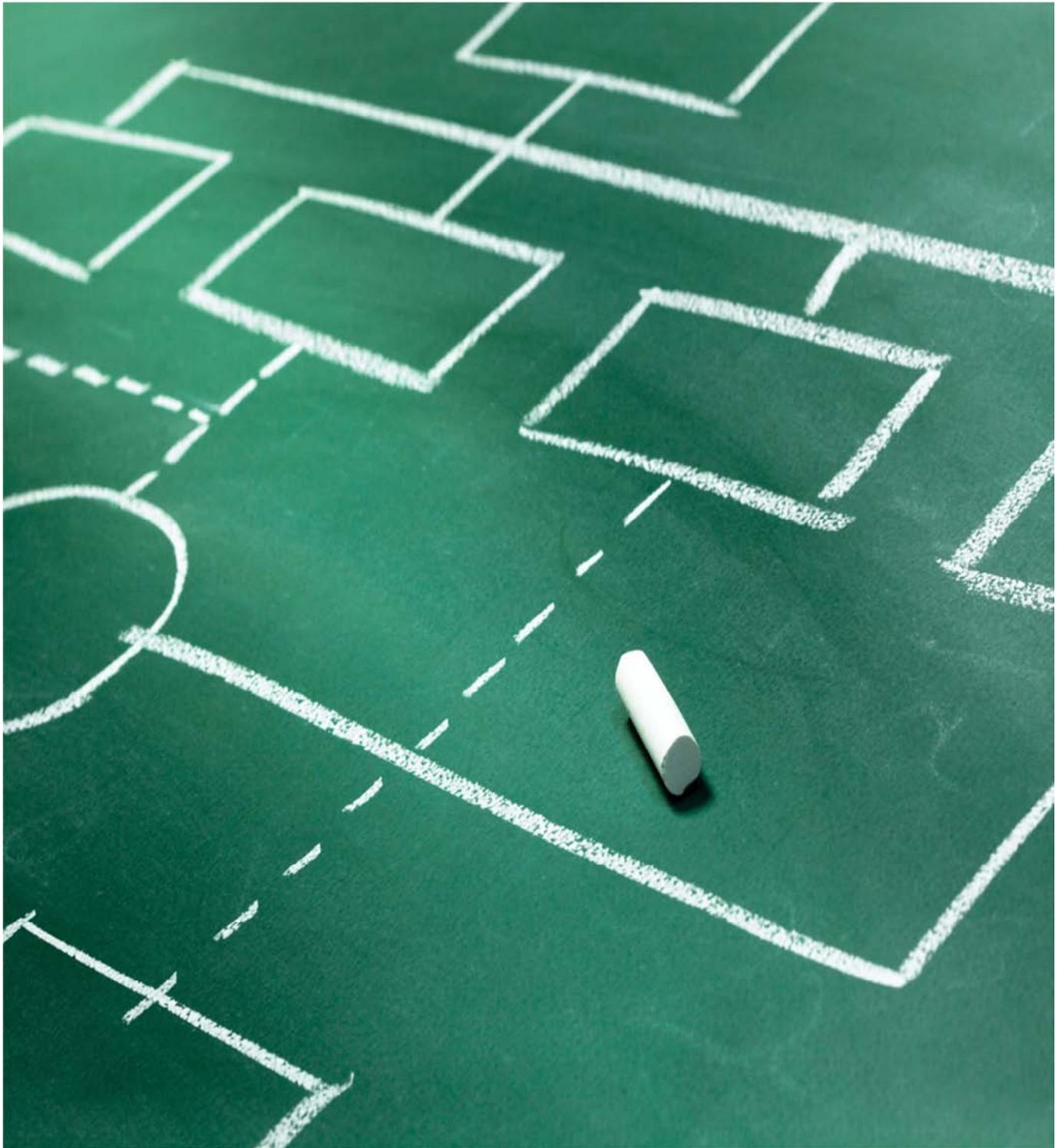


# Audit Strategy Memorandum

Chief Constable for Northumbria – year ended 31<sup>st</sup> March 2014

February 2014



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6 February 2014

Dear Mrs Sim

**Audit Strategy Memorandum for the year ending 31 March 2014**

We are delighted to present our Audit Strategy Memorandum for the Chief Constable for Northumbria for the year ending 31 March 2014.

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 you 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 Joint Independent Audit Committee meeting on 24 February. If you would like to discuss any matters in more detail please do not hesitate to contact me on 07979 164467.

Yours sincerely



Gareth Davies  
Mazars LLP

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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 the Chief Constable for Northumbria for the year ending 31 March 2014, and forms the basis for discussion at the Joint Independent Audit Committee on 24 February 2014.

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 facing the Chief Constable for Northumbria 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 the Chief Constable for Northumbria for the year to 31 March 2014. The scope of our engagement is laid out in the Audit Commission's Code of Audit Practice for Local Government bodies.

## **Responsibilities**

The Audit Commission's Statement of Responsibilities of Auditors and of Audited Bodies sets out our respective responsibilities as the auditor and the audited body. The Audit Commission has issued a copy of the Statement to you.

The Statement summarises where the different responsibilities of auditors and of the audited body begin and end and we undertake our audit work to meet these responsibilities.

We comply with the statutory requirements governing audit work, in particular the:

- Audit Commission Act 1998; and
- Code of Audit Practice for Local Government bodies.

We, as auditors to the Chief Constable for Northumbria, are responsible for forming and expressing an opinion on the financial statements and reaching a conclusion on the arrangements you have put in place to secure economy, efficiency and effectiveness in the use of your resources (the Value for Money conclusion).

Our audit does not relieve management or the Chief Constable, as those charged with governance, of their responsibilities.

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 a whole are free from material misstatement, whether caused by fraud or error. However our audit should not be relied upon to identify all such misstatements.

As part of our audit procedures in relation to fraud 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.

# 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 on Auditing (UK and Ireland) and in accordance with the Code of Audit Practice for Local Government Bodies. 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

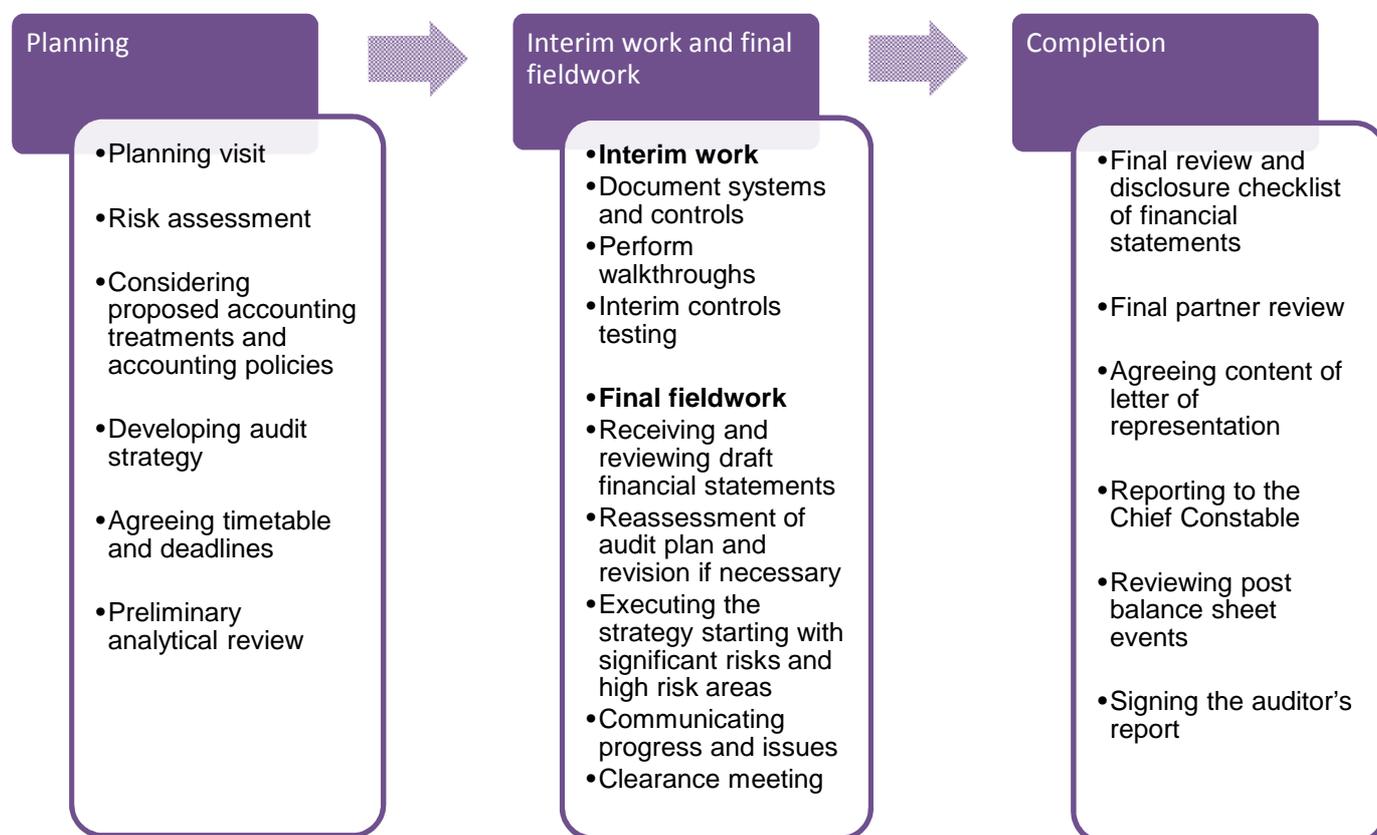
Our audit approach is a risk based approach primarily driven by the risks we consider to result in a higher risk of material misstatement of the financial statements. Once we have completed our risk assessment we develop our audit strategy and design audit procedures in response to this assessment. The work undertaken will 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 below outlines the procedures we perform at the different stages of the audit.



**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.

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

**Reliance on other auditors**

There are material entries in your financial statements where we will seek to place reliance on the work of other auditors.

Items of account	Other auditor	Nature of assurance to obtain from the auditor
Defined benefit liability and associated IAS 19 entries and disclosures	Tyne and Wear Local Government Pension Fund Auditor	Accuracy of data supplied to the pension fund actuary by the pension fund

**Service organisations**

There are material entries in your financial statements where the Chief Constable is dependent on an external organisation. We call these entities service organisations. The table below outlines our approach to understanding the services the Chief Constable receives from the 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
Ledger; Payroll; Accounts payable	Gateshead Council	Assurance gained from our work on Northumbria Police systems hosted by Gateshead Council

**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	Aon Hewitt Limited Actuary; Government Actuaries Department (GAD)	Audit Commission’s consulting actuary (PWC)

**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.





- Start fieldwork on 1<sup>st</sup> July
- Issue Audit Completion Report
- Clearance meeting on 31<sup>st</sup> August



- 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 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 Chief Constable faces and 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 and the areas of management judgement 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.

## Audit risks

### Management override of controls

#### Description of the risk

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 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 through performing audit work over:

- accounting estimates impacting amounts included in the financial statements;
- any identified significant transactions outside the normal course of business; and
- journals recorded in the general ledger and other adjustments made in preparation of the financial statements.

### Revenue and expenditure recognition

#### Description of the risk

There is a risk of fraud in the financial reporting relating to revenue and expenditure recognition due to the potential to inappropriately record revenue and expenditure in the wrong period. Due to there being a risk of fraud in revenue and expenditure recognition we consider it to be a significant risk on all audits.

#### How we will address this risk

We will address this risk through performing audit work over:

- cash receipts and payments in the months of March and April 2014 and their treatment in the financial statements.

## 'Stage 2' transfer

### Description of the risk

Stage 2 transfer will take place by 1 April 2014. There is a risk that the revised arrangements may not be accurately reflected and disclosed in the accounts, including pension liabilities if accurate and timely information about the transfer is not provided to actuaries.

### How we will address this risk

We will address this risk through performing audit work over:

- the proposed timing and nature of stage 2 proposals;
- the outcomes of the process; and
- information supplied to actuaries.

## Production of accounts and provision of financial systems

### Description of the risk

Current arrangements are under review and there is a lack of clarity, in particular around the preparation of the accounts. There is a risk of failure in succession planning for the transfer of functions or that the management of those plans could lead to significant loss of function for the Chief Constable and/or a failure to produce accounts in a timely manner.

### How we will address this risk

We will address this risk through performing audit work over:

- your project plans for transfer of functions; and
- your monitoring of the plans to ensure accurate execution and addressing of any issues arising.

## Key areas of management judgement

### Year-end annual leave accrual

#### Description of the area of judgement

Accounting standards require that an estimate be made of the value of accumulated absences awarded but not taken as at 31 March 2014.

#### Our planned audit approach

We will examine the method used for producing this estimate and compare it against that used in previous years. We will review the detail of the calculation for accuracy.

## Pensions Costs and Pensions Liability

### Description of the area of judgement

Pensions costs and pensions liabilities for both civilian and police officer pensions must be shown in the accounts of the body responsible for their pay expenditure. These amounts reflect the pensions earned by service up to the year end 31 March 2014 but to be paid in the future. These amounts are valued on your behalf by the actuaries Aon Hewitt Limited (Tyne and Wear Local Government Pension Scheme) and GAD (Police Pensions Scheme).

### Our planned audit approach

We will examine the pensions disclosures made by you to ensure that they accurately reflect the information provided by the actuaries. We will also test the information provided to the actuaries by you and by the Tyne and Wear Pension Fund.

# 04 Value for Money Conclusion

We are required to reach a conclusion on your arrangements to secure economy, efficiency and effectiveness in the use of your resources.

Our conclusion on your arrangements is based on two criteria, specified by the Audit Commission:

- securing financial resilience – focusing on whether you are managing your financial risks to secure a stable financial position for the foreseeable future; and
- challenging how you secure economy, efficiency and effectiveness – focusing on whether you are prioritising your resources within tighter budgets and the need to improve productivity and efficiency.

We set out significant risks that we will address through our work.

## Arrangements Fail to Provide Value for Money

### Description of the risk

There are many significant challenges facing the Chief Constable for 2013/14, including:

- reduced grant funding;
- budget pressures;
- changes in responsibilities as stage 2 is implemented; and
- developing governance and support service arrangements.

In addition, this is the first year that we are assessing arrangements against the full VFM criteria set by the Audit Commission. Last year, recognising that it was the first year of the new policing arrangements, the Audit Commission disapplied its criteria and instead required us to review your Annual Governance Statement, consider any inspection reports and carry out local work if required.

In line with good practice, the Chief Constable (together with the Police and Crime Commissioner) is reviewing critical support services. As organisational circumstances continue to develop, there are risks that governance and financial management arrangements do not keep pace with wider organisational changes.

### How we will address this risk

As a result, our work will be wide ranging in scope and will include:

- considering progress on the matters raised in the Annual Governance Statement for 2012/13;
- 'stage 2' transfer of powers to the Chief Constable from the Police and Crime Commissioner;
- financial management, systems and other governance arrangements including changes made as a result of reviewing existing service agreements; and
- robustness of budget setting and monitoring.

We will base our work on your self assessment, which officers have agreed to complete.

## 05 Your audit team

Below are your audit team and their contact details.

Engagement lead /  
Partner

- Gareth Davies
- [gareth.davies@mazars.co.uk](mailto:gareth.davies@mazars.co.uk)
- 07979 164467

Engagement senior  
manager

- Caroline Tyrrell
- [caroline.tyrrell@mazars.co.uk](mailto:caroline.tyrrell@mazars.co.uk)
- 0191 383 6316

Team leader

- David Hasnip
- [david.hasnip@mazars.co.uk](mailto:david.hasnip@mazars.co.uk)
- 0191 383 6332

## 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. Our fee for 2013/14 is the Audit Commission scale fee and the reduction since 2012/13 is due to a reduction in the Audit Commission scale fee. At this stage we do not expect to need to seek a variation in the scale fee, on the assumption that the necessary working papers and other supporting documents to the financial statements are available in time for the audit work to be completed in line with the timetable set out on pages 3-4. We are not proposing any non-audit work.

Area of work	2013/14 Proposed Fee	2013/14 Scale Fee	2012/13 Actual Fee
Code audit work	£25,000	£25,000	£25,000
Certification work	0	0	0
<b>Total fee</b>	<b>£25,000</b>	<b>£25,000</b>	<b>£25,000</b>

# 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 Ethical Standards issued by the Auditing Practices Board. 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 Gareth Davies.

Prior to the provision of any non-audit services Gareth Davies 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.

# 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 provide 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 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 to you.

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

## **Form, timing and content of our communications**

We will present to the Chief Constable the following reports:

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

These documents will be discussed with management prior to being presented to the Chief Constable 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; and
- 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; and
- Our independence.

# Appendix D – Forthcoming accounting and other issues

The 2013/14 CIPFA Code of Practice on Local Authority Accounting (the Code) has made several changes, of which you should be aware. Officers from the finance function will be invited to workshops that will provide full details of the changes in the 2013/14 Code as well as a forward look to potential future accounting changes that may be of relevance to the Chief Constable. The main change likely to impact on the Chief Constable is set out below. If you require detailed information on this change or any other emerging issues, please contact any member of the engagement team.

## Forthcoming accounting issues

Employee benefits	How this may affect the Chief Constable
The Code includes changes as a result of the adoption of the amended IAS 19 Employee Benefits.	<p>The main potential impacts of the changes are:</p> <ul style="list-style-type: none"><li>• changes in terminology used for some entries in the Chief Constable's CIES and disclosure notes;</li><li>• minor changes to the recognition point for termination benefits that may either delay or bring forward the recognition of expenses such as redundancy payments;</li><li>• significant changes to the format and content of relevant disclosure notes; and</li><li>• changes to the classification, recognition and measurement of post-employment benefits.</li></ul> <p>Where these changes have a material impact on the accounts, it is likely that the Chief Constable will need to restate the 2012/13 comparative entries in the accounts.</p>