effect of any audit misstatements, and our evaluation of materiality at that date.

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## Key messages

Planning Materiality for the audit has been determined at £1.8 million, representing 1.5% of estimated gross expenditure.

Tolerable Error is set at £0.9 million.

Our SAD nominal amount is £90,000.

# 3. Financial statements audit (cont.)



We outline our initial assessment of the financial statement risks facing the IJB, identified through our knowledge of the environment in which the IJB operates; discussion with those charged with governance and officers; and through handover and transition arrangements with your previous auditor.

Our risk assessment is ongoing throughout the conduct of our audit and we will report to you any notable changes in our risk assessment during the course of our work.

Risk assessment includes the requirement to consider whether the financial statements as a whole are free of material misstatements whether caused by fraud or error.

## Financial statement risks

Auditing standards require us to consider whether any of the risks identified are 'significant' risks to our audit of the IJB and the group. Financial statement significant risks are defined as those with a higher likelihood of occurrence and, if they were to occur, a higher magnitude of impact which could result in a material misstatement of the financial statements.

We are required to perform specific procedures over those risks. These include the identification and testing of the design and implementation of key controls designed to address the risks plus performance of additional substantive procedures in response to the specific risk. We are also required to specifically highlight these significant risks to 'those charged with governance' i.e. the Audit and Risk Committee.

Significant risks (including fraud risks)	Our audit approach
<b>Risk of fraud in revenue recognition</b>	
<p>Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting IJB, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.</p> <p>Given the nature of the funding to the IJB, we apply the concept of Practice Note 10 and consider the risk of fraud to be in respect of expenditure recognition.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>▶ Review and test expenditure recognition policies.</li> <li>▶ Review, test and discuss with management any accounting estimates on expenditure recognition for evidence of bias.</li> <li>▶ Develop a testing strategy to test material expenditure streams.</li> <li>▶ Review and test expenditure cut-off around the year end.</li> </ul>
<b>Risk of management override</b>	
<p>As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> <li>▶ Testing the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements.</li> <li>▶ Reviewing accounting estimates made in preparation of the financial statements for any evidence of management bias.</li> <li>▶ Evaluating the business rationale for any significant unusual transactions.</li> </ul>

## Key messages

### Significant risks:

In line with auditing standards we identify significant risks in respect of fraud in expenditure recognition, and in respect of the risk of management override of controls.

At this stage of our audit planning, we have not identified any other significant financial statement risks. We will confirm our updated risk assessment as part of our Annual Audit Report.

Our approach is designed to develop an audit strategy that is responsive to the IJB's risks of material misstatement for transactions and account balances in the financial statements. We obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud.

In addition, we plan and perform certain general audit procedures on every audit to address areas that are not directly related to financial statement account assertions. Examples of such procedures include compliance with applicable laws and regulations, litigation and claims, related parties and consideration of fraud.

We remain aware of any changes in the applicable financial reporting framework.

## Overview of audit approach

We determine which accounts, disclosures and relevant assertions could contain risks of material misstatement based on our understanding of the business, understanding of internal control arrangements and our determination of planning materiality.

We document and walkthrough the key accounting processes within the IJB, in particular with respect to how the IJB has established budgetary oversight of its annual expenditure budget. As part of this work, we will also look to understand the need for an interface with audit work at NHS Lothian. We will also have regard to the work undertaken by internal audit in the year in respect of the IJB's internal controls.

To ensure efficiency in our audit work, we employ data analytics as appropriate to allow the testing of full populations of financial transactions.

## Responsibilities in respect of fraud and error

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

Our responsibility is to plan and perform audits to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud. As auditors, we approach each engagement with a questioning mind that accepts the possibility that a material misstatement due to fraud could occur, and design the appropriate procedures to consider such risk.

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

- Identifying fraud risks during the planning stages.
- Enquiry of management about risks of fraud and the controls to address those risks.
- Understanding the oversight given by those charged with governance of management's processes over fraud.
- Consideration of the effectiveness of management's controls designed to address the risk of fraud.
- Determining an appropriate strategy to address any identified risks of fraud.
- Performing mandatory procedures regardless of specifically identified risks.

## Changes to the Accounting Code of Practice in 2016/17

We will engage with management to consider their assessment and incorporation of changes to the 2016/17 Accounting Code. Principal amongst these is the introduction of a new expenditure and funding analysis to enable greater transparency and linkage to the management commentary on the performance of the IJB. In addition, the comprehensive income and expenditure statements will now provide a service analysis in line with the basis of the IJB's operational structure, as far as is applicable.

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## Key messages

We obtain an understanding of the IJB's control environment and key accounting processes in operation.

Management has primary responsibility for the prevention and detection of fraud. We design appropriate audit procedures in response to identified fraud risk factors, for the purpose of detecting material misstatements.

There are no significant changes to the Accounting Code of Practice for 2016/17 although a new expenditure and funding analysis is required.

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## **4. Wider scope audit and other work**

# 4. Wider scope audit framework



Together the Accounts Commission and the Auditor General for Scotland agreed the four dimensions set out in the Code which comprise the wider-scope audit for public sector in Scotland. These are: financial sustainability, financial management, governance and transparency, and value for money.

The Code sets out an expectation that 'significant' risks identified through our planning process that relate to the wider scope dimensions will be communicated with you. In undertaking our risk assessment in respect of the wider scope audit areas, we distinguish between the definition of 'significant risks' which apply to the audit of the financial statements, by referring in our report to 'Wider Scope Audit Focus Areas'.

The focus areas represent where we have identified that we will direct most of our audit effort in the year.

## Risk Assessment

The following two Wider Scope Audit Focus Areas have been identified for 2016/17. In undertaking our work, we will factor in the relatively early stage of the IJB's maturity. Our five-year appointment will provide the opportunity to revisit our considerations as the IJB's arrangements continue to evolve.

Wider Scope Audit Focus Areas	Our audit approach
<b>Financial sustainability</b>	
<p>Achieving a balanced budget for the IJB in 2016/17 will be achieved by the partners providing additional resources.</p> <p>The 2017/18 budget has not yet been approved as this is dependent on the budget allocations from both Midlothian Council and NHS Lothian.</p> <p>Delivering on the IJB's strategic priorities will, however, require an ability to transform and deliver significant recurring efficiency savings.</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> <li>▶ The effectiveness of the financial planning systems and identifying and addressing risks to financial sustainability across shorter and longer terms.</li> <li>▶ Whether the IJB can demonstrate the affordability and effectiveness of funding and investment decisions that it has made.</li> <li>▶ The appropriateness of the arrangements to address identified funding gaps and whether the body can demonstrate that these arrangements are working.</li> </ul>
<b>Linkage to Accounts Commission Strategic Priority:</b>	
<ul style="list-style-type: none"> <li>▶ The clarity of priorities and quality of long-term planning to achieve these.</li> <li>▶ How effective are arrangements to ensure board members and officers have the right knowledge, skills and time to lead and manage delivery of priorities.</li> </ul>	
<b>Governance and transparency</b>	
<p>The Board and officers of the IJB are responsible for establishing robust governance arrangements. This includes ensuring effective systems of internal control, including arrangements to safeguard public money, and compliance with applicable laws and regulations.</p> <p>With this being the first year of full operation of the IJB, it is important that appropriate governance arrangements are established from the outset, to support delivery of strategic objectives and transparent scrutiny of the IJB's performance.</p>	<p>Our approach will focus on consideration of whether:</p> <ul style="list-style-type: none"> <li>▶ The IJB can demonstrate that the governance arrangements are appropriate and operating effectively.</li> <li>▶ There is effective scrutiny, challenge and transparency on decision making and financial and performance reports.</li> <li>▶ Finance and performance reports support effective scrutiny and challenge.</li> </ul>
<b>Linkage to Accounts Commission Strategic Priority:</b>	
<ul style="list-style-type: none"> <li>▶ The clarity of priorities and quality of long-term planning to achieve these.</li> </ul>	

## Key messages

The wider scope audit as set out in the Code plays a key role in the public sector audit framework in Scotland. We have identified two wider-scope audit focus areas for 2016/17. Firstly, we will consider the work undertaken by chief officers and the IJB to consider the achievement of Financial Sustainability in delivery of key priorities.

Secondly, in respect of Governance and Transparency, we will consider the arrangements established to ensure effective governance and scrutiny and transparency in performance reporting.

In local government, the Accounts Commission has also agreed its five Strategic Audit Priorities, which should be incorporated in audit planning.

Our annual audit work in respect of the wider scope audit, and the judgements and conclusions reached in these areas, contribute to the overall assessment and assurance on the achievement of Best Value.

### Other aspects of the wider scope audit

- **Financial management** - With the significant financial challenges facing public sector bodies, it is essential that the IJB has robust financial management arrangements to ensure that it can continue to deliver services. This dimension has more focus therefore on in-year budget management and maintaining a sound system of internal control.
- **Value for Money** – this dimension is focused on how the IJB effectively utilises its resources and the arrangements in place to continually improve services.

We undertake work in respect of these additional audit dimensions but have not at this time scoped these as having a need for higher audit focus.

Key to the assessment and judgement in the wider scope audit areas is the quality of the IJB's self-evaluation to be able to demonstrate the quality and effectiveness of their arrangements.

### Accounts Commission's Strategic Audit Priorities

In undertaking our work in respect of the four audit dimensions, we draw your attention to the Accounts Commission's recently published Strategic Audit Priorities, being:

- The clarity of priorities and quality of long-term planning to achieve these.
- How effective is the evaluation of options for significant changes in delivering services.
- How effective are arrangements to ensure board members and officers have the right knowledge, skills and time to lead and manage delivery of priorities.
- How effectively are citizens involved in decisions about services.
- The quality of public performance reporting to help citizens gauge improvement.

We take these into account when planning our work and link them to the wider scope audit focus areas identified.

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### Key messages

Key to the assessment and judgement in the wider scope audit areas is the quality of the IJB's self-evaluation to be able to demonstrate the quality and effectiveness of their arrangements.

In planning and performing our audit work, we take into account the Accounts Commission's Strategic Audit Priorities.

## **5. Other audit responsibilities**



## 4. Wider scope audit and other work (cont.)



Under the terms of our appointment, our role and responsibilities extend beyond the audit of the financial statements and the wider-scope audit dimensions.

There a number of further areas of audit activity that we will cover over the term of our appointment. These include for example, participation in the wider Shared Risk Assessment at local authority level which may impact on the IJB, our responsibilities in relation to Following the Public Pound and the impact of national studies undertaken by Audit Scotland.

### **Shared Risk Assessment (SRA)**

While there is no formal SRA process for integration authorities, the Local Area Network (LAN) for the associated local authority will consider health and social care outcomes, governance and partnership working as part of their assessment of the local authority. We are also the appointed auditor of Midlothian Council and participate in the Midlothian Council SRA. The Local Scrutiny Plan for the Council has not been finalised at the time of preparing this report.

### **Following the Public Pound**

Local Authorities have a statutory responsibility to comply with the Accounts Commission / COSLA Code of Guidance on Funding External Bodies and Following the Public Pound (the FtPP Code). By extension, there is an expectation on the IJB to be able to demonstrate adherence to the principles of the FtPP Code, as these are embedded into the new approach to auditing Best Value. As part of our risk based planning approach we will consider the IJB's arrangements to comply with the FtPP Code.

Over our five year appointment, Audit Scotland undertake performance audits across local authority bodies. During 2017, Audit Scotland will be undertaking a performance audit relating to Arms Length Organisations (ALEOs). It is not clear at this stage to what extent IJB's will be scoped into this work.

We link this work directly to that undertaken to support the conclusions on the Governance and Transparency audit dimension.

### **Audit Scotland – National Study Programme**

Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. Audit Scotland ask us to ensure that public bodies review the national studies relevant to them at an appropriate committee level and act on them accordingly.

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### **Key messages**

The extent of our other audit responsibilities is expected to develop as the IJB's operations mature. We have regard to statutory responsibilities on local authority bodies in respect of compliance with the Following the Public Pound Code, to the extent it is applicable to the IJB's operations.

## **6. Team, fees and deliverables**

# 6. Team, fees and deliverables



We identify an audit team with the relevant skills and experience. All member of our core team have several years experience in the audit of local government. The engagement team is led by Stephen Reid, who is one of three partners leading EY's Government and Public Sector practice in the UK. Stephen is supported by Keith Macpherson, our Head of Government & Public Sector Audit in Scotland. John Boyd will be the senior manager for the financial statements audit.

The audit fee is determined in line with Audit Scotland's fee setting arrangements, set out in recent communications to all audited bodies in line with their publication on 'Our Approach to setting audit fees'

([http://www.audit-scotland.gov.uk/uploads/docs/um/audit\\_fee\\_approach.pdf](http://www.audit-scotland.gov.uk/uploads/docs/um/audit_fee_approach.pdf)).

## Audit team

Individual	Contact details
Stephen Reid	T: 07795 307 033 E: sreid2@uk.ey.com
Keith Macpherson	T: 07831 136 496 E: kmacpherson@uk.ey.com
John Boyd	T: 07870 738834 E: jboyd1@uk.ey.com

## 2016/17 Audit fee

Due to the nature of the IJB, with this being the first full year of operation, no expected fee has been set centrally by Audit Scotland. At this time, we are still in discussion with senior officers in respect of the audit work requirements and consequently we have not yet agreed the fee with them. We will confirm this to you in due course.

## Timeline and deliverables

Audit activity	Deliverables
Planning, identification and assessment of risks: December 2016 – March 2017	
<ul style="list-style-type: none"><li>▶ Introductory meetings with senior management</li><li>▶ Handover discussions with outgoing auditor</li><li>▶ Review of Audit Scotland planning guidance</li><li>▶ Review of IJB documentation</li></ul>	1. Annual Audit Plan, presented to Audit and Risk Committee, 9/3/2017
Design and execute response to risks (April – Aug 2017)	
<ul style="list-style-type: none"><li>▶ Onsite fieldwork, documentation and walkthrough of key accounting processes</li><li>▶ Testing of key financial controls as appropriate</li><li>▶ Commencement of year-end substantive audit fieldwork on unaudited financial statements</li></ul>	2. Submit any fraud returns to Audit Scotland by 26/5/2017
Conclude and communicate (Sept – Oct 2017)	
<ul style="list-style-type: none"><li>▶ Conclude on results of audit procedures</li><li>▶ Audit clearance meeting with senior management, and report findings to those charged with governance</li><li>▶ Issue opinion on the IJB's financial statements</li></ul>	3. Annual Audit Report, to Audit and Risk Committee (date tbc) 4. Certify Annual Accounts – by 30/9/2017 5. Submit other assurance / data returns as required (requirements to be confirmed)

## Key messages

Stephen Reid is your audit engagement partner, supported principally by Keith Macpherson and John Boyd.

As this is first year of the IJB audit, no central fee has been set by Audit Scotland for any integration authorities. We will agree the fee with chief officers on completion of our audit planning, and our understanding of the year-end audit requirements.

We have agreed a high level timetable with management to meet statutory and other guidance for reporting.

# Appendices

**A – Auditor Independence**

**B – Required Communications**

The APB Ethical Standards and ISA (UK and Ireland) 260 'Communication of audit matters with those charged with governance', requires us to communicate with you on a timely basis on all significant facts and matters that bear on our independence and objectivity.

The Ethical Standards require that we do this formally both at the planning stage and at the conclusion of the audit, as well as during the audit if appropriate.

The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communication	
Planning stage	Final stage
<ul style="list-style-type: none"> <li>▶ The principal threats, if any, to objectivity and independence identified by EY including consideration of all relationships between you, your affiliates and directors and us.</li> <li>▶ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality Review.</li> <li>▶ The overall assessment of threats and safeguards.</li> <li>▶ Information about the general policies and process within EY to maintain objectivity and independence.</li> </ul>	<ul style="list-style-type: none"> <li>▶ A written disclosure of relationships (including the provision of non-audit services) that bear on our objectivity and independence, the threats to our independence that these create, any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed.</li> <li>▶ Details of non-audit services provided and the fees charged in relation thereto.</li> <li>▶ Written confirmation that we are independent.</li> <li>▶ Details of any inconsistencies between APB Ethical Standards, Audit Scotland's Terms of Appointment and your policy for the supply of non-audit services by EY and any apparent breach of that policy.</li> <li>▶ An opportunity to discuss auditor independence issues.</li> </ul>

During the course of the audit we must also communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of our safeguards, for example when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future contracted services, and details of any written proposal to provide non-audit services;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period are disclosed, analysed in appropriate categories.

### Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including any principal threats. However we have adopted the safeguards below to mitigate these threats along with the reasons why they are considered to be effective.

#### Self-interest threats

A self-interest threat arises when EY has financial or other interests in your entity. Examples include where we have an investment in your entity; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with the IJB.

At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services, and we will comply with any of the policies that the IJB may have approved and that are in compliance with Audit Scotland's Terms of Appointment. At the time of writing, no non-audit services have been provided.

## ***Self-interest threats (cont.)***

A self-interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to the IJB. We confirm that no member of our audit engagement team, including those from other service lines, is in this position, in compliance with Ethical Standard 4.

There are no self-interest threats at the date of this report.

## ***Self-review threats***

Self-review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no other self-review threats at the date of this report.

## ***Management threats***

Partners and employees of EY are prohibited from taking decisions on behalf of management of your entity. Management threats may also arise during the provision of a non-audit service where management is required to make judgements or decisions based on that work.

There are no management threats at the date of this report.

## ***Other threats***

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

The 2016/17 audit year is the first year that Stephen Reid has led the audit of the IJB. We assessed this relationship prior to the commencement of the audit period and concluded that there are no considerations that compromise, or could be perceived to compromise, Stephen Reid's independence or objectivity.

## ***Overall Assessment***

Overall we therefore confirm that EY is independent and the objectivity and independence of Stephen Reid, the Audit Engagement Partner and the audit engagement team have not been compromised.

EY has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained. Details of the key policies and processes within EY for maintaining objectivity and independence can be found in our annual Transparency Report, which the firm is required to publish by law. The most recent version of this report is for the year ended June 2016 and can be found here:

<http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2016>

There are certain additional communications that we must provide to the Audit and Risk Committee, which are set out below.

Required communication	Reference
<p><b>Planning and audit approach</b></p> <ul style="list-style-type: none"> <li>▶ Communication of the planned scope and timing of the audit including any limitations.</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Plan</li> </ul>
<p><b>Significant findings from the audit</b></p> <ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations that we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters if any, significant to the oversight of the financial reporting process</li> <li>▶ Findings and issues regarding the opening balances on initial audits</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>
<p><b>Misstatements</b></p> <ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ In writing, corrected misstatements that are significant</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>
<p><b>Fraud</b></p> <ul style="list-style-type: none"> <li>▶ Enquiries of the Audit and Risk Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ A discussion of any other matters related to fraud</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Plan</li> <li>▶ Annual Audit Report</li> </ul>
<p><b>Related parties</b></p> <p>Significant matters arising during the audit in connection with the entity's related parties including, when applicable:</p> <ul style="list-style-type: none"> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the entity</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>
<p><b>External confirmations</b></p> <ul style="list-style-type: none"> <li>▶ Management's refusal for us to request confirmations</li> <li>▶ Inability to obtain relevant and reliable audit evidence from other procedures</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>

## B. Communications (cont.)



Required communication	Reference
<b>Significant deficiencies in internal controls identified during the audit</b>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>
<b>Consideration of laws and regulations</b> <ul style="list-style-type: none"> <li>▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off</li> <li>▶ Enquiry of the Audit and Risk Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit and Risk Committee may be aware of</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>
<b>Independence</b> <p>Communication of all significant facts and matters that bear on EY's objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> <li>▶ The principal threats, and any safeguards adopted and their effectiveness</li> <li>▶ An overall assessment of threats and safeguards</li> <li>▶ Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Plan</li> <li>▶ Annual Audit Report</li> </ul>
<b>Going concern</b> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>
<b>Group audits</b> <ul style="list-style-type: none"> <li>▶ An overview of the type of work to be performed on the financial information of the components, and of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components</li> <li>▶ Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work</li> <li>▶ Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted</li> <li>▶ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Report</li> </ul>
<b>Fee information and confirmation of additional certification work</b> <ul style="list-style-type: none"> <li>▶ Details of the audit fee</li> <li>▶ Summary of additional audit certification work undertaken</li> </ul>	<ul style="list-style-type: none"> <li>▶ Annual Audit Plan</li> <li>▶ Annual Audit Report</li> </ul>



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