

# External Opinion Plan

West Midlands Fire & Rescue Authority

Audit 2008/09

**Date: June 2009**

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The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors/members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
- any third party.

# Introduction

- 1 The purpose of this plan is to provide a summary of our approach to the opinion audit at the planning stage and set out the key deadlines and milestones for 2008/09.
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## Background

- 2 As auditors in the public sector we give an independent opinion on the financial statements.
- 3 Our work must be undertaken in accordance with current legislation, ethical standards and international auditing standards applicable to the UK – the International Standards of Auditing - ISA (UK&I). The Commission, along with other UK national auditing agencies has adopted the Audit Practices Board (APB) engagement standards and quality control standards as the basis of our approach to the audit of financial statements.
- 4 In order to give an opinion on the accounts, we have to identify the material figures, ascertain what systems gave rise to them, design and undertake tests that give, as efficiently as possible, adequate assurance that the figures are not materially misstated by using either substantive testing or controls testing or a combination of the two, undertake further post statement procedures as necessary to gain sufficient assurance and give an opinion, qualified or otherwise, as is appropriate.
- 5 In order to be able to do these things we need to understand the audited body, how it works and the wider environment it operates in, as well as understanding the regulatory infrastructure that surrounds our work. We must be able to:
  - plan our audit strategy;
  - identify material amounts in the accounts and the information systems that give rise to them;
  - identify opinion audit risk at the audited body level;
  - identify opinion audit risk at the information system level;
  - develop a testing strategy to gain assurances about those risks;
  - undertake pre-statement testing;
  - undertake post-statement testing; and
  - conclude on the audit evidence and give the opinion.
- 6 We also consider the findings and conclusions of Internal Audit and work closely with Internal Audit to ensure that our audit work is focused and avoids duplication.
- 7 The concept of assurance accompanies all our opinion work. We seek reasonable assurance against the inherent risks of material misstatement in the financial statements:

- that the accounts present fairly the financial position of the West Midlands Fire & Rescue Authority;
  - that they comply with statute and other applicable guidance; and
  - that they comply with all relevant requirements for accounting presentation and disclosure.
- 8 In preparing and approving the financial statements the Treasurer is implicitly or explicitly making assertions regarding the recognition, measurement, presentation and disclosure of the various elements of financial statements and related disclosures.
- 9 ISA (UK&I) 500 sets out the assertions that the auditor should use to make an assessment of risks of material misstatement and to design and perform further audit procedures. The assertions used by the auditor fall into the following categories.

**Table 1**

<b>Assertions about classes of transactions and events for the period under audit.</b>	
Occurrence	Transactions and events that have been recorded have occurred and pertain to the entity.
Completeness	All transactions and events that should have been recorded have been recorded.
Accuracy	Amounts and other data relating to recorded transactions and events have been recorded appropriately.
Cut-off	Transactions and events have been recorded in the correct accounting period.
Classification	Transactions have been recorded in the appropriate place in the accounts
Assertions about account balances at the period end	
Completeness	All assets and liabilities that should have been recorded have been recorded
Existence	Confirmation that the asset/liability actually exists
Rights & Obligations	Confirmation that the asset/liability belongs to the Authority and that the Authority is entitled to use it
Valuation and allocation	Assets and liabilities are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.

Source: ISA (UK&I) 500.

# Audit approach

10 The main stages of our work are set out below.

## Reliance on the control environment and key financial systems

- 11 In order to comply with ISA (UK&I) 315 we demonstrate that we understand the audited body, how it works and the wider environment it operates in, as well as understanding the regulatory infrastructure that surrounds our work in order to identify opinion risk.
- 12 We also identify, evaluate and document those of the Authority's information systems that have a material impact upon its financial statements. Each year we confirm our understanding of these material systems through walkthrough tests of the key and significant controls in the system to check that the controls continue to operate as we have documented. This is an area where we cannot place reliance on the work of Internal Audit as this is not allowed by the ISA.
- 13 We then consider how to obtain assurance for the material entries in the accounts against each of the management assertions. If there are sufficient controls in place to address the assertion we elect to test compliance with key controls and if our controls testing successful then, under certain circumstances, we can place reliance on these controls for three years. However, if there are circumstances such as changes to the financial system or to key staff we have to test controls again within the three year cycle.

## Internal Audit

- 14 At least once every three years, we undertake a full review of Internal Audit's compliance with CIPFA Audit standards. This review was carried out in 2007/08 and it covered the following areas set out in the standard.
  - Scope of internal audit.
  - Independence.
  - Ethics for internal auditors.
  - Audit committees.
  - Relationships.
  - Staffing, training and continuing professional development.
  - Audit strategy and planning.
  - Undertaking audit work.
  - Due professional care.
  - Reporting.
  - Performance, quality and effectiveness.

- 15 This enables us to plan to place reliance on work carried out by internal audit. We can then review and evaluate specific areas of internal audit work and re-perform or extend some of the testing to confirm that it has been carried out satisfactorily.
- 16 We are in the process of discussions to agree a risk based programme for 2009/10 for financial systems to be undertaken by internal audit.

### Identification of the Key financial systems

- 17 Table 2 summarises our cyclical plan for controls assurance testing of the key financial systems.

**Table 2 Information Systems Cyclical Plan**

System	2007/08	2008/09	2009/10
Balance Sheet			Ongoing discussion with IA in regards to cyclical testing.
Debtors	Documented and tested in conjunction with Internal Audit.	<p>Walkthrough of system. Internal Audit has also tested system.</p> <p>Due to failures in some controls as reported by internal audit:</p> <ul style="list-style-type: none"> <li>• Debt position not being monitored appropriately.</li> <li>• Credit balances on accounts not being cleared on timely basis.</li> <li>• Access rights not being reviewed.</li> <li>• Lack of trail for invoice requests.</li> </ul> <p>We will adopt a substantive testing approach.</p>	To be confirmed (tbc)
Creditors	Documented and tested in conjunction with Internal Audit.	<p>Walkthrough of system. Internal Audit has also tested system.</p> <p>Reliance can be placed on controls in place.</p>	tbc
Pensions	Documented system and substantive testing of pensions at post statements audit.	<p>Documented and tested in conjunction with Internal Audit.</p> <p>Reliance can be placed on controls in place.</p>	tbc

## Audit approach

System	2007/08	2008/09	2009/10
Cash	Documented system. Limited controls as SMBC provide service. Substantive testing.	Walkthrough of system.  We will review year end bank reconciliations and carry out cut-off testing to confirm that all income has been posted to the correct year.	tbc
Income & Expenditure:			
Payroll	Documented and tested in conjunction with Internal Audit.  Reliance on Controls	Walkthrough of system.  Reliance on Controls	tbc
Pensions	Documented and tested. Substantive Testing undertaken.	Walkthrough of system. Tested in conjunction with Internal Audit.  Reliance on Controls	tbc
Sandwell MBC systems:			
General Ledger, cash, treasury management, VAT, valuation and some elements of debtors system.	We have written to KPMG requesting assurance over these systems.		
The Authority uses the following spreadsheet based system that are only updated at year-end.			
<ul style="list-style-type: none"> <li>• Land &amp; Buildings, Vehicles, Plant &amp; Equipment</li> <li>• Long Term Borrowing - Sandwell MBC and Dudley MBC provide annual figures for inclusion in the accounts.</li> <li>• Usable Capital Receipts</li> <li>• Earmarked Reserves</li> </ul> <p>We have therefore not reviewed the processes in place for these areas, and will substantively test them following the receipt of the authority's financial statements.</p>			

- 18 For 2008/09, we will seek a controls testing approach where this is the most efficient way of delivering our audit, again relying on internal audit work wherever possible.
- 19 As at 31 May 2009, we have updated our review of your key systems as listed at table 2. Our testing strategy at appendix 1 outlines the broad approach that we plan to take to gaining audit assurance for the financial statements audit. The strategy is based on the work undertaken in previous years and from our 2008-09 pre statement work as at 31 May 2009. The strategy will be finalised as part of our post statements planning prior to receipt of the Authority's draft accounts at the beginning of July 2009.

## Financial Statement Audit

- 20 Following receipt of the draft accounts we will complete our planning and ascertain which figures in the financial statements are generated from the financial systems. As in previous years we will plan to rely on the controls operating over the financial systems, wherever possible, and focus our testing on the year end generated balances such as accruals, provisions etc.
- 21 Our ability to undertake the audit efficiently & effectively will be determined by a number of factors, including:
- Overall control environment & the level of reliance on the key financial systems;
  - The closedown arrangements;
  - The level & quality of supporting working papers; and
  - The priority given the external audit during the main period of the audit (July & August 2009)

We will continue to work with the Authority to ensure that the accounts are submitted by the required timescales.

- 22 In preparation for the financial statements audit, the Authority should ensure that they:
- Review the ISA 260 from 2007-08 and ensure they have addressed the issues raised last year.
  - Carry out a high level review of the draft accounts and ensure that all movements in excess of £250,000 and 10% are supported by explanation and evidence. This will support the efficiency of the audit.

## Specific Financial Statements Issues

We have identified the following matters which we will address during the opinion audit:

Issue	Proposed Action
<b>Generic Issues</b>	
Circular 1/2008 advises Fire & Rescue Authority's on the pension increase order 2008 and the possible overpayments paid to PFS pensioners who have reached state pension age as a result of late or non notification of Guaranteed Minimum Pensions.	The Authority should ensure that they have complied with the requirements of Circular 1/2008.  We will sample test transactions to confirm compliance with Circular 1/2008 requirements as part of the Financial Statements pensions' audit.
Fixed Asset Valuations - there have been significant reductions in land & building valuations during 2008-09 and the	The Authority should review all land and building values and ensure these are reasonable in light on current market

## Audit approach

<p>Authority need to have considered this as part of the production of the accounts on an asset by asset basis.</p>	<p>conditions. We will consider the reasonableness of valuations held in the Authority's balance sheet.</p>
<p><b>WMF&amp;RA Specific Issues</b></p> <p>WMF&amp;RA rely on the Sandwell MBC systems (General Ledger, cash, treasury management, VAT, valuation and some elements of debtors system) to produce their accounts.</p> <p>This is part of the services purchased by WMF&amp;RA under SLA.</p>	<p>We have written to KPMG as external auditors to Sandwell MBC requesting confirmation that we can rely on their work and the systems in place at Sandwell MBC used to generate the figures for the WMF&amp;RA financial statements.</p>
<p>At systems testing we were unable to confirm if there were controls in place to check the accuracy of the brought forward balances.</p> <p>The Authority place reliance on the Sandwell MBC ledger to accurately carry forward balances.</p>	<p>We will carry out testing to ensure that balances brought forward are correctly.</p>
<p>We identified approvals of creditor payments in excess of delegated limits of £50k taking place. This situation occurred when a senior officer was not available to authorise a payment due to leave or other off-site commitments. Retrospective approval of these payments was made however this represents a significant fraud risk.</p>	<p>The Authority need to ensure cover arrangements are in place for authorisation of payments over delegated limits at all times.</p>
<p>Our testing last year identified significant weaknesses in controls over journals. Internal Audit have reviewed controls put in place this year and have identified the following weaknesses:</p> <ul style="list-style-type: none"> <li>• Journals are not (sequentially) numbered.</li> </ul> <p>In addition, our work identified:</p> <ul style="list-style-type: none"> <li>• Journals below £10k are not checked by a senior office prior to processing.</li> <li>• Any financial management staff can</li> </ul>	<p>The Authority need to review controls in place over journals and ensure weaknesses are urgently addressed.</p> <p>We will carry out an increased sample of testing in order to reduce the level of risk from potential fraudulent reporting.</p>

input a journal, with no system restrictions on access or value of journal.	
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## IFRS

- 23 Over the next few years, local authorities will face a range of challenges to their accounts production processes. The 2008 SORP introduces some minor amendments to local authority accounting for 2008/09 which will require implementation and International Financial Reporting Standards (IFRS) will also be relevant. All local authorities are required to produce IFRS-compliant accounts from 2010/11, so 1 April 2009 is the date of transition to IFRS in local government in order to prepare comparative information.
- 24 Based on our experience of auditing and working alongside the NHS with their IFRS conversion, successful organisations have by the date of transition:
- established a project team – this should include wider representation than finance e.g. estates;
  - developed a project plan which has been taken to Audit Committee;
  - reviewed which standards will have the biggest impact and which will be the most complex;
  - completed the information-gathering stage - for example, gathering the information on all leased assets in order to review whether they are finance or operating leases under IFRS; and
  - engaged the audit team with the process.
- 25 Based on our experience of working with other AIBs a potentially time consuming exercise is reviewing all current leases to determine the appropriate accounting treatment under the new requirements. Depending on the Authority's circumstances, other standards may also require a similar exercise to be undertaken. The Authority should continue to ensure that sufficient capacity is available to manage the process and regularly appraise the Audit Committee of progress.

# Timetable

**26** Set out below are the timescales involved in the work set out previously.

**Table 3 Timescales for the 2008/09**

Timescale/Date	Description
March 2009	Update of the continuous planning including the overall control environment, and review of Internal Audit.
April 2009	Walkthrough of the key financial systems.
March/April 2009	Review of Internal Audits work on the key financial systems.
May/June 2009	Final planning of the financial statements audit, updating for any emerging issues.
01 July 2009	Draft 2008/09 financial statements submitted for audit
July/August 2009	Audit of the draft financial statements
September 2009	Annual governance report & audit opinions
November 2009	Annual letter issued

# Appendix 1 – Testing Strategy

**Table 4      Summary of Opinion Testing Strategy**

Item	Pre-statements	Post-statements
<b>Balance Sheet</b>		
Fixed Assets - land & buildings and vehicle, plant & equipment	<p>Initial review of systems documentation and walkthrough completed.</p> <p>NB: the system is a spreadsheet based system updated post-year end and therefore substantive testing approach more efficient.</p>	<p>Substantive approach to gaining assurance over completeness, existence, rights &amp; obligations and valuation.</p> <p>Reliance on external valuers for fixed asset valuation.</p>
Fixed Assets - assets under construction and investment properties	None.	Substantive approach to gaining assurance over completeness, existence, rights & obligations and valuation.
Debtors	Updated system documentation. Walkthrough testing completed. Review of internal audit work.	Substantive approach.
Cash	Updated system documentation. Walkthrough testing completed.	Substantive approach.
Creditors	Updated system documentation. Walkthrough testing of payments completed.	Controls approach plus year end feeder system reconciliation (cut-off)
Pensions	Updated system documentation. Walkthrough testing completed.	<p>Controls approach.</p> <p>However, we will review statements to ensure compiled in accordance with appropriate regulations.</p>

Item	Pre-statements work completed	Post-statements planned approach
Payroll	Updated system documentation. Walkthrough and controls testing completed.	<p>Reliance on key controls tested with remaining assurance to be gained from specific tests:</p> <p>Cut-off Testing posting of expenditure to correct year.</p>

## Appendix 2 – Action Plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
	<Recommendation Title>					
8	<p>In preparation for the financial statements audit, the Authority should ensure that they:</p> <ul style="list-style-type: none"> <li>Review the ISA 260 from 2007-08 and ensure they have addressed the issues raised last year.</li> <li>Carry out a high level review of the draft accounts and ensure that all movements in excess of £250,000 and 10% are supported by explanation and evidence. This will support the efficiency of the audit.</li> </ul>	3	Finance Manager	Yes	Working papers supporting the statement of accounts will be provided to the Audit Commission.	July 2009
8	The Authority should ensure that they have complied with the requirements of Circular 1/2008.	2	Finance Manager	Yes	Working papers supporting the statement of accounts will be provided to the Audit Commission.	July 2009

<b>Page no.</b>	<b>Recommendation</b>	<b>Priority 1 = Low 2 = Med 3 = High</b>	<b>Responsibility</b>	<b>Agreed</b>	<b>Comments</b>	<b>Date</b>
9	The Authority should review all land and building values and ensure these are reasonable in light on current market conditions.	3	Finance Manager	Yes	The Valuer at Sandwell MBC instructed Wilks Head and Eve to carry out an impairment review and valuation of the new Headquarters	
9	The Authority need to ensure cover arrangements are in place for authorisation of payments over delegated limits at all times.	3	Finance Manager	Yes	A review of Officers able to authorise has taken place to ensure there is sufficient cover	
9	The Authority need to review controls in place over journals and ensure weaknesses are urgently addressed.	3	Finance Manager	Yes	Numbering of journals is in place, issues raised regarding controls over journals will be referred to the SBS Control Team at Sandwell MBC	July 2009
10	The Authority should ensure that sufficient capacity is available to manage the move to IFRS and regularly appraise the Audit Committee of progress.	2	Finance Manager	Yes	A report to the October Audit Committee will update Members on the progress towards IFRS and seek views on further report requirements.	Oct 2009