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WALES AUDIT OFFICE

Final Audit Findings Report

Year ended 31 March 2017

Presented to the Directors
By RSM UK Audit LLP

on 6 June 2017

RSM

CONTENTS

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 2017.

The scope of our work has already been communicated to you via our Audit Plan document dated 22 February 2017.

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 Directors 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.

2 AUDIT AND ACCOUNTING ISSUES IDENTIFIED AT PLANNING STAGE

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 and any provisions required.
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. We will review correspondence with audit managers to establish the estimated costs to complete and any required provisions at the year end, considering the impact of any time spent after the year end on these estimations. We will also review time postings after the year end for any time posted by employees relating to work done before the year end that may not have been factored into the above calculations.
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. This has been done by way of a cost to complete exercise involving the Resource Managers for the 2016-17 year end. This has resulted in management reducing revenue recognised for projects where costs are expected to exceed the quoted fees. An adjustment has been calculated by management of £64k to decrease the work in progress provision on open jobs at year end in line with a cost to complete exercise that has been undertaken on a project basis. We have reviewed costs on a sample of closed projects in the year and on average costs exceed the budgeted fees by approximately 3%. If this was applied to the remaining open projects at year end, work in progress would be reduced by a further £141k. 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 on open projects which are currently in a deferred income position. A potential reclassification has been included in section 5 below.

Management override 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	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. We will review significant accounting estimates and policies which could involve bias resulting in a material misstatement. 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.
Response	The testing was completed as planned with no significant issues identified to report to management. We have tested the journal entries made as part of the preparation of the financial statements, with no significant issues to note. We have reviewed estimates in operation within the WAO and we have not identified any areas whereby there are any indicators of bias.

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	During the course of the audit, we have not identified any areas from the Office's operations that suggests as though there are any areas whereby the reputation could appear to be damaged. We have reviewed judgemental areas, aside of the WIP provisioning, and not noted any areas of subjectivity; including provisions, recoverability of debtors as well as disclosure of remuneration.

3 AUDIT AND ACCOUNTING ISSUES IDENTIFIED DURING THE AUDIT

HMRC death in service provision

Issue	It was noted during the fieldwork that correspondence was received from HMRC confirming that the Death in Service costs are not taxable. We have reviewed available documentation that confirms there are no further amounts required to be paid by the Office. As a result, the death in service provision has subsequently been released. There is the potential that some amounts may be recoverable, however, as a result of the uncertainty of these amounts and timing, these cannot be recognised as a contingent asset.
Resolution	An adjusted journal has been agreed and raised within Section 5 below.

Firms income and costs matching

Issue	It was identified that there was one Firm's project that was still subject to the old billing methodology whereby only the contribution should be recognised and thus the income and costs should be offset against each other. A balance sheet reclassifying journal was raised to remove £134k between WIP and Accruals relating to this project.
Resolution	An adjusted journal has been agreed and raised within Section 5 below.

WIP recoverability

Issue	As part of our testing over the work in progress balance, we identified one small project whereby amounts owed from the Government of Anguilla had not been billed. The project had been started back in 2014. Although trivial, we had recommended that action be taken to raise the invoice and chase the amounts owing. The value of this project was £5k.
Resolution	It was resolved that the finance team would chase these amounts and to ensure that the regular process is adhered to for chasing projects not invoiced. This would safeguard against any smaller amounts not being recovered. Management agreed that there was no reason to believe that these amounts would not be paid and that there was no need for a provision to be made against these amounts.

4 REGULARITY ISSUES IDENTIFIED DURING THE AUDIT

Procurement

Issue	Three issues were identified during the testing of the procurement policy on a sample basis. Firstly, it was noted that one contract was renewed by way of the renewal date passing, rather than the purchase being made in line with normal tendering process. For the level of purchase, two written quotations were required. The value of the contract renewed was £7k. Whilst two quotes were obtained, the renewal date notice period had passed before notice was served. Secondly, it was noted that for one purchase made the expected supporting documentation as required per the procurement policy was incomplete. For the size of purchase, two written quotations were required. One written quotation was obtained and evidenced, however from discussions it was confirmed that the other quotation was a verbal quote but this was not documented. As such, we could not gain evidence that the policy was being followed on this particular item. The value of this particular item was less than £1k. Thirdly, we noted for one purchase that three quotations were required to be obtained. The Wales Audit Office had used the "Sell-2-Wales" portal to obtain quotations however only two responses were received. Currently, the financial management handbook does not reference the Sell-2-Wales portal as a means for obtaining quotations, however we are aware that the portal does advertise the tender as widely as possible to all approved suppliers.
Resolution	Whilst the above are not material in terms of regularity, A process should be put in place to ensure renewals are examined on a timely basis as there is a risk that contracts could be renewed when they may no longer represent value for money and the best possible value. We are aware that for the above specific item, there has been a diarised review stage to prepare for the upcoming renewal date. We are aware that a process is currently in place where renewals are reviewed monthly and quotes are requested and obtained, however we understand that the review and reminders for February was undertaken in March due to staff absence. For verbal quotations received, there should be a follow up communication made to confirm that the amounts quoted are confirmed. These should be documented alongside any normal quotations received. We recommend that the financial management handbook is updated to reflect the Sell-2-Wales portal as an approved method of obtaining quotations.

Contractors

Issue	The Office has taken the view to place all contractors on the payroll to mitigate any employment status questions. The Office believes that the majority of these workers would be deemed to be employees however there may be some that could be considered contractors. As a result the Office pays employers national insurance at 13.8% over and above the contractor standard rates. These additional costs are not material to our regularity opinion. The Office has applied this methodology to ensure that they remain compliant with the relevant tax legislation should any questions arise regarding the status of these individuals as contractors, of which had previously been experienced. This is seen by the Office as an appropriate treatment .
Resolution	Whilst the above is not material, The Office should continuously review contractors to ensure that they continue to comply with legislation.

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 £5,000 individually and £10,000 in aggregate.

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

	Profit (£’000)	Net assets (£’000)	
Adjusted misstatements	**Dr/(Cr)**	**Dr/(Cr)**	
HMRC DIS provision Expenditure release – I&E	 (79)	79	To derecognise the HMRC provision no longer required.
Work in progress provision Audit Income	 (64)	64	Being management's adjustment of the WIP provision based on the cost to complete exercise.
Accruals Trade payables		286 (286)	To reclassify pre year end invoices included as accruals at the year end.
Trade payables Prepayments		(130) 130	To recognise a rates invoice which was received pre year end.
Other accruals Work in progress		134 (134)	Being the reclassification of ongoing firms work on old billing method.
Total	**(143)**	**143**	
Unadjusted misstatements Judgemental	**Dr/(Cr)**	**Dr/(Cr)**	
Work in progress provision Audit Income	 140	(140)	Being the judgemental assessment of projects open at year end expected to exceed budget.
Deferred income Other payables		132 (132)	Being the judgemental reclassification of refunds payable based on open projects at and historic refund rate.
Underlying total	**140**	**(140)**	

6 SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL

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

Refunds – de Minimis level	
Fact and potential consequence	It was noted during our audit, that the decision to either pay or not pay a refund was being assessed taking account of a de Minimis level of £200, but that this had not been agreed with the board.
Possible action	A de Minimis level should be agreed with the Board and then the financial handbook updated to reflect this.
Management response	Agreed – the Financial Management Handbook has been updated to include the process for fee setting and the proposed de-minimis level of £200 for making refunds. This will be considered by ARAC in June 2017.
Timing of implementation and responsibility	June 2017. Nicola Evans

WIP cost to complete exercise	
Fact and potential consequence	It was noted during our review of the costs to complete exercise that the assumptions made in the Resource Managers assessment of open projects at year end appeared to be under resourced in some instances. Consideration for average historical performance as well as the probability of realistic small overspends of general audit practice could have been built in to the cost to complete exercise with more detail. It was noted that an adjustment for these elements was later made by the finance team.
Possible action	The cost to complete exercise completed by the Resources Managers should factor in acknowledgement to the appropriateness of historical actual performance. We appreciate that there are few periods for comparison, being a new process, though these should remain under review.
Management response	Agreed. The cost to complete of open projects will be reviewed at least quarterly by Resource Managers in the first instance with oversight by the finance team. There has been a notable improvement in project management within budget in the last year and this is reflected in the year end cost to complete assessments.

WIP cost to complete exercise

Timing of implementation and responsibility	Immediate. Resource Managers and Finance Team.

Firms actual outturn positions

Fact and potential consequence	The costing structure, of direct plus overhead costs, is used in setting the fee rates and fee scales that are approved by the National Assembly as part of the WAO Fee Scheme, which are laid annually. The Fee Scheme is directly linked to annual Estimate which the Assembly also approves. Legislation states that The WAO charge must be in accordance with the approved Fee Scheme, but it does not require any retrospective review of it. It was noted that, for audits undertaken by Firms, the WAO allocate overhead costs in a manner consistent with its costing model, however excluding functions that are not applicable to the Firms
Possible action	We acknowledge that the current fee regime as set out in legislation causes additional complexity in relation to “the full cost of audit” for audits contracted out to the firms. We recommend that this be further considered as part of ongoing discussions about reviewing the fee regime.
Management response	The contribution towards overheads received under Firms contracts is allocated across our overhead base to reflect the services available to them. A retrospective review of this allocation would be administratively complex – requiring significant input from internal support services and placing additional reporting requirements on the Firms. There would be a significant additional cost associated with this exercise. A consultation on proposals to simplify our fee regime is due to be issued in June 2017. We will reconsider the overall costing model should changes to the fee regime be progressed thereafter.
Timing of implementation and responsibility	Post-consultation. Steve O’Donoghue.

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:

-It was noted that in the first draft of accounts, timings associated with the release of dilapidations provisions were allocated incorrectly.

-Within the Remuneration Report, the exit payment associated with a member of the Senior Leadership team had not been disclosed. This has now been reflected within the final accounts

-The disclosure of non-audit services provided by the external auditor had not been disclosed in the first draft of accounts. This has now been included as nil.

-Upon review of the FReM checklist it was noted that the first draft of the financial statements could have included more disclosure with regards to which sections of the Accountability Report are subject to opinion.

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 22 February 2017.

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, Jonathan Da Costa and the audit staff and the related safeguards from those disclosed in the Audit Plan dated 22 February 2017.

APPENDIX A - DRAFT LETTER OF REPRESENTATION

RSM UK Audit LLP
Davidson House
Forbury square
Reading
RG1 3EU

Dear Sirs

Audit of Financial Statements– Year ended 31 March 2017

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 2017.

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 2017 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 2017 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 2017.

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 2017 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

APPENDIX B - UPDATED FINANCIAL REPORTING DEVELOPMENTS

Off-payroll engagements update

HMRC has recently published draft legislation following the 2016 Autumn Statement, which provides clarification on a number of areas.

The new rules relating to off-payroll engagements of workers supplied via an intermediary are still on-track for implementation in April 2017. For the purposes of these rules, the intermediary can be a limited company (personal service company), but can also be a partnership (where the worker has at least a 60 per cent share) or even another individual. All public sector bodies that engage workers supplied through an intermediary will need to consider all necessary employment status factors (control, substitution, mutuality, etc) in order to determine whether a ‘deemed employment’ exists.

Where the new rules apply, the engager must operate PAYE to pay over to HMRC the income tax national insurance contributions (NICs) (and apprenticeship levy) on the payments made, as the fee paid to the intermediary is treated as a payment of the worker’s employment income. It is important to note that other employment rights will not apply, such as stakeholder pensions, statutory payments, etc.

Where a public authority engages a worker, who provides his personal services via an intermediary, the authority must inform the worker of the decision as to whether PAYE deductions will be made or not. It is therefore vital that thorough procedures are introduced to identify all such workers who may be caught by these new rules. We are currently working with a number of clients specifically in these areas. It is important to remember that failure to correctly analyse and process such payments from April 2017 may give rise to penalties based on the deductions that should have been made.

The online HMRC digital tool for public sector organisations to use should be available ahead of 6 April 2017. HMRC is currently in private testing with invited stakeholders and anticipates public testing will start in February.

Apprenticeship levy

HMRC has published draft legislation for the apprenticeship levy. Further guidance on certain aspects of the levy has also been published.

As an employer, you’ll have to pay the apprenticeship levy each month from 6 April 2017 if you:

have an annual pay bill of more than £3m (based on pay subject to NICs); or

are connected to other employers (companies or charities) for employment allowance purposes, where the total annual pay bill of the connected employers is more than £3m.

Employers that are not connected to other employers will have an apprenticeship levy allowance of £15,000 each year. Employers that are connected to other employers can decide how to split the allowance between the connected organisations, but this allocation must be applied the first time that the levy is paid in a tax year and cannot then be changed during the year.

You’ll still need to pay apprenticeship levy even if you already contribute to an industry-wide training levy arrangement, for example the Construction Industry Training Board (CITB) levy.

The technical consultation on the draft apprenticeship levy regulations continues and anyone wishing to respond to HMRC must do so by 3 February.

The Department of Education has produced guidance on how employers in England can access the funds in their digital accounts and the Scottish Government has also published a report setting out how it intends to use the funds generated for it by the UK-wide levy.

Salary sacrifice arrangements from April 2017

The Government will legislate in Finance Bill 2017 to remove the income tax and NICs advantages of benefits provided through salary sacrifice arrangements. The legislation will apply from 6 April 2017. The draft legislation is now in a period of consultation, which runs until 1 February 2017 and the final details will be confirmed in the Spring Budget 2017.

Therefore, with effect from April 2017, certain benefits provided through salary sacrifice will be chargeable to income tax and class 1A employer NICs on the higher of the value of the benefit provided or the amount of salary foregone. The benefits that will not be affected by the changes are pensions, cycle to work, ultra-low emission (ULEVs) cars, employer-supported childcare (childcare vouchers, directly-contracted childcare and workplace nurseries) and intangible benefits such as annual leave purchase.

Salary sacrifice arrangements in existence before April 2017 that remain in place and are not ‘renewed’ will be protected until April 2018, with an extended protection period until April 2021 for cars, accommodation and school fees. However, the protections are subject to certain conditions.

It is therefore essential that employers consider the implications and plan accordingly for the changes to ensure existing and new benefits provided through salary sacrifice arrangements are dealt with correctly.