

Water Industry Commission for Scotland

Annual Audit Plan 2017/18



 AUDIT SCOTLAND

Prepared for Water Industry Commission for Scotland

February 2018

Who we are

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

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



About us

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

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

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

Contents

Risks and planned work	4
Audit risks	4
Reporting arrangements	6
Audit fee	6
Responsibilities	6
Audit scope and timing	8
Financial statements	8
Materiality	8
Internal audit	10
Audit dimensions	10
Independence and objectivity	11
Quality control	11
Adding Value	11

Risks and planned work

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

Audit risks

3. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for the Water Industry Commission Scotland (WICS). We have categorised these risks into financial risks and wider dimension risks. The key audit risks, which require specific audit testing, are detailed in [Exhibit 1](#).

Exhibit 1

2017/18 Key audit risks

Audit Risk	Source of assurance	Planned audit work
Financial statement issues and risks		
<p>1 Risk of management override of controls</p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance.</p>	<p>Detailed testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Focused testing of accruals and prepayments.</p> <p>Evaluation of significant transactions that are outside the normal course of business.</p>
<p>2 Risk of fraud over income</p> <p>WICS receives the majority of its income from two sources. These are the statutory contributions from Scottish Water and the levies charged to licensed providers. However, in accordance with ISA 240, the extent of income means there is an inherent risk of fraud.</p>	<p>Financial monitoring reports are produced on a monthly basis and reviewed by management. These are presented to the Board and Audit Committee as a standing agenda item. These arrangements allow for monitoring of income and expenditure, providing explanations on any significant</p>	<p>Analytical procedures on income streams.</p> <p>Detailed testing of revenue transactions focusing on the areas of greatest risk.</p>

Audit Risk	Source of assurance	Planned audit work
movements		
<p>3 Risk of fraud over expenditure</p> <p>The revised version of Practice Note 10, Audit of Financial Statements of Public Sector Bodies in the UK, states that there is a risk that misstatements may arise from fraudulent financial reporting where the audited body may manipulate its results to meet externally set targets. Therefore, there is a risk of material misstatement due to fraud related to expenditure.</p>	<p>Financial monitoring reports are produced on a monthly basis and reviewed by management. These are presented to the Board and Audit Committee as a standing agenda item. These arrangements allow for monitoring of income and expenditure, providing explanations on any significant movements</p>	<p>Analytical procedures on expenditure.</p> <p>Detailed testing of expenditure focusing on the areas of greatest risk.</p>
Wider dimension risks		
<p>4 Financial sustainability</p> <p>WICS is a member of the Falkirk Council Local Government Pension Scheme (LGPS). Following the triennial valuation of the scheme, indications are that the employer pension contributions will increase from 19.1% to 28.3% from 1 April 2018.</p> <p>Management estimate these additional contributions will equate to over £100,000 per annum.</p> <p>WICS may be able to fund the additional contributions from existing cash balances in the short term. However there is a risk that this is not sustainable in the longer term.</p>	<p>WICS has prepared a revised Corporate Plan for the 6-year period 2018-24. The budget outlined in this plan includes an increase in levy to cover the potential pension costs of 28.3% and would cover an increase of up to 30% from 1 April 2021. This plan is with the Scottish Government for approval.</p>	<p>Review of financial monitoring reports and WICS' year-end financial position.</p>
<p>5 Performance management</p> <p>WICS is required to include performance measurement analysis within its annual report. In our 2016/17 annual audit report, we noted that it was not clear how WICS currently monitors and reports performance and progress against delivering their core functions as established in the corporate plan. There is a risk that WICS be may not be able to sufficiently monitor performance and identify areas for improvement.</p>	<p>WICS is developing performance management indicators as part of an overall review of its governance framework. It is hoped that these indicators can be agreed and monitored from 1 April 2018.</p>	<p>Consideration of the performance information included within the performance report in the 2017/18 financial statements.</p>

Reporting arrangements

4. Audit reporting is the visible output for the annual audit. All annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

5. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officer(s) to confirm factual accuracy.

6. We will provide an independent auditor's report to WICS, Scottish Parliament and the Auditor General for Scotland setting out our opinions on the annual accounts. We will provide the Accountable Officer and the Auditor General for Scotland with an annual report on the audit containing observations and recommendations on significant matters which have arisen in the course of the audit.

Exhibit 2

2017/18 Audit outputs

Audit Output	Target date	Committee Date
Annual Audit Report	September 2018	Audit committee - 24 July 2018 Board – September 2018 (TBC)
Independent Auditor's Report	September 2018	Board – September 2018 (TBC)

Audit fee

7. The proposed audit fee for the 2017/18 audit of WICS is £12,910 (2016/17: £12,710). In determining the audit fee we have taken account of the risk exposure of WICS, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited financial statements, with a complete working papers package on 4 June 2018.

8. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

Responsibilities

Audit and Risk Committee and the Accountable Officer

9. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

10. The audit of the financial statements does not relieve management or the Audit and Risk Committee as those charged with governance, of their responsibilities.

Appointed auditor

11. Our responsibilities as independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice (including supplementary guidance) and guided by the auditing profession's ethical guidance.

12. Auditors in the public sector give an independent opinion on the financial statements and other specified information accompanying the financial statements. We also review and report on the arrangements within the audited body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Financial statements

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

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

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

- whether they give a true and fair view of the financial position of WICS and their expenditure and income
- whether they have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements
- the regularity of the expenditure and income.

Materiality

15. We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinion in the auditor's report.

16. We calculate materiality at different levels as described below. The calculated materiality values for WICS are set out in [Exhibit 3](#).



Exhibit 3

Materiality values

Materiality level	Amount
Planning materiality – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It has been set at 1% of gross expenditure for the year ended 31 March 2018 based on the prior year audited accounts.	£36,000
Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 75% of planning materiality.	£27,500
Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 5% of planning materiality.	£2,000

17. We review and report on other information published with the financial statements including the performance report and accountability report, which include the governance statement and remuneration and staff report. Any issues identified will be reported to the Audit and Risk Committee.

Timetable

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

Exhibit 4

Financial statements timetable

 Key stage	 Date
Latest submission date of unaudited annual accounts with complete working papers package	4 June 2018
Latest date for final clearance meeting	By end of June 2018
Issue of letter of representation and proposed independent auditor's report	July 2018
Agreement of audited unsigned annual accounts	July 2018
Issue of Annual Audit Report including ISA 260 report to those charged with governance	By end of September 2018
Independent auditor's report signed	By end of September 2018

Internal audit

19. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. Internal Audit is provided by BDO. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carried out an assessment of the internal audit function and determined that it has sound documentation standards and reporting procedures in place.

Areas of Internal Audit reliance

20. In respect of our wider dimension audit responsibilities we plan to consider areas of internal audit work including:

- HR processes
- Hydro Nation
- Strategic review of charges
- Budgeting and management reporting

Audit dimensions

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

Exhibit 5

Audit dimensions



Source: Code of Audit Practice

22. In consideration of the size and nature of the financial transactions, and functions provided by WICS, and based on our professional judgement, we have concluded that the full application of the wider scope is not appropriate or proportionate.

23. In such circumstances, the Code of Audit Practice requires auditors to undertake annual audit work on the wider scope that enables conclusions to be reached on:

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

24. We will review the annual governance statement and assess the financial sustainability of the WICS as part of our financial statements audit. Conclusions on these matters will be reported accordingly in our annual audit report.

Independence and objectivity

25. Auditors appointed by the Accounts Commission or Auditor General must comply with the Code of Audit Practice and relevant supporting guidance. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has in place robust arrangements to ensure compliance with these standards including an annual “fit and proper” declaration for all members of staff. The arrangements are overseen by the Director of Audit Services, who serves as Audit Scotland’s Ethics Partner.

26. The engagement lead for WICS is Stephen O’Hagan (Senior Audit Manager). Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of WICS.

Quality control

27. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor’s report or opinion is appropriate in the circumstances.

28. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice (and relevant supporting guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews, internal quality reviews and is currently reviewing the arrangements for external quality reviews.

29. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time and this may be directed to the engagement lead.

Adding Value

30. Through our audit work we aim to add value to WICS. We will do this by ensuring our Annual Audit Report provides a summary of the audit work done in the year together with clear judgements and conclusions on how well the WICS has discharged its responsibilities and how well it has demonstrated the effectiveness of its arrangements. Where it is appropriate we will recommend actions that support continuous improvement and summarise areas of good practice identified from our audit work.

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Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
T: 0131 625 1500 E: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk