

Audit Strategy Memorandum

North Tyneside Council



North Tyneside Council

For the year ending 31 March 2017



Contents

Executive summary	1
Audit scope and approach	2
Significant risks and key judgements	4
Timetable and communication	6
Value for money conclusion	8
Fees	10
Our team	11
Appendix A – Service organisations and experts	12
Appendix B – Independence	13
Appendix C - Materiality	14
Appendix D - Our added value	15

Executive summary

Purpose of this report

The Audit Strategy Memorandum sets out our audit plan in respect of the audit of North Tyneside Council ('the Council') for the year ending 31 March 2017, and forms the basis for discussion at the Audit Committee meeting on 29 March 2017.

The plan sets out our proposed audit approach and is prepared to assist you in fulfilling your governance responsibilities. The responsibilities of those charged with governance are defined as overseeing the strategic direction of the entity and obligations related to the accountability of the entity, including overseeing the financial reporting process. Full Council is 'those charged with governance', with the Audit Committee supporting full Council in its role in respect of external audit functions.

Timing of our work	Our audit will be delivered in four main phases as outlined in page 6 of this report. The statutory deadline for the completion of our audit work is 30 September 2017.
Financial statements audit	<p>Significant risks</p> <p>We have identified the following areas on which we will carry out specific audit procedures to mitigate the risks of material misstatements in the Council's financial statements.</p> <ul style="list-style-type: none">• Management override of controls;• Revenue recognition;• Valuation of property, plant and equipment; and• Valuation of the defined benefit pension scheme. <p>Materiality</p> <p>At the planning stage of the audit we have set materiality for the financial statements as a whole at £6.604m. In reporting the results of our work we do not report identified misstatements below a clearly trivial level. We have set this level at £198k.</p>
Value for money conclusion	<p>The work we carry out to form a conclusion on whether the Council has proper arrangements in place for securing economy, efficiency and effectiveness in its use of resources is summarised on page 8. We have identified the following significant risk in respect of our VFM work:</p> <ul style="list-style-type: none">• the level of savings over the period of the medium term financial strategy.
Independence	We have considered any actual, potential or perceived threats to our independence on page 13. We have not identified any such threats at this stage of the audit.

Audit scope and approach

The scope of our work

The detailed scope of our work as your appointed auditor for 2016/17 is set out in the National Audit Office's (NAO) Code of Audit Practice. Our responsibilities and powers are derived from the Local Audit and Accountability Act 2014 ('the 2014 Act') and are summarised below.

Opinion on the financial statements

We are responsible for forming and expressing an opinion on the financial statements. Our audit is planned and performed so to provide reasonable assurance that the financial statements are free from material error and give a true and fair view of the financial performance and position of the Council for the year.

Our audit does not relieve management, the full Council or the Audit Committee on behalf of those charged with governance of their responsibilities.

Value for money conclusion

We are required to conclude whether the Council has proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources. We discuss our value for money work in greater detail later in this report.

Whole of Government Accounts (WGA)

We report to the NAO on the consistency of the Council's financial statements with its WGA submission.

Electors' rights

The 2014 Act requires us to give an elector, or any representative of the elector, the opportunity to question us about the accounting records of the Council and consider any objection made to the accounts by an elector. We also have a broad range of reporting responsibilities and powers that are unique to the audit of local authorities in the United Kingdom.

Our response to the risk of fraud

International Standards on Auditing (ISAs) require us to obtain reasonable assurance that the financial statements are free from material fraud and/or error. There are a range of ways in which fraud may arise in the context of your financial statements and we formally consider the risk of fraud as part of our planning work and design appropriate procedures to mitigate risks identified. We maintain an appropriate level of professional scepticism throughout the audit and are mindful that a material misstatement due to fraud is possible, however our audit should not be relied upon to identify all such misstatements.

Management, the full Council and the Audit Committee on behalf of those charged with governance also have responsibilities in respect of fraud. They are responsible for safeguarding assets and for the prevention and detection of fraud, error and non-compliance with laws and regulations.

We will make enquiries of the Mayor (on behalf of full Council) as part of our audit. Our enquiries will focus on:

- what role the Mayor has in relation to fraud and how it is kept informed of fraud related matters by management;
- what anti-fraud measures are in place and how policies and procedures are monitored; and
- whether the Council is aware of any actual, alleged or suspected fraud.

We will formally write to the Mayor, making the enquiries above, towards the end of the audit cycle.

Our approach to obtaining assurance over service organisations

There are material entries in your financial statements where the Council is dependent on an external organisation. We call these entities service organisations. In Appendix A, we outline our approach to understanding the services received from each organisation and the approach we intend to take to obtain sufficient appropriate evidence over items of account that derive from them.

Our use of experts and other auditors

Management and auditor experts

There are material entries in your financial statements which are provided by management experts. For some of these entries, we will use our own expert to provide us with the assurance we require in relation to the work of your expert.

In addition to setting out information in respect of service organisations, Appendix A also summarises management's experts and our planned audit approach to obtaining assurance over their work.

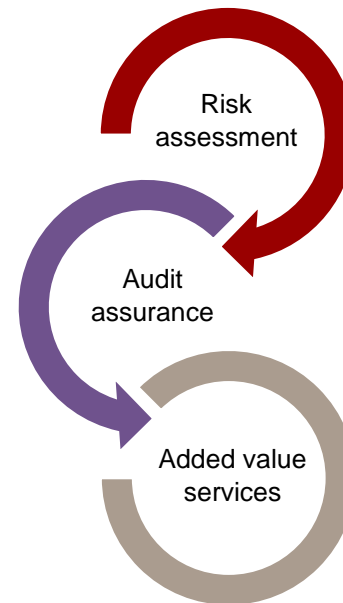
Internal audit

Where appropriate, we will seek to rely on work performed by internal audit where it provides us with the required assurance. We will meet with internal audit to discuss their work programme and findings, and factor this in when determining the most efficient testing strategy.

Where we intend to rely on the work of internal audit, we will evaluate their work and perform our own audit procedures to determine its adequacy for our audit.

Audit efficiency and our use of IT

Innovative and integrated use of IT drives the efficiency and effectiveness of our audit. Your audit team uses the latest IT-based audit solutions and is supported by a team of IT auditors each of who have extensive knowledge of the public sector and providing assurance and advisory services across the public sector.



We know that all organisations are different and face different risks. Our audit platform is modern and flexible and allows us to tailor our audit approach to the specific risks relevant to the Council, while ensuring compliance with underlying auditing standards.

We focus on the risks to your business continuity and those that give rise to a risk of material misstatement in the financial statements. Your audit team has access to a full suite of data analytics tools which allow them to determine the most effective and efficient testing strategy using IT-audit techniques where appropriate.

Significant risks and key judgements

Identified significant risks

As part of our planning procedures we have considered whether there are risks of material misstatement in the Council's financial statements that require special audit consideration. Although we report identified significant risks at the planning stage of the audit, our risk assessment is a continuous process and we regularly consider whether new significant risks have arisen and how we intend to mitigate these risks. Where we identify any significant risks in addition to those set out below, we will report these to the Audit Committee (and full Council) as part of our Audit Completion Report.

Significant risk	How we will mitigate the risk
<p>Management override of control</p> <p>In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Due to the unpredictable way in which such overrides could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.</p>	<p>We will address this risk by performing work in the following areas:</p> <ul style="list-style-type: none"> • accounting estimates affecting amounts included in the financial statements; • significant transactions outside the normal course of business; • the selection and application of accounting policies; and • journals recorded in the general ledger and other adjustments made in preparation of the financial statements.
<p>Revenue recognition</p> <p>There is a risk of fraud in financial reporting relating to income recognition due to the potential to inappropriately record revenue in the wrong period. ISA 240 allows the presumption of fraud relating to revenue recognition to be rebutted in exceptional circumstances, but given the Council's range of revenue sources we have concluded that there are insufficient grounds for rebuttal in 2016/17.</p>	<p>We will evaluate the design and implementation of controls to mitigate the risk of income being recognised in the wrong period. In addition, we will undertake a range of substantive procedures including:</p> <ul style="list-style-type: none"> • testing revenue items recorded to ensure they have been recognised in the appropriate year; • testing adjustment journals; and • for major grant income, agreeing amounts to third party documentation.
<p>Valuation of property, plant and equipment (PPE)</p> <p>The financial statements contain material entries on the balance sheet as well as material disclosure notes in relation to the Council's holding of PPE. The value of the Council's PPE is material to the accounts and involves management judgements over the valuations and useful lives of assets.</p>	<p>We will:</p> <ul style="list-style-type: none"> • consider the Council's arrangements for ensuring that PPE values are reasonable; • engage our own expert to provide data to enable us to assess the reasonableness of the valuations provided by the Council's valuer (where appropriate);

Significant risk	How we will mitigate the risk
	<ul style="list-style-type: none"> • assess the competence, skills and experience of the valuer and the instructions issued to the valuer; and • where necessary, perform further audit procedures on individual assets to ensure the basis of valuations is appropriate.
<p>Valuation of defined benefit pension scheme</p> <p>The financial statements contain material pension entries in respect of retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. This results in an increased risk of material misstatement.</p>	<p>We will:</p> <ul style="list-style-type: none"> • evaluate the Council's arrangements (including relevant controls) for making estimates in relation to pension entries within the financial statements; and • consider the reasonableness of the Actuary's assumptions that underpin the relevant entries made in your financial statements, through the use of an expert commissioned by the National Audit Office.

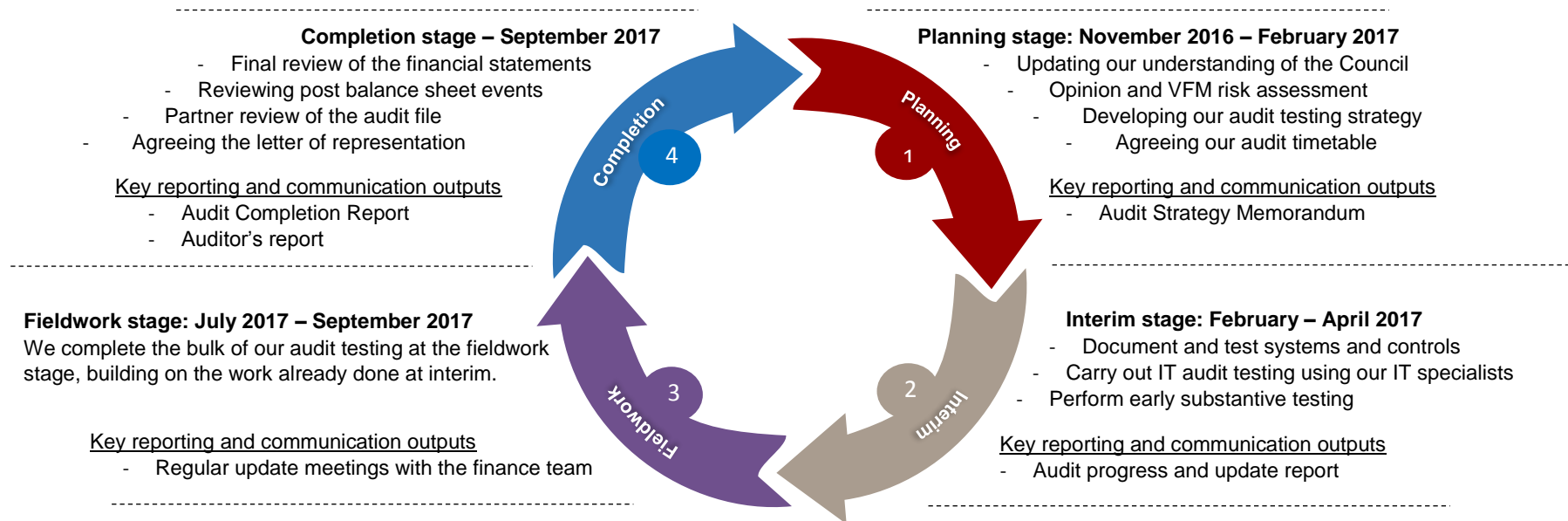
Timetable and communication

Our approach to communication

International Standards on Auditing require us to communicate a number of matters with you at various points during the audit cycle. Later in this section we outline exactly how we will communicate with the Audit Committee on behalf of those charged with governance. As well as being an integral part of our responsibilities under auditing standards, we see two-way communication with the Audit Committee and the Council's staff as being critical to building a robust knowledge of your business, the risks and challenges you face and the plans you have in place to meet those challenges.

Audit timetable

The diagram below outlines the main phases of your audit, when each will be carried out and the outputs that you will receive at each stage. This is underpinned by a 'no surprises' approach to communication that ensures management and the Audit Committee are kept aware of significant issues on a timely basis. We intend to issue our Audit Strategy Memorandum in March 2017, our Audit Completion Report in September 2017 and our Annual Audit Letter in November 2017.



Key communication points

ISA 260 'Communication with those charged with governance' and ISA 265 'Communicating deficiencies in internal control to those charged with governance and management', require us to communicate a number of matters to you. These matters are set out below.

Matter to be communicated	Audit Strategy Memorandum	Audit Completion Report
Our responsibilities in relation to the audit of the financial statements and our wider responsibilities	✓	
Planned scope and timing of the audit	✓	
Significant audit risks and areas of management judgement	✓	
Confirmation of our independence	✓	✓
Responsibilities for preventing and detecting errors	✓	
Materiality	✓	✓
Fees for audit and other services	✓	
Significant deficiencies in internal control		✓
Significant findings from the audit		✓
Significant matters discussed with management		✓
Conclusions on the significant audit risks and areas of management judgement		✓
Summary of unadjusted misstatements		✓
Management representation letter		✓
Our proposed audit report		✓

In addition to the matters outlined above which we are required to communicate under auditing standards, we also communicate regularly with the Audit Committee through our Audit Progress Reports, presented on a quarterly basis. We also report to the Council on an annual basis to summarise our work and main conclusions through our Audit Completion Report and Annual Audit Letter.

Value for money conclusion

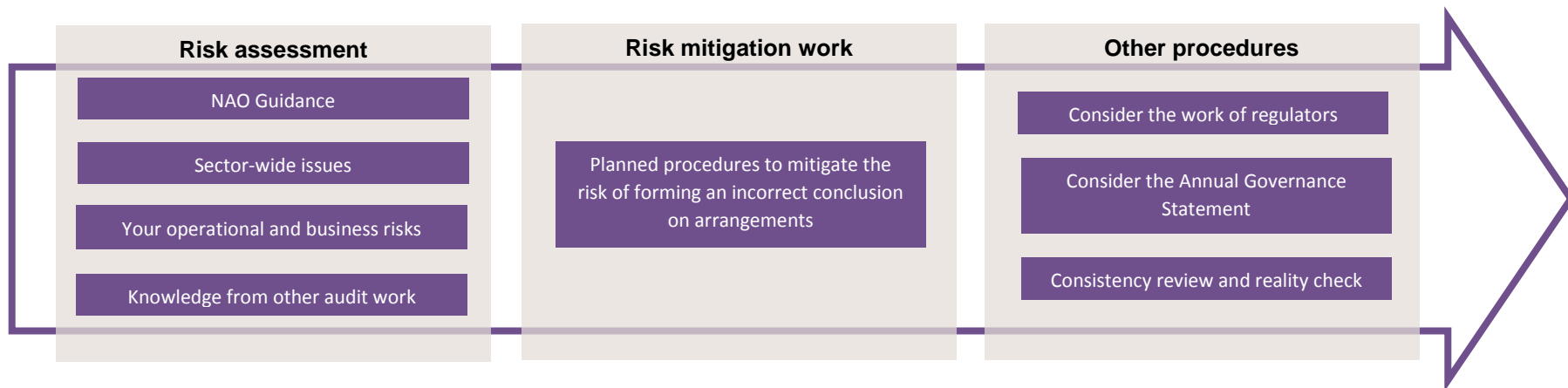
Our approach to Value for money work

We are required to form a conclusion as to whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The National Audit Office (NAO) issues guidance to auditors that underpins the work we are required to carry out in order to form our conclusion, and sets out the criterion and sub-criteria that we are required to consider.

The overall criterion is that, 'in all significant respects, the Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.' To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:

- Informed decision making;
- Sustainable resource deployment; and
- Working with partners and other third parties.

A summary of the work we undertake to reach our conclusion is provided below.



Significant Value for money risks

The NAO's guidance requires us to carry out work at the planning stage to identify whether or not a risk to the VFM conclusion exists. Risk, in the context of our VFM work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Council being inadequate. As outlined above, we draw on our deep understanding of the Council and its partners, the local and national economy and wider knowledge of the public sector.

For 2016/17, we have identified a risk for our VFM conclusion. A summary of the risk and the work we intend to undertake to ensure we reach the correct conclusion is set out in the following table.

Value for Money conclusion risk	Work we intend to carry out
<p>Level of savings required in medium term financial strategy</p> <p>The Council is facing continuing financial pressures from reduced funding, increased demand and changing responsibilities. The Council is responding to these challenges via a programme of efficiencies, service reviews and developing new ways to manage demand and deliver services, encapsulated in its 'Target Operating Model' and 'Creating a Brighter Future' programme. The level of savings the Council needs to achieve over the period of its medium-term financial strategy, on top of savings already achieved in recent years, represents a significant risk to the value for money conclusion.</p>	<p>We will carry out audit procedures reviewing the robustness of:</p> <ul style="list-style-type: none">• the medium-term financial strategy;• budget monitoring reports and other finance updates; and• a sample of the savings plans and underlying assumptions to their delivery.

Fees

Fees for work as the Council's appointed auditor

At this stage of the audit we are not planning any divergence from the scale fees set by Public Sector Audit Appointments Ltd (PSAA) as communicated to you in our fee letter of 12 April 2016.

Area of work	2016/17 proposed fee	2015/16 final fee
Code audit work	£135,765	£135,765
Housing Benefit Subsidy certification	£12,075	£16,970

Fees for non-PSAA work

In addition to the fees outlined above in relation to our appointment by PSAA, we anticipate being separately engaged by the Council to carry out additional work as outlined in the table below. Before agreeing to undertake any additional work we consider whether there are any actual, potential or perceived threats to our independence. Further information about our responsibilities in relation to independence is provided in Appendix B.

Area of work	2016/17 proposed fee	2015/16 final fee
Teachers Pensions	TBC*	£3,750
Skills Funding Agency	TBC*	£1,500
SCITT	TBC*	£2,000
Polling of housing capital receipts	TBC*	£1,800

* We have not been formally engaged by the Council yet to complete this work for 2016/17. If we are, we will report the fees in future correspondence with the Audit Committee.

Trading companies

For 2015/16, we were appointed as the external auditor of the Council's wholly-owned subsidiaries, North Tyneside Trading Company and North Tyneside Trading Company (Development) Limited, with a fee of £3,500, excluding VAT. We anticipate similar work in respect of 2016/17.

Our team



Partner – Gareth Davies

Email: gareth.davies@mazars.co.uk

Phone: 07979 164 467

Bio: Gareth has been the engagement lead for this audit since 2012.



Manager name – Diane Harold

Email: diane.harold@mazars.co.uk

Phone: 07971 513 174

Bio: Diane has been the manager for the audit of the Council since 2016. Diane will manage and coordinate the different parts of the audit. She will be the key point of contact for the finance team.



Team leader name – Elaine Hall

Email: elaine.hall@mazars.co.uk

Phone: 07881 283 350

Bio: Elaine has been the team leader for the Council's audit for a number of years. She will be a key contact for the finance team, leading the day-to-day audit, reviewing the work of more junior members of the team and performing the audit work in more specialised areas.

In accordance with our internal policies for audit quality and risk management, we consider the audit of the Council to be a 'major audit'. As a result, and in line with the requirements of International Standards on Quality Control (ISQC) 1, the firm has appointed an Engagement Quality Control Reviewer to the Council's audit who will bring an additional level of quality control to the engagement team.

Appendix A – Service organisations and experts

Service organisations

As we outline in the main body of this report, the Council makes use of service organisations. ISA 402 defines a service organisation as one that provides services to another entity that form part of that entity's information systems relevant to financial reporting. The table below sets out the service organisations that we have identified as part of our planning work together with a description of how we intend to obtain assurance over the entries in your financial statements that are derived from them.

Service organisation	Services provided	Planned audit approach
Engie	Processing of transactions and preparation of financial statements.	We have full access to the systems and staff, therefore no additional procedures required.

Experts

The Council also uses experts to provide entries in its financial statements. The table below outlines the areas of the financial statements where we expect the Council to use experts and an explanation of the approach we will take to obtaining assurance over those entries.

Financial statement area	Management's expert	Planned audit approach
Defined benefit liability and associated IAS 19 entries and disclosures.	Actuary (Aon Hewitt)	Review and consideration of work undertaken by the NAO's consulting actuary (PWC).
Property, plant and equipment valuations.	Capita	Review and consideration of the work undertaken by NAO's consulting valuer (Gerald Eve).
Financial instruments: fair value estimates.	Capita Asset Services	Consider the reasonableness of Capita's output, referring to central assurances commissioned annually by the National Audit Office.

Appendix B – Independence

We are required by the Financial Reporting Council to confirm to you at least annually in writing, that we comply with the Auditing Practices Board's Ethical Standards. In addition we communicate any matters or relationship which we believe may have a bearing on our independence or the objectivity of the audit team.

Based on the information provided by you, and our own internal procedures to safeguard our independence as auditors, we confirm that in our professional judgement, there are no relationships between us, and any of our related or subsidiary entities, and you, and your related entities, creating any unacceptable threats to our independence within the regulatory or professional requirements governing us as your auditors.

We have policies and procedures in place which are designed to ensure that we carry out our work with integrity, objectivity and independence. These policies include:

- all partners and staff are required to complete an annual independence declaration;
- all new partners and staff are required to complete an independence confirmation and also complete computer-based ethical training;
- rotation policies covering audit engagement partners and other key members of the audit team who are required to rotate off a client after a set number of years; and
- use by managers and partners of our client and engagement acceptance system which requires all non-audit services to be approved in advance by the audit engagement partner.

We wish to confirm that in our professional judgement, as at the date of this document, we are independent and comply with UK regulatory and professional requirements. However, if at any time you have concerns or questions about our integrity, objectivity or independence please discuss these with either Gareth or Diane.

Prior to the provision of any non-audit services, Gareth will undertake appropriate procedures to consider and fully assess the impact that providing the service may have on our auditor independence. No threats to our independence have been identified.

We were appointed the external auditor (for 2015/16 and anticipated similar for 2016/17 of the Council-owned subsidiaries (North Tyneside Trading Companies). There are no threats to our independence as a result of this work.

Appendix C - Materiality

Materiality is an expression of the relative significance or importance of a particular matter in the context of financial statements as a whole. Misstatements in financial statements are considered to be material if they, individually or in aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Judgements on materiality are made in light of surrounding circumstances and are affected by the size and nature of a misstatement, or a combination of both. Judgements about materiality are based on consideration of the common financial information needs of users as a group and not on specific individual users.

The assessment of what is material is a matter of professional judgement and is affected by our perception of the financial information needs of the users of the financial statements. In making our assessment we assume that users:

- have a reasonable knowledge of business, economic activities and accounts;
- have a willingness to study the information in the financial statements with reasonable diligence;
- understand that financial statements are prepared, presented and audited to levels of materiality;
- recognise the uncertainties inherent in the measurement of amounts based on the use of estimates, judgement and the consideration of future events; and
- will make reasonable economic decisions on the basis of the information in the financial statements.

We consider materiality whilst planning and performing our audit.

Whilst planning our audit, we make judgements about the size of misstatements which we consider to be material and which provides a basis for determining the nature, timing and extent of risk assessment procedures, identifying and assessing the risk of material misstatement and determining the nature, timing and extent of further audit procedures.

The materiality determined at the planning stage does not necessarily establish an amount below which uncorrected misstatements, either individually or in aggregate, will be considered as immaterial.

We revise materiality for the financial statements as our audit progresses should we become aware of information that would have caused us to determine a different amount had we been aware of that information at the planning stage.

We discuss with management any significant misstatements or anomalies that we identify during the course of the audit and we report in our Audit Completion Report all unadjusted misstatements we have identified other than those which are clearly trivial, and obtain written representation that explains why these remain unadjusted.

Appendix D - Our added value

Our primary responsibilities as the Council's external auditor are outlined in the main body of this report. As your external auditor we are ideally placed to provide added value in delivering those responsibilities and the diagram below provides a summary of how we do this.

