

# Wales Audit Office

Audit findings report year ended 31st March 2020

1 June 2020

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# Executive Summary

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 31st March 2020.

The scope of our work was communicated to you via our Audit Plan document. We believe that the audit approach adopted will provide the Audit and Risk Assurance Committee with the required confidence that a thorough and robust audit has been carried out.

Our audit work is substantially complete and subject to the successful resolution of outstanding matters, we anticipate issuing an unmodified audit opinion on the group's financial statements in line with the agreed timetable.

## Final materiality

Materiality was determined based on an effective rate of 2.1% of expenditure for the year. This benchmark and percentage are consistent with the calculations detailed in the Audit Plan.

## Unadjusted audit differences

We have not identified any nontrivial audit adjustments, which is confirmed within the Appendix. We have not identified any material disclosure omissions that have not been updated in the draft statutory accounts.

## Risks and approach

We have carried out testing as planned on the risks identified during planning and draw your attention to the following key points for discussion:

- Revenue and WIP recognition
- Management override of internal controls
- Reputational risk
- Brexit financial reporting considerations

We have also identified additional risks during the course of our audit which are discussed below:

- COVID-19 financial reporting considerations

## Risks identified at the planning stage

Risk	Description	Response	Findings
Management override of internal controls	In any organisation there will be an extent to which management can bypass internal controls. By definition, there can be no controls over this risk and this is specifically stated in International Standards on Auditing: 240. Such override, if exercised, could give rise to material fraud or misstatement in the financial statements.	<p>We will discuss and consider segregation of duties within the established control environment.</p> <p>We will review controls over journal entries and, using data analytics and based our on risk assessment, test a sample of journals to ensure that they are valid and appropriately supported.</p> <p>We will obtain an understanding of the business rationale of significant transactions that we become aware of during the audit process that appear to be outside the normal course of business or that appear to be unusual, given our understanding of the entity's operating environment.</p> <p>We will consider estimates and judgements made by management in the preparation of the statutory accounts and conclude on their appropriateness.</p>	<p>The testing was completed as planned with no significant issues identified to report to management.</p> <p>We have tested a sample of the journal entries posted during the year, and this did not highlight any erroneous entries, or items indicative of undue management bias.</p> <p>We have reviewed the significant estimates adopted in the preparation of the financial statements, and we have not identified any areas where there appears to be indication of management bias. Our review of the estimates made in respect of the dilapidations provision and the bad debt provision indicated that these appear to have been derived on an appropriate and consistent basis.</p>
Reputational risk	Given the public interest in the financial statements, there is a risk that accounting judgements may be influenced by the desire to demonstrate good financial management and remain within the Estimate.	<p>We will undertake internal specialist technical reviews of both the accounts, and also our audit work, given the increased reputational risk associated with the audit.</p> <p>We will review the judgemental aspects of year-end balances, particularly focusing on any round sum provisions, estimates, recoverability of debtors, disclosure of remuneration and related party transactions.</p>	<p>During the course of the audit, we have not identified any areas from the WAO's operations that suggests there are any matters whereby the reputation could appear to be significantly damaged.</p> <p>As discussed previously, our review of judgemental areas has not noted any areas of inappropriate activity, or areas where the Office has been acting inappropriately.</p> <p>We are satisfied that there appears to be appropriate disclosure of the remuneration of directors and senior management.</p> <p>Our conclusions on our regularity reporting are discussed later in this report.</p>

Risk	Description	Response	Findings
Revenue recognition – WIP and deferred income	The recognition of income, WIP and deferred income is considered to be a significant risk due to the level of judgement applied to the stage of completion of an audit assignment and any provisions required.	<p>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.</p> <p>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.</p> <p>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.</p>	<p>Our work indicated that the organisation has appropriate systems for assessing the stage of completion of its ongoing contracts, and hence for determining the amount of revenue that should be reported at the year end.</p> <p>Our review of the actual outturn on prior year contracts indicated that the estimates made at the prior year end proved materially accurate.</p> <p>We have selected a sample of contracts as planned. Based on our analysis of the cost to complete estimates, discussions with project managers, and post year end performance, we have not identified any misstatements with regards to revenue recognition. We have tested the reliability of the underlying time recording system and not noted any inaccurate or incomplete data.</p> <p>In the prior year, we noted that where onerous contracts were identified, the full loss was not initially recognised as a provision in the financial statements (instead being apportioned based on the stage of completion). While this was recorded as an audit adjustment in the prior year, no such adjustment is required in 2020 as the full loss provision has been recognised as expected.</p> <p>Where refunds are due because audits have been completed at a lower cost than budgeted, the balance of refunds were originally classified within deferred income. This would normally be reclassified to accruals however the reclassification would be a trivial adjustment at approximately £3,000 and has therefore not been made.</p> <p>We have noted that all cost to complete assessments made by project managers have had an additional 5% added to them by the finance team. This is to estimate the additional cost expected to be incurred resulting from COVID-19. While there are no detailed calculations to support this percentage, it represents managements best estimate of the additional cost – however management acknowledge there is a high level of estimation within this percentage. The total impact of adding 5% to costs to complete is approximately £55,000 on 2020 revenue and not considered a material amount, or necessarily an error.</p>

Risk	Description	Response	Findings
Brexit financial reporting considerations	<p>The longer-term effects of the UK's potential exit from the European Union remain unclear.</p> <p>Businesses face a period of political and economic uncertainty which may expose them to new opportunities and/or risks, or change the scale and likelihood of existing ones, that affect their business model and strategies.</p> <p>Identifying the significant effects, or possible significant effects, of Brexit and assessing their impact may prove challenging in the current political and economic environment. However, we expect management to provide us with their analysis of the potential Brexit effects they have identified, together with supporting evidence in relation to key assumptions and related disclosures.</p>	<p>As part of our audit we will consider management's analysis of the potential Brexit effects on the entity's operations and strategies (e.g. specific audits, staff costs, and reputational focus), and the forward-looking assumptions used by management in their assessment relating to future activity and decision making.</p> <p>We shall consider the appropriateness of the disclosures in the Annual Report in respect of Brexit related principal risks and uncertainties and future plans.</p> <p>We may seek written representations from management about their plans for mitigating potentially adverse effects of Brexit.</p>	<p>Our review of the Annual Report indicates there appears to be appropriate disclosure of the risks associated with the UK's potential departure from the European Union.</p>

# Risks identified during the audit

Risk	Description	Response	Findings
COVID-19 financial reporting implications	Since our Audit Plan was issued on 26 February, COVID-19 has been declared a global pandemic by the World Health Organisation and has had a major impact on the world economy. All businesses are expected to be impacted by COVID-19 and we therefore consider the impact of COVID-19 on all of our audits.	We have discussed the impact of COVID-19 with management. Given COVID-19 was declared a global pandemic on 11 March, this was pre year end and therefore an adjusting event for the purposes of considering carrying values of assets and liabilities. We asked management to prepare a paper for us to assess the impact COVID-19 has on the financial statements, and also on the going concern assumption adopted in the financial statements.	<p>We have reviewed the paper prepared by management. We agree with the conclusion that there is no material impact on the carrying value of assets or liabilities from COVID-19.</p> <p>We have also considered the impact of COVID-19 on going concern.</p> <p>As laid out in the Public Audit (Wales) Act 2013, there is a requirement for the Wales Audit Office to be funded to continue to provide its services. We have reviewed recent estimates prepared by management which have identified substantial cost savings in the event of reduced fee income. We have noted the Chair and Auditor General have advised the Senedd's Finance Committee of the need for supplementary funding in 2020-21 which will allow the entity to continue its operations for the full financial year.</p> <p>In the event that the Committee does not approve additional resources in the autumn, immediate steps will be taken to contain expenditure within existing approved limits, which management believe can be done to ensure Wales Audit Office remains a going concern.</p> <p>Our audit report contains no modification in respect of this conclusion and the financial statements have appropriate disclosure relating to this matter.</p>

# Regularity issues identified during the audit

Issue	Response
<p>Since the Wales Audit Office Board came fully into effect in 2014, expenses incurred by and on behalf of the Chair of the Board have been funded through the WAO's Estimate from the Welsh Consolidated Fund.</p> <p>From April 2019, HMRC required that the tax liability on the Chair's expenses to be directly recovered through the payroll. The WAO does not administer the Chair's salary through payroll, the Commission itself does.</p>	<p>An agreement has been reached with the Assembly Commission to amend the payment process. The Chair's expenses are now directly charged on the Welsh Consolidated Fund, rather than being indirectly recovered through the Estimate. It has been agreed with the Assembly that the 2021 estimate will be reduced by the value of the Chair's expenses, approximately £5,000, as part of the year end outturn. No adjusting corrections are needed in respect of previous years because there is no consequential misstatement in any accounts.</p>
<p>An internal audit report on financial controls identified that one item within the sample of 25 purchase orders was not correctly authorised by the budget holder. We have considered the impact of this on our regularity audit.</p>	<p>The purchase order system providers to Wales Audit Office were able to match all purchase orders to identify a total of 6 purchase orders totalling approximately £36,000 which were not sent to the budget holder for their approval. Retrospective approval was sought and obtained for all of these items. We do not believe this incident to have any impact on our regularity opinion, on the basis that the issue arose from unforeseen network performance issues with the server which have since been rectified, and these items were followed up when identified and subsequently approved. Managements have resolved that going forward, reports are ran on a monthly basis to match purchase orders to their subsequent approval to confirm no items remain unapproved.</p>
<p>We have noted that a lift maintenance contract was entered into during the period. However, on inspection of the retained procurement documentation, we have noted that two quotes were not sought for this contract in line with the procurement policy. When a purchase invoice was received for the service, it has been matched to an existing PO and subsequently approved.</p>	<p>This is not in line with the procurement policy. The amount is not considered material (at approximately £3,000) and all other items in our sample had sought the appropriate number of quotes. We have included a control deficiency in respect of this item below.</p>



# Recommendations on controls

We have set out below recommendations on internal controls which came to our attention during the course of our audit work. This does not constitute a comprehensive statement of all internal control matters 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.

## Assessment Issue and risk



### • Review of payroll

#### Recommendations

- We have noted that variance analysis is prepared on monthly payroll costs, however this analysis does not contain a set variance that would require investigation and is instead up to the preparer to determine what constitutes a difference worth investigating. Additionally, while the ultimate payment of the payroll is subject to a review, there is no line by line documented review of the payroll, other than this variance analysis.

#### Management Response

- Changes to payroll are processed and checked by the HR team prior to being sent to our external payroll providers for processing. The resulting payroll is subject to a check by the Finance team prior to being approved for payment. Any unexpected month on month variances are checked back to source documents to ensure appropriate approvals are in place. Going forward we will formalise this to ensure that all variances of more than 2% are checked and documented.



### • Procurement

#### Recommendations

- As part of our regularity work, we have noted that one item in our procurement sample did not obtain the required number of quotes. We understand that there had been a change in the staff responsible for obtaining these quotes and managing the process. We would recommend that staff training in this area is revisited, and that there is a periodic review of the contracts schedule to ensure the correct number of quotes were sought, with supporting evidenced retained.

#### Management Response

- Further training is planned for the team in relation to purchase orders and contracts. We will be further developing our contract management arrangements to automate review of the schedule for timely reminders and procurement. Work will also include periodic review of arrangements for compliance.

## Assessment

- Significant control recommendation
- Other control recommendations

## Going concern

We have reviewed the budget prepared. Based on our analysis we believe the company is a going concern and the financial statements have been prepared on this basis.

## Significant difficulties encountered during the audit

No significant difficulties have been encountered during the audit. We would like to thank Steven O'Donoghue, Nicola Evans and the rest of the finance team for their hard work and cooperation during the audit.

## Representations Requested

In addition to those representation which we request on all audit assignments (<http://www.rsmuk.com/standard-representations>) we will be seeking no specific representations from the Board.

## Accounting estimates

As part of our audit, we review the significant accounting estimates contained within the financial statements of the WAO. We note the following:

### Costs to complete/work in progress

Our work indicates that the historical estimates of costs to complete are materially accurate, and that estimates made by the Resource Managers are an appropriate basis to determine percentage completion.

### Dilapidations provision

These continue to be derived using latest available third-party surveyor reports, and there is no evidence that these are not an appropriate source of evidence to derive such provisions. Previous surveyor reports provided have not identified any significant issues that would necessitate a material increase in the value of the reported provision.

## Management judgements and accounting estimates

The following areas are considered to be the principal areas of management judgement or accounting estimates. The graphic below visually represents the impact (lower or higher) on the financial statements of a change in management's estimate. In overview, a reasonably possible change in estimate that has a low impact means that such a change will have limited impact on the financial statements. Conversely a reasonably possible change that has a higher impact, means that such a change can have a significant impact.

### Judgments and estimates

	Low impact		High impact
Provision for bad debts	●		
Revenue recognition – stage of completion			●
Dilapidations provision		●	
Senior team restructuring	●		

# Update on matters communicated at the planning stage

Matter communicated	Update
<b>Fees</b>	We confirm that the fees charged during the year in respect of services performed are consistent with those contained within our Audit Plan submitted to you
<b>Independence</b>	In accordance with International Standard on Auditing (UK) 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

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## Adjusted and unadjusted statements and disclosures

### Accounting 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. Our level of triviality was set at £23,000.

Adjustment	Type of adjustment	Financial statements area	Value £'000	Description
1	Adjusted	Accrued income	21	Adjustment to correct prior year charge out rates used in costs to complete assessments
	Adjusted	Audit fee income	(21)	Adjustment to correct prior year charge out rates used in costs to complete assessments
2	Unadjusted - judgemental	Accrued income	26	Being judgemental element added to costs to complete assessments for COVID-19 impact
	Unadjusted - judgemental	Deferred income	29	Being judgemental element added to costs to complete assessments for COVID-19 impact
	Unadjusted - judgemental	Audit fee income	(55)	Being judgemental element added to costs to complete assessments for COVID-19 impact

We have identified no unadjusted disclosure misstatements.

## Communication of audit matters to those charged with governance

### Our communication plan

	Audit plan	Audit findings
Respective responsibilities of auditor and management/those charged with governance	●	
Overview of the planned scope and timing of the audit, form, timing, materiality and expected general content of communications including significant risks and key audit matters	●	
Confirmation of independence and objectivity	●	●
Significant matters in relation to going concern (if any)		●
Views about the qualitative aspects of the Group's accounting and financial reporting practices including accounting policies, accounting estimates and financial statement disclosures		●
Significant findings from the audit		●
Significant matters and issues arising during the audit and written representations that have been sought		●
Significant difficulties encountered during the audit (if any)		●
Unadjusted misstatements and material disclosure omissions		●
Expected modifications to the auditor's report, or emphasis of matter		●

ISA (UK) 260, as well as other ISAs (UK), prescribes matters which we are required to communicate with those charged with governance, and which we set out in the table here.

The Audit Plan outlined our audit strategy and plan to deliver the audit, while the Audit Findings presents key issues, findings and other matters arising from the audit, together with an explanation as to how these have been resolved.

### Respective responsibilities

As auditor we are responsible for performing the audit in accordance with ISAs (UK), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance.

The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

## Financial reporting updates

### Important updates

A full list of financial reporting updates can be found by clicking the link below:



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Our Report is prepared solely for the confidential use of Wales Audit Office and solely for the purpose of explaining the scope of the audit, our proposed audit approach, and to highlight the key risks that we will be focusing our audit work upon, forming part of the ongoing communications we are required to make under International Standard on Auditing (UK and Ireland) 260 – Communication of audit matters with those charged with governance. Therefore, the report may not, without our express written permission, be relied upon by Wales Audit Office for any other purpose whatsoever, be referred to in whole or in part in any other external document or made available (in whole or in part) or communicated to any other party. RSM UK Audit LLP neither owes nor accepts any duty to any other party who may receive our Report and specifically disclaims any liability for any loss, damage or expense of whatsoever nature, which is caused by their reliance on our Report.

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