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WALES AUDIT OFFICE

Final Audit Findings Report

Year ended 31 March 2016

Presented to those charged with Governance
By RSM UK Audit LLP

on 6 June 2016



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This report has been prepared for the sole use of Wales Audit Office and must not be disclosed to any third party, or quoted or referred to, without our written consent. No responsibility is assumed to any other person in respect of this report.

1 INTRODUCTION AND COVERAGE

This report summarises our key findings in connection with the audit of the financial statements of Wales Audit Office in respect of the year ended 31 March 2016.

The scope of our work has already been communicated to you via our Audit Plan document dated 25 February 2016.

A summary of adjusted and unadjusted misstatements identified during the audits has been prepared and is included in Section 5.

We consider that the audit approach adopted will provide the Audit Risk and Assurance Committee (ARAC) with the required confidence that a thorough and robust audit has been carried out and can confirm that, at the date of this report, we anticipate no modifications from our pro-forma audit report provided in the Audit Plan previously communicated to you.

Materiality is a judgemental area since it has both quantitative and qualitative elements. It is necessary to consider not only the impact of an error on the financial statements as a whole, but also on the individual accounting items affected, taking into account the level of risk associated to that item. Additionally, the cumulative impact of all unadjusted errors must be considered. As a guide our performance materiality used was £142,000.

2 AUDIT AND ACCOUNTING ISSUES IDENTIFIED AT PLANNING STAGE

Management over ride of internal controls

Key area of audit focus	Systems of internal control are designed to mitigate inherent risks of error within the core control systems to an acceptable level. By nature, a management override or by-pass of controls cannot be eliminated by the implementation of controls and therefore as part of our audit we will perform additional tests of detail to address this risk.
Our approach	<p>We will test the appropriateness of a sample of journal entries recorded in the general ledger and other adjustments made in the preparation of financial statements, tracing selected entries back to source documentation.</p> <p>We will review significant accounting estimates and policies which could involve bias resulting in a material misstatement.</p> <p>We will discuss the basis and business rationale for any significant non-routine or contentious transactions which come to our attention during the course of our audit and will fully report the outcomes of our testing in our audit findings report.</p>
Response	The testing was completed as planned with no significant issues identified to report to management.

Income recognition, WIP and deferred income

Key area of audit focus	The recognition of income, WIP and deferred income is considered to be a high risk due to the level of judgement applied to the stage of completion of an audit assignment.
Our approach	We will select a sample of projects that have commenced throughout the year and test the revenue recognised with reference to the stage of completion of the assignment in order to determine that the revenue recognition is appropriate and consequently whether the WIP and deferred income are appropriately stated.

Income recognition, WIP and deferred income

Response

In the prior year we recommended that the Office should consider actual out-turn on projects overall and factor this in when calculating stage completion for revenue recognition.

Management have reduced revenue recognised for projects where costs were expected to exceed the quoted fees.

We have reviewed costs on open projects at the year end and on average costs exceed the budget upon which the revenue is based by approximately 4%.

If this was applied to the remaining projects, revenue would be reduced by further £193k. However as the unadjusted amounts estimated in the prior year was £206k the in year net impact is only £12k in the current year. This amount has been included as a potential adjustment in section 5 below.

As in prior years we have estimated the potential amount of refund that would be due when projects which are currently in a deferred income position complete. A potential reclassification has been included in section 5 below.

Reputation

Key area of audit focus

Due to public interest in the financial statements there is a desire to maintain reputation and demonstrate exemplary financial management. Accounting judgements may be influenced by the desire to demonstrate good financial management and remain within the Estimate.

Our approach

Independent technical review of the accounts and key judgement areas.
Review of judgemental aspects in year-end balances particularly focusing on any;

- Round sum provisions
- Estimates
- Recoverability of debtors
- Disclosure of remuneration

Response

No significant issues were identified to be reported to management.

3 AUDIT AND ACCOUNTING ISSUES IDENTIFIED DURING THE AUDIT

Caerphilly Contingent liability / CIPFA

Issue

A complaint has been made to the Auditor General regarding an appointed auditor's public interest report on a local authority. The report resulted in the suspension of three local authority employees and disciplinary and criminal investigations.

Criminal charges against the three employees were dismissed, but the disciplinary process has not yet concluded.

As part of the process of responding to the criminal investigation, the Office identified that a formal record of the approval of the Chartered Institute of Public Finance & Accountancy (CIPFA), necessary to make a person eligible for appointment as an auditor, could not be located. Legal advice, however, confirms that the actions of CIPFA qualified individuals in the role of appointed auditor are valid.

There has been media coverage of this issue.

Resolution

No disclosure is required in the financial statements as no claim has been made against the Office. Furthermore, the legal advice indicates that no claim is likely in practice and that it is not clear that there is a means by which it could be raised. The position could be defended if a claim were made.

It is considered remote that a claim will be made.

4 REGULARITY ISSUES IDENTIFIED DURING THE AUDIT

Gifts and hospitality policy

Issue	We noted as part of our review of the gifts and hospitality policy that alcoholic drink gifts are to be auctioned off with the proceeds going to a nominated charity. We identified one instance where this policy was not followed. The amounts involved totalled £25.
Resolution	Whilst the policy was not followed we note that the gifts had been appropriately declared by the individuals concerned. This is considered trivial and does not impact our opinion.

Refunds

Our approach	Under the provisions of the Public Audit Wales Act the WAO is not permitted to charge audit fees in excess of cost. In such cases where the cost of conducting the audit is lower than the fee a refund is required to the audited body. It is WAO policy to issue these refund once the project has closed. We noted one instance where this policy was not followed. The value of the refund is £6k.
Recommendation	Controls over refunds should be reviewed to ensure that similar commissions do not happen in future.
Response	Controls are now in place to identify all potential refunds. The accounts have been restated to take this refund into account.

Contractors

Our approach	<p>The Office places all self-employed contractors on the payroll to ensure that there is no question that could be raised by HMRC regarding employment status.</p> <p>As a result the Office pays employers national insurance at 13.8% over and above the contractor standard rates. In the year the additional payroll costs for all contractors were £42k.</p> <p>This is not material to our regularity opinion.</p>
Recommendation	Management should consider whether the approach taken represents value for money or whether processes should be put in place to either reduce the paid rates or to review the contractor's specific circumstances and evaluate if they would be deemed an employee or a contractor under the HMRC rules in order to prevent incurring avoidable costs.

Contractors

Response

The office consider that value for money has been addressed in the setting of the contractor rates as these are compared to the in-house cost of completing the work.

A process will be put in place to assess employment status for new self-employed contractors.

5 UNADJUSTED/ADJUSTED MISSTATEMENTS

A summary of the unadjusted/adjusted errors identified during the course of our work is set out below, analysed between errors of fact and differences in judgement.

We have not disclosed below those items that we consider to be “clearly trivial” in the context of our audit. For this purpose we consider “clearly trivial” to be any matter less than £5k individually and £10k in aggregate.

We advised management of all these misstatements throughout the audit and requested management to correct them.

Wales Audit Office

	Profit (£'000)	Net assets (£'000)	
Adjusted misstatements	Dr/(Cr)	Dr/(Cr)	
Deferred income	-	206	Being the judgemental reclassification of potential refunds included within deferred income.
Trade and other payables	-	(206)	
Training Costs – Operating Costs Accruals	11	(11)	Being the accrual of training costs in January to March 2016 that were invoiced in April 2016.
Income	6	-	Being the adjustment for additional client refunds identified.
Trade and other payables	-	(6)	
Other operating expenses	41	-	Being the late client adjustment to reinstate the previously released HMRC provision for the death in service settlement.
Staff costs	21	-	
Provisions	-	(62)	
Total	79	(79)	
Unadjusted misstatements Factual	Dr/(Cr)	Dr/(Cr)	
Unadjusted misstatements Judgemental	Dr/(Cr)	Dr/(Cr)	
WIP	-	12	Judgemental revenue adjustment for stage completion ¹ .
Income	(12)	-	
Total unadjusted	(12)	12	

¹ The actual adjustment impacting current year out-turn is £193,000. The adjustment above takes into account the unadjusted error in the prior year of £206,000. Management consider that they currently have appropriate work in progress provision in place and do not wish to adjust for this judgemental potential. We accept this as the adjustment would not be material to the reported result and is an estimate only.

6 SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL

There were no significant control deficiencies identified. This does not constitute a comprehensive statement of all deficiencies that may exist in internal controls or of all improvements which may be made and has addressed only those matters which have come to our attention as a result of the audit procedures performed. An audit is not designed to identify all matters that may be relevant to you and accordingly the audit does not ordinarily identify all such matters.

Internal control recommendation not considered as significant in the context of ISA 265

We have set out below internal control recommendations which came to our attention during the course of our audit work.

Segregation of duties

Fact and potential consequence	<p>A member of the finance team is the administrator for COA and the bank payment system and therefore can both submit payments and authorise payments.</p> <p>The other members of the finance team are split into those who can submit and those who can authorise and thus providing sufficient segregations of duties. This has been previously identified by the finance team and as such this member of staff's bank payment card was being held by the director of finance to mitigate the risk. The card is provided to the member of the finance team if required and any activity is monitored.</p>
Possible action	<p>We recommend that this member of the finance team is removed as administrator and in their place the director of finance becomes the administrator for the system. The director of finance will be administrator, however as he does not have a payment card will not be able to make payments. As a result no member of the finance team could process an entire transaction alone.</p>
Management response	<p>The recommendation was accepted by management.</p>
Timing of implementation and responsibility	<p>Changes have already been implemented.</p>

Firms invoices

Fact and potential consequence	<p>We noted that one of the external firms used had effectively issued credit notes for c. £110k of work which had been recognised in the prior year.</p> <p>Overall the correct invoicing to the end users had been invoiced over the duration of the work but the timing of revenue recognition and invoicing was split incorrectly over the two years.</p> <p>There is a risk that revenue is recognised inappropriately.</p>
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Firms invoices

Possible action	<p>Firm's statements should be closely reviewed and credit balances should be challenged and explanations sought.</p> <p>Some form of budgeting and review should be put in place for this outsourced work so that costs can be challenged if they are not in line with budget expectations.</p>
Management response	<p>We have historically relied on returns provided by these professional firms to determine the amount of income and expenditure to be recognised in our Accounts. This instance has called this approach into doubt, although the particular Firm involved is no longer contracted to undertake work for the WAO. We will need to discuss with the Financial Audit Practice a reasonable approach to checking the value of work completed by Firms that is consistent with their contractual terms.</p>
Timing of implementation and responsibility	<p>Director of Finance / Head of Financial Audit Practice. By December 2016.</p>

WIP provisioning

Fact and potential consequence	<p>Income recognition is based upon the costs incurred and reflected on the system. If these exceed the fee the revenue recognition is capped at the fee.</p> <p>This method is reliant on audit managers identifying and notifying finance of variations to budget. We are not aware that all managers compare costs to date against budget and re-look at costs to complete.</p> <p>As a result the revenue recognition may be inappropriate.</p>
Possible action	<p>As a minimum a quarterly process should be put in place for audit managers to compare actual costs to budgeted costs to date and to re-consider expected costs to complete on all their jobs.</p> <p>Finance should be notified of all variations above a de – minimus value to allow the revenue recognition to be amended.</p>
Management response	<p>Agreed. Managers are currently asked each month to check that income recognised is consistent with their knowledge of the extent of project completion. We will implement tighter quarterly controls in partnership with Practice Business Managers.</p>
Timing of implementation and responsibility	<p>Finance Team. June 2016.</p>

7 SIGNIFICANT ACCOUNTING POLICIES, DISCLOSURES AND ESTIMATES

Accounting policies and estimates

Accounting disclosures

During the course of our audit, we reviewed the adequacy of the disclosures contained within the financial statements and their compliance with both relevant accounting standards and the requirements of the Companies Act 2006. The following disclosure matters were brought to your attention and subsequently reflected in the revised financial statements:

1. The draft financial statement included an incorrect operating lease commitment for rent payable for the extended Ewloe lease. The commitment should have been £10k higher.
2. The draft financial statements omitted the disclosure of a capital commitment of £10k at year end for IT equipment.
3. The draft financial statements did not include cash and cash equivalents split into funds held commercially and funds held with the Government Banking Service as required by the FReM.
4. The draft financial statements disclosed the real increase in pension and related lump sum at pension age amounts in bands of £5k rather than the £2.5k required by the FReM.
5. The draft financial statements did not make clear which elements of the Remuneration and Staff report were subject to audit.

Under the revised FReM disclosure is required of contingent liabilities that are considered remote if they are potentially material. This is in addition to the requirements of the ISA and covers those potential liabilities that are disclosed under parliamentary reporting requirements. We are not aware of any such liabilities but have agreed with management that a generic statement about complaints in progress would be included,

Significant difficulties identified during the audit

No significant difficulties were encountered during the course of our audit and we would like to take this opportunity thank the finance team for their assistance during the audit.

8 UNCERTAINTIES, RISKS, EXPOSURES, JUDGEMENTAL ISSUES AND GOING CONCERN

There are no further matters that we wish to bring to the attention of the committee.

9 FEES

We confirm that the fees charged during the year in respect of services performed for Wales Audit Office are consistent with those contained within our Audit Plan submitted to you and dated 25 February 2016.

10 INDEPENDENCE

In accordance with International Standard on Auditing (UK and Ireland) 260 "Communication with those charged with governance", there are no changes to the details of relationships between RSM UK Audit LLP and its related entities and Wales Audit Office and its related entities and directors that may reasonably be thought to bear on RSM UK Audit LLP's independence and the objectivity of the audit principal, Jenny Hill and the audit staff and the related safeguards from those disclosed in the Audit Plan dated 25 February 2016.

Jenny has acted as the Audit Principal for the Office for a period of five years. This is the mandatory rotation point for a listed entity. For a non-listed entity our firms policy is to consider at ten years. The AGW has an eight year term.

The committee should give consideration as to which point they wish auditor rotation to happen. RSM have one year remaining on their existing external audit contract.

APPENDIX A - DRAFT LETTER OF REPRESENTATION

RSM UK Audit LLP
Davison House
Forbury Square
Reading
Berkshire
RG1 3EU

Dear Sirs

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2016

We confirm to the best of my knowledge and belief, and having made appropriate enquiries of other senior executives of the Wales Audit Office, the following representations given to you in connection with your audit of the financial statements for the period ended 31 March 2016.

The following representations reflect circumstances up to the date of this letter, on which the financial statements were approved, and management's knowledge and intentions regarding the future of the Wales Audit Office.

Responsibility for financial statements

We acknowledge our responsibilities under the Public Audit (Wales) Act 2013 and Treasury Directions made in accordance with that Act for maintaining adequate accounting records and for preparing financial statements in accordance with the applicable accounting framework that give a true and fair view and for making accurate representations to you.

We confirm that we have taken all the steps we ought to have taken in order to make ourselves aware of any relevant audit information and to establish that it has been communicated to the auditors. We confirm that, as far as we are aware, there is no relevant audit information of which the auditors were unaware.

Availability of information

All the accounting records have been made available to you for the purpose of your audit and all transactions undertaken by the Wales Audit Office have been properly reflected and recorded in the accounting records. All other records and related information have been made available to you, including the minutes of all committee meetings, which are a complete and authentic record of the proceedings at those meetings. I have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud

Related party transactions

We have disclosed to you the identity of the related parties and all related party relationships and transactions of which I am aware. There were no transactions with the WCF and with the audited bodies other than those in the ordinary course of business (fees) requiring disclosure in the financial statements. There were no other transactions with related parties requiring disclosure during the year.

Use of funds and regularity

- We acknowledge our responsibility, as specified by the Public Accounts Committee of the National Assembly under the Public Audit (Wales) Act 2013, for ensuring that expenditure disbursed and income received is applied for the purposes intended by Parliament and the National Assembly for Wales and that the financial transactions conform to the authorities which govern them.
- To the best of our knowledge and belief we confirm that, in all material respects, the expenditure disbursed and income received during the year ended 31 March 2016 have been applied to purposes intended by Parliament and the National Assembly for Wales and the financial transactions conform to the authorities which govern them.
- Neither the board nor the senior management team have knowingly authorised a course of action, the financial impact of which was that transactions infringe the requirements of regularity.
- All transactions undertaken by the Wales Audit Office have been properly reflected and recorded in the accounting records.
- There were no events of which we are aware which involve suspected non-compliance with the framework of authorities which govern the running of the Office.

Assets

1. General

All assets included in the Statement of Financial Position belong to the Wales Audit Office and except as disclosed in the accounts were free from any charge. All non-current assets belonging to the Wales Audit Office are included.

2. Impairment of non-current assets

Each non-current asset is worth to the Wales Audit Office at least the amount at which it is included in the Statement of Financial Position, either through continued use by the Wales Audit Office or through the opportunity for sale on the open market.

Liabilities

1. General

All known liabilities of the Wales Audit Office at 31 March 2016 have been included in the balance sheet. All secured liabilities are disclosed.

2. Contingent liabilities

There were no contingent liabilities at the balance sheet date. All guarantees or warranties or other financial commitments have been fully disclosed in the financial statements. There were no known actual or possible litigation and claims whose effect should be considered when preparing the financial statements.

We confirm we have disclosed to you all banking and financing arrangements including related contracts and hedging products. We confirm that no tax avoidance schemes were used by the Wales Audit Office.

Accounting estimates

We confirm that all significant assumptions used in making accounting estimates, including where applicable those measured at fair value, are reasonable in the circumstances, and appropriately reflect our intentions and our ability to carry out the specific courses of action necessary to justify the accounting estimates and disclosures. The disclosures in the financial statements relating to accounting estimates are complete and appropriate.

We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

Commitments

All commitments of the Wales Audit Office of a material amount, whether of a capital or revenue nature, have either been provided for or noted in the financial statements as appropriate. An adequate provision has been made for any losses, which may be expected to result there from, or from events which had occurred before 31 March 2016.

Remuneration report

All amounts paid to members of the Wales Audit Office Management committee have been appropriately included in the Remuneration Report.

All items of personal expenditure paid by the Wales Audit Office on the Management committee's behalf have either been reimbursed by the individuals concerned or have been treated as benefits in kind.

The benefits in kind in respect of the PAYE settlement will be met by the Wales Audit Office. This has been fully disclosed in the remuneration report.

No member of the Management committee or their connected persons had any indebtedness (or agreement concerning indebtedness) to the Wales Audit Office at 31 March 2016 or at any time during the year.

Governance Statement

We confirm the Governance Statement within the Annual Report fairly reflects the Wales Audit Office's current position in relation to our compliance with internal control requirements set out in HM Treasury's guidance.

Fraud and regulation

We acknowledge that the responsibility for the detection of fraud, error and non-compliance with laws and regulations rests with me. We confirm that we are not aware of any known or suspected frauds, error and non-compliance, involving management, employees or third parties which may have a material effect on the financial statements. We confirm that, insofar as we are able to determine, in my opinion the financial statements are not materially misstated as a result of fraud.

In particular we confirm that the Wales Audit Office has made full disclosure of actual or suspected fraud brought to our attention by employees, former employees and other external parties.

We confirm that there has been no possible or actual instance of non-compliance with those laws and regulations which are central to the Wales Audit Office's ability to conduct its business, except as explained to you and as disclosed in the financial statements.

Events subsequent to the date of the Statement on Financial Position

There were no events, transactions or discoveries since the Statement of Financial Position date which:

- would have a material effect on the financial statements, or
- are of such importance to users of the financial statements that they should be disclosed in the financial statements.

Yours faithfully

Signed on behalf of the board of Wales Audit Office

AGW

Chair of the Board