



Accountants &
business advisers

**Joint Audit Arrangements
between Lewes District Council
and PKF**

2007/08 to 2011/2012



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1 Introduction

- 1.1 The Audit Commission continues to encourage appointed auditors to work to ensure that audit work is being effectively targeted, thereby seeking to reduce the time spent on the external audit. In addition, Audit Committees are increasingly keen to ensure that the services of internal and external audit are as integrated as possible, in order to maximise the effectiveness of the overall approach to audit operated within their organisation.
- 1.2 One of the critical success factors supporting a fully integrated audit approach is effective communication and co-ordination between internal and external audit, such that it allows best use of joint audit resources and enables external audit to place the maximum level of reliance on the work of internal audit in the discharge of external audit's duties under the Audit Commission's Code of Audit Practice ("the Code")

The approach at Lewes District Council

- 1.3 PKF (UK) LLP, as the Audit Commission's appointed external auditors for Lewes District Council, will work together with internal audit to achieve an integrated approach. Therefore, in developing the external Annual Audit Plan for Lewes District Council, PKF has made some assumptions about the quality and appropriateness of the work of internal audit on which PKF might place reliance. In setting the level of fees PKF has anticipated that all of those assumptions will be met.
- 1.4 This joint protocol has been produced to formalise the working relationship between internal and external audit in order to:
- clarify areas of co-operation in planning the audit, reviewing internal audit work and reporting to clients
 - improve communication and co-ordination and therefore further enhance the audit approach, maximising the potential for each party to rely on the work undertaken
 - help reduce any unnecessary overlap of audit effort.

2 Scope and responsibilities

Code of Audit Practice

- 2.1 External audits in Local Government are carried out in accordance with the *Code of Audit Practice* ('the Code') issued by the Audit Commission. The main area of co-operation between Lewes District Council and PKF arising from the Code centres on the responsibility of PKF to express an opinion on whether the financial statements present fairly the financial position and income and expenditure for the year under audit.
- 2.2 In carrying out this work PKF is required to consider:
- the extent to which the accounting and internal control systems are a reliable basis from which to prepare the financial statements
 - the risk of material misstatements, including the risk of fraud and error, which may have an impact on the audit opinion
 - the consistency of the disclosures in the Annual Governance Statement to evidence provided by the organisation in its effectiveness review and our knowledge of the client.
- 2.3 This involves evaluating the key controls within the organisations' financial systems, with particular focus on assessing whether the controls in place are suitably designed and operating as intended in order to mitigate significant risks and prevent material misstatements within the accounts.

CIPFA Internal Audit Standards

- 2.4 The internal audit service is carried out in line with the CIPFA Code of Practice for Internal Auditors in Local Government in the UK. All local authorities should make provision for internal audit in accordance with this Code of Practice. In addition, the Accounts and Audit Regulations 2006 (which came into force on 1 April 2006) require bodies to conduct a review of the effectiveness of internal audit at least once a year.
- 2.5 In carrying out its work internal audit at Lewes District Council undertakes annual reviews of a sample of key financial systems, with additional testing of the key controls on the other key financial systems, to provide assurance that appropriate financial controls are in place and that the associated risks are sufficiently mitigated.
- 2.6 Internal audit at Lewes District Council also investigates all reported cases of fraud, impropriety or misconduct and reports to senior management and the Audit Committee as appropriate. The Head of Audit and Performance assesses the strength of the arrangements to prevent and detect fraud as part of the annual review of Corporate Governance and via the feedback from the Assurance Framework.
- 2.7 In addition, internal audit carries out testing for the audits of the Housing and Council Tax Benefits and National Non Domestic Rates subsidy grant claims.

Assurance overlaps

- 2.8 There are areas of responsibility and review where the work of external audit and internal audit overlaps, particularly with respect to the review of the operating effectiveness of internal controls.
- 2.9 Under the integrated audit approach, the detailed review of the operating effectiveness of internal controls and the strength of the arrangements for the prevention and detection of fraud is usually undertaken by internal audit. The external auditor should then be able to place reliance on this work in order to be able to assess the strength of the overall control environment, to obtain sufficient evidence of the effectiveness of specific internal financial controls, and to assess the impact of any reported frauds on the financial statements

3 Planning

3.1 In planning its audit work PKF gives regard to the strategic audit plan and annual audit plan of internal audit in terms of the:

- coverage of key financial systems
- coverage of other areas of audit risk under the Code.

3.2 The table below highlights the key mechanisms for achieving this:

Joint working arrangements for planning and liaison
<p>Planning</p> <ul style="list-style-type: none"> • PKF and internal audit will liaise during preparation of their draft strategic audit plan and/or annual audit plan to agree audit coverage, methodologies, timing of work and staffing arrangements. • The Annual Audit Plan will be largely based on an assessment of risk, taking account of the organisation’s risk register, however it will also include annual consideration of all of the key financial systems at the Council. • The timing of internal audit work on the key financial systems will be scheduled so as to ensure maximum coverage of the audit year. • PKF will share its control evaluation summaries (“CESs”) with internal audit, highlighting those control objectives on which PKF will be placing reliance and requiring effectiveness testing under the external audit strategy for the audit of the accounts. • Planning of internal audit reviews will specifically include coverage of all key control objectives for the key financial systems, that require effectiveness testing by PKF’s CESs. • Prompt communication between internal and external audit of areas where coverage / depth of internal audit review is not planned to meet the needs of PKF or where either party needs to vary the coverage of work for any new requirements or unforeseen events.
<p>Liaison</p> <ul style="list-style-type: none"> • PKF and internal audit will have three formal liaison meetings during the year as follows: <ul style="list-style-type: none"> - February, to discuss audit plans and risk areas - June, to discuss feedback from external audit’s interim review - September, to discuss audit progress and key issues/risks arising. • PKF and internal audit will also maintain regular informal contact to advise each other of any significant new developments and key issues arising. • Internal audit will liaise with departments regarding delivery of internal audit work throughout the year and action will be taken should the timetable for delivery slip, including ability to comply with the delivery of all necessary files in line with the mutually agreed external audit start date.

4 Reviewing the work of Internal Audit

4.1 In order to determine the reliance that can ultimately be placed on the work produced by internal audit, PKF will undertake a review of the files that they will be seeking to place reliance on. This review will include some re-performance testing of internal audit work to determine the quality and adequacy of the testing performed, the sufficiency of the evidence retained to support the conclusions made and the appropriateness of those conclusions.

4.2 The table below highlights the key mechanisms for achieving this:

Review of key financial systems and grant claims transactions testing
<p>Internal Audit's review</p> <p><i>Systems documentation and walkthroughs</i></p> <ul style="list-style-type: none"> • For each of the key financial systems internal audit's working papers will document the actual key controls in place. • For each of the key controls in place within the key financial systems, internal audit will obtain 'walkthrough' evidence to support the existence of the control operating in practice (this may be taken from the sample of controls tested for effectiveness) and consider whether it achieves its intended objective, and this evidence will be retained on file. <p><i>Effectiveness testing</i></p> <ul style="list-style-type: none"> • Internal audit will carry out detailed testing on all of the key controls which external audit has indicated require effectiveness testing in PKF's CESs (unless specific areas of non-coverage are agreed at the planning stage). • Internal audit samples will be selected so as to: <ul style="list-style-type: none"> ○ achieve maximum coverage the financial year being audited to the date of the audit work ○ cover all significant income and expenditure streams for which coverage has been requested by external audit. • A minimum sample of 20 (pro-rated downwards for populations below 100) will be tested to ensure the effectiveness of each existing key control and auditor judgements on increases to these sample sizes will be documented. • The population source, population size (estimated if necessary) and method of sample selection will be documented for each test undertaken. • A full set of supporting evidence for at least one of the sample reviewed for effectiveness testing (where there was a satisfactory result) will be retained on file along with copies of documentation to evidence all failures of the operating effectiveness of the control. This may be the same documentation as that retained for the existence walkthrough above. • Documentation retained on file as audit evidence will be annotated to state its source (if it is an extract of a larger document), cross referenced to the test for which it is being used as evidence and marked/annotated to identify which specific part of the document evidences the test's conclusion. • Where errors in the effectiveness of a key control are identified, further audit work will be done to ascertain whether those errors are isolated or systematic. Where it is deemed that there has been a systematic breakdown in effectiveness, a quantification of the impact of that control breakdown on the system's output will be performed. • Every test will include its own individual conclusion. • Notes from discussions with officers will state the officer consulted and the date of discussion, as well as the outcome. • There will be a clear audit trail from the test conclusions through to the matters raised and recommendations contained in the draft report.

- All of the required internal audit files will be provided for review on the mutually agreed external audit review dates.

Effectiveness of internal audit

- The Head of Audit and Performance carries out an annual review of the effectiveness of internal audit, with the results independently reviewed by the Director of Finance and Community and Services and reported to the Audit Committee.

External audit's review of internal audit's work

- PKF will carry out its review of internal audit work at Lewes District Council offices on the dates agreed with internal audit.
- PKF will also review and seek to rely on the annual effectiveness review carried out by the Head of Audit and Performance.
- Upon completion of the review PKF will feed back to internal audit any issues arising, and assess the potential for remedy and the impact of any matters not easily rectified.
- PKF will assess the impact of any areas where the work of internal audit does not satisfy the requirements of external audit and discuss and agree the way forward with internal audit.

Reporting

- The final reports of internal audit will be available before commencement of the final external audit of the financial statements.
- PKF will provide feedback to internal audit on the results of their reviews of key financial systems before finalisation of PKF's report.
- External audit reports will not duplicate recommendations already raised by internal audit but will, where applicable, emphasise matters deemed to be of particular significance in the main body of the report.