Audit Strategy Memorandum

City of Bradford Metropolitan District Council

March 2016

Mazars LLP
Mazars House
Gelderd Road
Leeds
LS27 7JN

Governance and Audit Committee
City of Bradford Metropolitan District Council
City Hall
Centenary Square
Bradford
BD1 1HY

March 2016

Dear Members

Audit Strategy Memorandum for the year ending 31 March 2016

We are delighted to present our Audit Strategy Memorandum for City of Bradford Metropolitan District Council for the year ending 31 March 2016.

The purpose of this document is to summarise our audit approach, highlight significant audit risks and areas of key judgements and provide you with the details of our audit team. It is a fundamental requirement that an auditor is, and is seen to be, independent of its clients, and Appendix A summarises our considerations and conclusions on our independence as auditors.

We value two-way communication with yourselves and we see this document, which has been prepared following our initial planning discussions with management, as being the basis for a discussion through which we can also understand your expectations.

This document will be presented at the Governance and Audit Committee meeting on 15 April 2016. If you would like to discuss any matters in more detail please do not hesitate to contact me on 0113 387 8850Yours faithfully

Mark Kirkham
Partner, for and on behalf of Mazars LLP

Contents

Our reports are prepared in the context of the 'Statement of responsibilities of auditors and audited bodies' and 'Terms of Appointment' issued by Public Sector Appointments Limited. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the Council and we take no responsibility to any member or officer in their individual capacity or to any third party.

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01 Purpose and Background

Purpose of this document

This document sets out our audit plan in respect of the audit of the financial statements of City of Bradford Metropolitan District Council for the year ending 31 March 2016, and forms the basis for discussion at the Governance and Audit Committee meeting on 15 April 2016.

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 to oversee the strategic direction of the entity and obligations related to the accountability of the entity, including overseeing the financial reporting process.

We see a clear and open communication between ourselves and you as important in:

- reaching a mutual understanding of the scope of the audit and the responsibilities of each of us;
- sharing information to assist each of us to fulfil our respective responsibilities;
- providing you with constructive observations arising from the audit process; and
- ensuring as part of the two-way communication process that we, as external auditors, gain an understanding of your attitude and views in respect of the internal and external operational, financial, compliance and other risks you face, which might affect the audit, including the likelihood of those risks materialising and how they are monitored and managed.

Appendix C outlines the form, timing and content of our communication with you during the course of the audit. Appendix D sets out forthcoming accounting and other issues that will be of interest.

Scope of engagement

We are appointed to perform the external audit of your accounts for the year to 31 March 2016. The scope of our engagement is laid out in the National Audit Office's Code of Audit Practice.

Responsibilities

- **Audit opinion and value for money conclusion**

  We are responsible for forming and expressing an opinion on the financial statements. Our audit does not relieve management or the Governance and Audit Committee, as those charged with governance, of their responsibilities. We are also required to reach a conclusion on the arrangements that the Council has put in place to secure economy, efficiency and effectiveness in its use of resources (our Value for Money conclusion).

- **Whole of Government Accounts**

  We report to the National Audit Office in respect of the consistency of the Council's Whole of Government Accounts submission with the financial statements.

- **Fraud**

  The responsibility for safeguarding assets and for the prevention and detection of fraud, error and non-compliance with law or regulations rests with both those charged with governance and management. In accordance with International Standards on Auditing (UK and Ireland), we plan and perform our audit so as to obtain reasonable assurance that the financial statements taken as whole are free from material misstatement, whether caused by fraud or error. Our audit, however, should not be relied upon to identify all such misstatements.

We are required to enquire of those charged with governance as to their knowledge of instances of fraud, the risk of fraud and their views on management controls that mitigate the fraud risks.

Significant matters considered

As part of our risk based approach to planning we consider a number of key performance and control environment features together with external developments. The following paragraphs set out some of the key aspects for 2015/16. We take into account the impact of the Council's financial performance and control environment, together with external factors in sections 2 and 3 of this document. Our current view is that this information does not give rise to any additional significant risks for our audit.

Key performance and control environment features

We use the Council's latest financial monitoring reports and medium term financial plan to consider the current financial position. The following table summarises in year activity to date.

Area	Budget	Forecast as at 31/12/2015	Projected year end outturn
Net revenue expenditure	£400.8m	£400.1m	£0.7m surplus
Capital expenditure	£102.8m	£81.4m re-profiled due to scheme deferrals	£21.4m net planned change in year

Ongoing pressure on the public finances presents significant challenges for the Council and the need to plan for further reductions in spending power, coupled with increased demand for services.

The Council approved planned savings of £37.7m for 2015/16 and further savings of nearly £89m will be needed to achieve a balanced position by the end of 2017/18. This is against a backdrop of having already delivered savings of £135m in the period 2011/12 to 2014/15.

The latest financial position statement, as at 31 December 2015, forecasts that 86% of planned total savings of £37.7m for 2015/16 will be achieved. Compensating measures have been identified that aim to ensure the shortfall in planned savings has no adverse impact on the Council's overall financial position.

Unallocated corporate reserves are forecast to total £19.6m at 31 March 2016 after the transfer of the forecast £0.7m surplus for 2015/16. The reserves will be utilised to support the budgets for 2016/17 (£6.1m) leaving a forecast balance of £13.5m at 31 March 2017.

The budget for 2016/17, approved in February 2015, shows a balanced position although projections for 2017/18 show a budget shortfall of £7.6m and a significantly greater shortfall of £28m in 2018/19. Further deep reductions in the net cost of Council services will be required to bridge the projected shortfall in future years.

02 Audit scope, approach and timeline

Audit scope

Our audit approach is designed to provide you with an audit that complies with all professional requirements.

Our audit of the financial statements will be conducted in accordance with International Standards of Auditing (UK and Ireland) and in accordance with the National Audit Office's Code of Audit Practice. Our work is focused on those aspects of your business which we consider to have a higher risk of material misstatement such as those impacted by management judgement and estimation, application of new accounting standards, changes of accounting policy, changes to operations or areas which have been found to contain material errors in the past.

Audit approach

We apply a risk-based audit approach primarily driven by the matters we consider to result in a higher risk of material misstatement of the financial statements. Once we have completed our risk assessment we develop our audit strategy and design audit procedures in response to this assessment. The work undertaken could include a combination of the following as appropriate:

- testing of internal controls;
- substantive analytical procedures; and
- detailed substantive testing.

If we conclude that appropriately designed controls are in place then we may plan to test and rely upon these controls. If we decide controls are not appropriately designed, or we decide it would be more efficient to do so, we may take a wholly substantive approach to our audit testing.

Our audit will be planned and performed so as to provide reasonable assurance that the financial statements are free of material misstatement and give a true and fair view. Materiality and misstatements are explained in more detail in Appendix B.

The diagram overleaf outlines the procedures we perform at the different stages of the audit.

Planning

- Planning visit
- Risk assessment
- Identifying material financial systems
- Considering proposed accounting treatments and accounting policies
- Developing audit strategy
- Agreeing timetable and deadlines
- Preliminary analytical review

Interim work and final fieldwork

- **Interim work**
- Document systems and controls
- Perform walkthroughs
- Interim controls testing
- **Final fieldwork**
- Receiving and reviewing draft financial statements
- Reassessment of audit plan and revision if necessary
- Executing the strategy starting with significant risks and high risk areas
- Communicating progress and issues
- Clearance meeting

Completion

- Final review and disclosure checklist of financial statements
- Final Engagement Lead review
- Agreeing content of letter of representation
- Reporting to the Governance and Audit Committee
- Reviewing post balance sheet events
- Signing the auditor's report

Reliance on Internal Audit

Where possible we will seek to utilise the work performed by internal audit to modify the nature, extent and timing of our audit procedures. We will meet with internal audit to discuss the progress and findings of their work prior to the commencement of our controls evaluation procedures.

We intend to rely internal audit's work for council tax and business rates income. We will evaluate the work they performed and carry out our own audit procedures to determine its adequacy for our audit. We also indirectly use the work of internal audit in assessing the control environment, which informs our review of the Annual Governance Statement and the sample sizes for our substantive testing.

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. The table below outlines our approach to understanding the services the Council receives from each organisation and the effectiveness of controls in place to reduce the risk of material misstatement in the financial statements.

Nature of services provided and items of account	Name of service organisation	Audit approach to be adopted
Payroll service for schools that use an external provider to pay employees rather than the Council's payroll service.	The two material providers are Data-plan and Working for Schools.	Sufficient appropriate audit evidence is held at schools for us to substantively test schools' external payroll without contacting the service organisations.

The work of experts

We plan to rely on the work of the following experts:

Item(s) of account	Management's expert	Our expert
Defined benefit liability and associated IAS 19 entries and disclosures	Actuary (Aon Hewitt)	National Audit Office's consulting actuary (PWC)
Property, plant and equipment valuations	In house valuer (Estates and Property)	National Audit Office's consulting valuer (Gerald Eve)
Financial instruments: fair value estimates	Capita	Central assurance provided by the National Audit Office

Timeline

The diagram below sets out the timing of the key phases of our audit work. We will communicate with management throughout the audit process and will ensure significant issues identified are communicated to those charged with governance on a timely basis.

February to March 2016

- Planning meeting
- Issue Audit Strategy Memorandum

February to April 2016

- Interim work (walk through tests, control testing, IT risk assessment)
- Report interim findings and update Audit Strategy Memorandum if required

July to Sept 2016

- Start fieldwork on 1 July 2016
- Issue Audit Completion Report September 2016
- Clearance meeting September 2016

By 30 Sept 2016

- Issue representation letter
- Finalise financial statements review and issue auditor's report

03 Significant risks and key judgement areas

We have performed our planning procedures, including our risk assessment, as detailed in section 2. In addition, we met with management as part of the audit planning process to discuss the risks that, in management's opinion, the Council faces and we have considered the impact on our audit risk. The risks that we identify as significant for the purpose of our audit are the risks of material misstatement that in our judgement require special audit consideration.

We set out below the significant audit risks identified as a result of these meetings and planning procedures which we will pay particular attention to during our audit in order to reduce the risk of material misstatement in the financial statements.

Significant audit risks

Management override of controls

Description of the risk

International Standards on Auditing (ISA) 240 – *The auditor's responsibility to consider fraud in an audit of financial statements* requires us to consider the potential for management override because controls that may be sufficient to detect error may not be effective in detecting fraud.

In all entities, management at various levels is in a unique position to perpetrate fraud because of the 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 override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.

How we will address this risk

We will address this risk by:

- evaluating and testing the basis for material accounting estimates included in the financial statements;
- reviewing unusual or significant transactions outside the normal course of business; and
- testing a sample of journals recorded in the general ledger and other adjustments made in preparation of the financial statements.

Revenue recognition

Description of the risk

In accordance with ISA 240 we presume there is a risk of fraud in respect of the recognition of revenue because of the potential for inappropriate recording of transactions in the wrong period. ISA 240 allows the presumption to be rebutted but, given the Council's range of revenue sources we have concluded that there are insufficient grounds for rebuttal. This does not imply that we suspect actual or intended manipulation but that we continue to deliver our audit work with appropriate professional scepticism.

How we will address this risk

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:

- testing receipts in the pre and post year end period to ensure they have been recognised in the right year;
- testing a sample of adjustment journals; and
- obtaining direct confirmation of principal year-end bank balances and testing the reconciliations to the ledger.

Pension Estimates (IAS 19)

Description of the risk

The financial statements contain material pension entries in respect of the 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.

How we will address this risk

We will discuss with key contacts any significant changes to the pension estimates prior to the preparation of the financial statements. In addition to our standard programme of work in this area, we will:

- evaluate the management controls you have in place to assess the reasonableness of the figures provided by the Actuary; and
- consider the reasonableness of the Actuary's output, referring to an expert's report on all actuaries nationally which is commissioned annually by the National Audit Office.

Key management judgements

We recognise that within your financial statements there are specific accounting transactions and disclosures where management has exercised judgement. We consider that these areas require specific audit focus. We highlight below what we consider to be the key areas of management judgement and our planned audit approach.

Valuation of land and buildings

Description of the area of judgement

Land and buildings are the Council's highest value assets. Management use in house valuation services, as an expert, to determine the value of property to be included in the financial statements.

In addition a new financial reporting standard (IFRS13 fair value measurement) applies to the valuation of surplus property for 2015/16 and judgements may be required about 'highest and best' use values.

Our planned audit approach

We are liaising with management to update our understanding on the approach taken by the Council to the valuation of land and buildings including the requirements of IFRS13.

We will review:

- the scope and terms of the engagement with the valuer; and
- how management use the valuer’s report to value land and buildings in the financial statements.

We will write to the valuer to obtain information on the methodology and their procedures to ensure objectivity and quality.

We will also consider evidence of regional valuation trends.

04 Value for Money Conclusion

Scope of work

For 2015/16, we are required to satisfy ourselves the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We perform our work in this area in accordance with guidance set out by the NAO in Auditor Guidance Note 3. This requires us to consider one overall criterion which is made up of three sub-criteria.

Overall criterion: *in all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.*

Sub-criteria	Guidance
Informed decision-making	• Acting in the public interest, through demonstrating and applying the principles and values of sound governance. • Understanding and using appropriate and reliable financial and performance information (including, where relevant, information from regulatory/monitoring bodies) to support informed decision making and performance management. • Reliable and timely financial reporting that supports the delivery of strategic priorities. • Managing risks effectively and maintaining a sound system of internal control.
Sustainable resource deployment	• Planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions. • Managing and utilising assets effectively to support the delivery of strategic priorities. • Planning, organising and developing the workforce effectively to deliver strategic priorities.
Working with partners and other third parties	• Working with third parties effectively to deliver strategic priorities. • Commissioning services effectively to support the delivery of strategic priorities. • Procuring supplies and services effectively to support the delivery of strategic priorities.

As part of our work, we will also:

- review your annual governance statement;
- consider the work of other relevant regulatory bodies or inspectorates, such as Ofsted and the Care Quality Commission, to the extent the results of the work have an impact on our responsibilities; and
- carry out any risk-based work we determine appropriate.

We have considered the risks that are relevant to our value for money conclusion and have identified the following significant risk that we will address through our work.

VFM risk – sustainable resource deployment
Description of the risk The Council faces significant financial pressure from reduced funding and increasing demand for some services. The challenge to identify and implement savings is increasingly difficult as by the year end the Council will have reduced spending by £172.6m over the past 5 years. The VFM risk is that we will not be able to reach a safe conclusion without undertaking further work to assess the Council's arrangements to achieve the planned balanced position in 2016/17 and to identify further plans to bridge the funding gaps for 2017/18 (£7.6m) and 2018/19 (£28m).
How we will address this risk We will review the Council's arrangements for: • monitoring budgets and ensuring that identified savings are being achieved; • revising the medium term financial plan; and • developing plans to bridge the funding gap for future years through the New Deal process. We will also review a sample of project plans for saving proposals and consider the arrangements in place for delivery.

05 Your audit team

Below are your audit team and their contact details.

Engagement lead (Partner)	• Mark Kirkham • mark.kirkham@mazars.co.uk • 0191 383 6300 or 07747 764 529
Engagement manager (Senior Manager)	• Steve Appleton • steve.appleton@mazars.co.uk • 07881 283 340
Team leader (Assistant Manager)	• Nicola Hallas • nicola.hallas@mazars.co.uk • 07881 283 559

In addition to your audit team, an Engagement Quality Control Reviewer has been appointed for this engagement.

06 Fees for audit and other services

Our audit fees for the audit of the financial statements and for any assurance or other services are outlined in the tables below.

Area of work	2015/16 Proposed fee	2015/16 Scale Fee	2014/15 Actual fee
Code audit work	185,317	185,317	247,089
Certification work	16,520	16,520	26,310
Total fee	**201,837**	**201,837**	**273,399**
Non audit work			
Teachers' pensions return – accountant's report	Subject to competitive quotation	N/a	2,100
Regional Growth Fund – accountant's report on a grant claim	N/a	N/a	1,750
Home and Communities Agency – accountant's report on 2 grant claims	N/a	N/a	1,500

Appendix A - 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 lead.

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 Mark Kirkham, Engagement Lead.

Prior to the provision of any non-audit services the Engagement Lead will undertake appropriate procedures to consider and fully assess the impact that providing the service may have on our auditor independence.

The following threats to our independence and associated safeguards have been identified.

Issue	Perceived threat	Safeguards and procedures
A member of the audit team has a close relation working as a senior manager in the Corporate Fraud Unit.	The close family relationship might be perceived as a threat to our independence.	The member of staff is not involved in audit work relating to benefits, fraud or value for money.
Services in relation to grants and returns certification and assurance.	We have considered threats and safeguards for all grants work as follows: • Self-review: the work does not involve the preparation of information that has a material impact on the financial statements subject to audit by Mazars;	

	• Self-interest: the total fee level is not deemed to be significant to either the Council or Mazars. The work undertaken is not paid on a contingency basis; • Management: the work does not involve Mazars making any decisions in behalf of management: • Advocacy: the work does not involve Mazars advocating the Council to third parties; • Familiarity: the work is not deemed to give rise to a familiarity threat given these pieces of assurance work used to be within the Audit Commission's certification regime and were the responsibility of the Council's appointed auditor; and • Intimidation: the nature of the work does not give rise to any such threat.	
Mazars provides a no charge insolvency support service including issuing to the Council weekly notifications detailing personal insolvencies in the area, submission of council claims and ad hoc insolvency advice.	Management: The perceived threat is that provision of the service may involve management functions.	The services do not involve the exercise of any management functions or decision making.

Appendix B – 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, 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.

We have set materiality at the planning stage at £19,425,000 with a clearly trivial threshold of £486,000 below which identified errors will not usually be reported. We have set lower materiality levels for the disclosure of senior managers' remuneration, members' allowances and exit packages as we consider these items to be of specific interest to users of the accounts sufficient to warrant audit procedures which would not otherwise be applied based on the materiality level for the audit as a whole. 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 C – 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 points with you.

Relevant points that need to be communicated with you at each stage of the audit are outlined below.

Form, timing and content of our communications

We will present to the Governance Committee the following reports:

- our Audit Strategy Memorandum;
- our Audit Completion Report; and
- Annual Audit Letter.

These documents will be discussed with management prior to being presented to the Audit Committee and their comments will be incorporated as appropriate.

Key communication points at the planning stage as included in this Audit Strategy Memorandum

- Our responsibilities in relation to the audit of the financial statements.
- The planned scope and timing of the audit.
- Significant audit risks and areas of management judgement.
- Our independence.
- Responsibilities for preventing and detecting errors.
- Materiality.
- Fees for audit and other services.

Key communication points at the completion stage to be included in our Audit Completion Report

- Significant deficiencies in internal control.
- Significant findings from the audit.
- Significant matters discussed with management.
- Our conclusions on the significant audit risks and areas of management judgement.
- Unadjusted misstatements.
- Management representation letter.
- Our proposed draft audit report.
- Independence.

Key communication points to be included in our Annual Audit Letter

- Summary of the key matters arising from the audit for the year.
- Final fees for audit and other services.
- Future challenges.

Appendix D – Forthcoming accounting and other issues

The 2015/16 CIPFA Code of Practice on Local Authority Accounting (the Code) has made several changes, of which you should be aware. Officers attended a local workshop we held to explain these changes and the possible impact on preparing the financial statements. The workshop provided full details of the changes in the 2015/16 Code as well as a forward look to potential future accounting changes that may be of relevance to the Council. If you require detailed information on any of these changes or any other emerging issues, please contact any member of the engagement team.

Forthcoming accounting issues

Transport infrastructure assets	How this may affect the Council
The measurement basis for the Council's Transport Infrastructure Assets will change from depreciated historic cost to depreciated replacement cost in 2016/17, but with no prior period restatement required. It is likely that the impact of this change will be significant and that the value of these assets on the Council's balance sheet will significantly increase.	We are aware that the Council has been doing work to meet the significant challenges that it faces in introducing this change in measurement basis and have engaged with them at an early stage to provide advice and assistance where required.
Early deadlines	**How this may affect the Council**
The Accounts and Audit Regulations 2015 outline earlier deadlines for local authorities to produce their statements of account to 31 May from the 2017/18 financial year. The deadline for the completion of the audit will also move forward to 31 July.	The impacts of this change on local authorities and their auditors are significant and we have begun to discuss with Council officers how we will meet the challenges the new dates place on us all.
Fair Value accounting	**How this may affect the Council**
The Code adopts the principles of IFRS 13 in respect of measuring fair value for the first time in 2015/16.	We have discussed with officers the implications of IFRS13 on the valuation basis for assets held as surplus assets (e.g. vacated premises) as they will need valuing at market value rather than existing use value.