



WALES AUDIT OFFICE

Final Audit Findings Report

Year ended 31 March 2019

Presented to the Audit and Risk Committee
By RSM UK Audit LLP

On 4 June 2019

And issued as final on 5 June 2019



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This report has been prepared for the sole use of Wales Audit Office and must not be disclosed to any third party, or quoted or referred to, without our written consent. No responsibility is assumed to any other person in respect of this report.

1 INTRODUCTION AND COVERAGE

This report summarises our key findings in connection with the audit of the financial statements of Wales Audit Office in respect of the year ended 31 March 2019.

The scope of our work has already been communicated to you via our Audit Plan document dated 27 February 2019.

A summary of adjusted and unadjusted misstatements identified during the audits has been prepared and is included in Section 5.

We consider that the audit approach adopted will provide the Directors with the required confidence that a thorough and robust audit has been carried out and can confirm that, at the date of this report, we anticipate no modifications from our pro-forma audit report provided in the Audit Plan previously communicated to you.

2 AUDIT AND ACCOUNTING ISSUES IDENTIFIED AT PLANNING STAGE

Management override of internal controls

| | |
|----------------------------|---|
| Area of audit focus | Systems of internal control are designed to mitigate inherent risks of error within the core control systems to an acceptable level. By nature, a management override or by-pass of controls cannot be eliminated by the implementation of controls and therefore as part of our audit we will perform additional tests of detail to address this risk. |
| Our approach | <p>We will test the appropriateness of a sample of journal entries recorded in the general ledger and other adjustments made in the preparation of financial statements, tracing selected entries back to source documentation.</p> <p>We will review significant accounting estimates and policies which could involve bias resulting in a material misstatement.</p> <p>We will discuss the basis and business rationale for any significant non-routine or contentious transactions which come to our attention during the course of our audit and will fully report the outcomes of our testing in our audit findings report.</p> |
| Response | <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. We have commented later in this report on the judgements made in assessing the stage of completion of the organisation's long-term contracts.</p> |

Brexit financial reporting considerations

Area of audit focus

The longer-term effects of the UK's potential exit from the European Union remain unclear.

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.

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.

Our approach

As part of our audit we will consider management's analysis of the potential Brexit effects on the entity's operations and strategies (eg 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.

We shall consider the appropriateness of the disclosures in the Annual Report in respect of Brexit related principal risks and uncertainties and future plans.

We may seek written representations from management about their plans for mitigating potentially adverse effects of Brexit.

Response

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.

As the nature and timing of any potential departure remains unclear, this is an area which the management and board need to keep under regular review.

Income recognition, WIP and deferred income

Area of audit focus

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.

Our approach

We will select a sample of projects that have commenced throughout the year and test the revenue recognised with reference to the stage of completion of the assignment in order to determine that the revenue recognition is appropriate and consequently whether the WIP and deferred income are appropriately stated.

We will review correspondence with audit managers to establish the estimated costs to complete and any required provisions at the year end, considering the impact of any time spent after the year end on these estimations.

We will also review time postings after the year end for any time posted by employees relating to work done before the year end that may not have been factored into the above calculations.

Response

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.

Our review of the actual outturn on prior year contracts indicated that the estimates made at the prior year end proved accurate.

However, our work did identify the following matters:-

a) On one contract, an additional fee of £74k had been agreed to compensate the WAO for the extra time incurred on the completion of the contract. As the finance team had not been notified of this additional fee, no allowance had been made in the reported revenues for the year.

b) We noted that there had not been full provision made for the full extent of anticipated losses on contracts where these are foreseen. An additional £87.5k provision is required to be made for such contracts.

c) At the year end, there were certain contracts which were closed, and where refunds were due. There are credit balances of £112k on such contracts which should be reclassified as creditors, rather than being held in deferred income.

d) The draft accounts made no adjustment for the work in progress relating to work undertaken by third party firms

It has been agreed that adjustment will be made for the matters in a) to d) above and these have been reported in Section 5 and adjusted in the final accounts.

Reputation

Area of audit focus

Due to public interest in the financial statements there is a desire to maintain reputation and demonstrate exemplary financial management. Accounting judgements may be influenced by the desire to demonstrate good financial management and remain within the Estimate.

Our approach

Independent technical review of the accounts and key judgement areas. Review of judgemental aspects in year-end balances particularly focusing on any;

- Round sum provisions
- Estimates
- Recoverability of debtors
- Disclosure of remuneration

Response

During the course of the audit, we have not identified any areas from the WAO's operations that suggests there are any matters whereby the reputation could appear to be significantly damaged.

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.

We are satisfied that there appears to be appropriate disclosure of the remuneration of directors and senior management.

We noted two data breaches in the year, one of which resulted in a report to the ICO, and which appears to have been fully followed up.

The second matter related to the theft of a business lap top, a personal lap top and various papers from a vehicle. This matter appears to have been subject to appropriate internal review by management and the legal team, which concluded that it was not a data breach that needed to be reported to the board or the ICO.

We have included a recommendation in Section 6 in relation to this event and shall also be seeking a representation in respect of this matter.

New accounting system

Area of audit focus

During the year, we are aware that a new accounting system has been implemented.

There is an inherent risk that the transition to a new system could result in incomplete or inaccurate data being held on the new finance system.

Our approach

We will review the process controls implemented by the WAO for the change in accounting system and the method for data transfer.

We will also review the closing and opening trial balances on each of the systems and undertake tests on a sample basis, that balance sheet codes have been properly transferred.

We will also consult with an internal IT specialist on the proposed approach, to ensure that we undertake appropriate procedures in response the change in the WAO's accounting systems.

New accounting system

Response

Our review indicated that there were appropriate processes and controls over the implementation of the new accounting system.

We undertook detailed targeted testing which helped confirm that the transition of the data from the old accounting system had been properly undertaken.

3 AUDIT AND ACCOUNTING ISSUES IDENTIFIED DURING THE AUDIT

Ongoing claim

Issue

Our work identified the existence of an ongoing claim, where the final outcome remains uncertain.

Based on legal advice, management consider it more likely than not that the organisation will incur a financial loss as a result of this matter.

Resolution

Management have proposed a late adjustment to include an accrual for £50,000, being the estimated costs of resolving this matter.

Given the uncertainty as to how this matter will be resolved, it is difficult to accurately quantify the loss than the organisation may incur in respect of the matter.

However, based on available evidence, the estimate made does not appear unreasonable, but we shall be seeking a specific representation in respect of this matter.

Ongoing dispute with contractor firm

Issue

We are aware that one of the contractor firms used by the WAO continues to dispute the fee structure for the work it undertakes.

Therefore, management have made a provision of £89,000 in respect of additional amounts which will become payable should this firm succeed in claiming the additional amounts it believes are due to it.

Also, there continues to be issues with some of the work undertaken by this firm, and management have identified the risk that additional costs may need to be incurred to finalise the work they have undertaken in previous years.

Resolution

We agree that it is appropriate to include the £89,000 provision for amounts which may become payable to this firm, representing the excess of the amount already included in accruals, and the maximum potential exposure.

Management have included an adjustment to provide for £20,000 of additional costs which may be necessary to finalise the prior year work. We are satisfied that it appears appropriate to make such further provision, and that this estimate appears reasonable in light of the costs incurred to carry out the work in prior years.

4 REGULARITY ISSUES IDENTIFIED DURING THE AUDIT

Whistleblowing

Issue

Our work indicated that there had been appropriate response and follow up to any whistleblowing incidents reported in the year, and there appears to be appropriate procedures for staff to raise any issues of concern.

However, we did note that the whistleblowing policy dates from June 2017 and is therefore potentially in need of review and update in light of recent incidents.

Recommendation

Management should consider reviewing and updating their policy at the earliest opportunity.

Management comment

The Law & Ethics Team is now reviewing the internal whistleblowing policy in the light of recent experience and will present proposals to the board for updating the policy by September 2019.

5 UNADJUSTED/ADJUSTED MISSTATEMENTS

A summary of the unadjusted/adjusted errors identified during the course of our work is set out below, analysed between errors of fact and differences in judgement.

We have not disclosed below those items that we consider to be “clearly trivial” in the context of our audit. For this purpose, we consider “clearly trivial” to be any matter less than £5,000 individually and £10,000 in aggregate.

We advised management of all these misstatements on 17 May 2019 and requested management to correct them.

| | Profit (£'000) | Net assets (£'000) | |
|---|----------------|--------------------|---|
| Adjusted misstatements | Dr/(Cr) | Dr/(Cr) | |
| Turnover | 87 | - | To recognise the full provision for loss anticipated at the year end |
| Work in progress | - | (87) | |
| Deferred income | - | 111 | To reclassify refunds due on closed contracts |
| Other creditors | - | (111) | |
| Turnover | (75) | - | To recognise additional income agreed on Agri Funds contract |
| Work in progress | | 75 | |
| Accruals | - | (241) | To adjust for the treatment of work in progress in respect of third-party firms |
| Deferred income | - | (29) | |
| Work in progress | - | 143 | |
| Prepayments | - | 87 | |
| Turnover | 40 | - | |
| Prepayments | - | 177 | To amend treatment of invoices dated 31 March 2019 |
| Accruals | - | (177) | |
| Direct costs | 20 | - | To make additional provision for amounts complete certain contracts |
| Provisions | | (20) | |
| Employee termination costs | 50 | - | To provide for estimated loss in respect of ongoing claim |
| Accruals | - | (50) | |
| Total | 122 | (122) | |
| Unadjusted misstatements Factual | Dr/(Cr) | Dr/(Cr) | |
| Underlying total | - | - | |
| Unadjusted misstatements Judgemental | Dr/(Cr) | Dr/(Cr) | |
| Underlying total | - | - | |

6 SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL

We have set out below deficiencies in internal control which came to our attention during the course of our audit work. This does not constitute a comprehensive statement of all deficiencies that may exist in internal controls or of all improvements which may be made and has addressed only those matters which have come to our attention as a result of the audit procedures performed. An audit is not designed to identify all matters that may be relevant to you and accordingly the audit does not ordinarily identify all such matters.

Notification of fee changes

Fact and potential consequence Our review of a sample of contracts identified one incidence where the finance team had not been notified of an agreed fee increase on a specific contract.

This resulted in an understatement of revenues being reported in respect of this contract.

Possible action There should be improved processes to help ensure that the finance department is promptly notified of changes the agreed value of contracts.

Management response The finance team rely on fee information held within the audit management system which had not been updated by audit colleagues due to the timing of information being received. We will strengthen this process to ensure that any significant variances between time charges and fees are followed up immediately to ensure that this scenario cannot recur.

Timing of implementation and responsibility Immediate, responsibility Head of Finance.

Information held on personal lap tops

Fact and potential consequence The theft of lap tops and papers discussed previously was as least in part contrary to the organisation's information security policy, though we note that there is scope for clarification of that policy. Such situations risk personal or confidential data becoming compromised.

Possible action All staff and board members should be reminded of the organisation's policy, which should be clarified in respect of the use of personal lap tops, and there should be consideration to gaining a positive statement that all individuals are fully aware of the policy in this regard.

Management response We will review our policies in light of the theft so as to ensure expectations are clear and consistently applied for staff and Board members in terms of use of WAO information on personal devices. We will advise staff and board members of any changes and remind them of the requirement to comply with the policies through our annual declarations process.

Timing of implementation and responsibility Our IT and legal teams will amend our policies for approval by the board by 26 September 2019.

Register of interests

| | |
|--|---|
| Fact and potential consequence | <p>It is a requirement that all board members and members of the management committee complete annual declarations of outside interests that are publicly available of the WAO's website.</p> <p>Our work indicated that whilst updated declarations appear to have been obtained, these were not yet available on the website.</p> |
| Possible action | <p>Every effort should be made to obtain and publish the latest available declarations for all relevant individuals.</p> |
| Management response | <p>We obtained up-to-date declarations (in March 2019) for all relevant individuals, and we are now arranging for those to be posted on the website.</p> |
| Timing of implementation and responsibility | <p>The Board Secretary has collated declarations for Board members with a view to publishing them online on receipt of Welsh translation.</p> <p>Our Law & Ethics Team is collating declarations for all other relevant individuals with a view to ensuring publication in June 2019.</p> |

7 SIGNIFICANT FINDINGS FROM THE AUDIT

Accounting practices, including accounting policies

We have reviewed the accounting policies adopted by the WAO, and found that these are consistent with those adopted in previous years, remain appropriate and have been generally fully disclosed.

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. The results of a surveyor's report produced in the year for the Cardiff office has not identified any significant issues that would necessitate a material increase in the value of the reported provision.

Other provisions

Subject to comments made previously, this appears to be derived on an appropriate basis.

Financial statement disclosures

During the course of our audit, we reviewed the adequacy of the disclosures contained within the financial statements and their compliance with both relevant accounting standards and the requirements of the Companies Act 2006. The following disclosure matters were brought to your attention and subsequently reflected in the revised financial statements:

- expansion of the revenue recognition policy on adoption of IFRS 15

There were no matters of significance that were brought to your attention which have not been reflected in the revised financial statements.

Significant difficulties encountered during the audit

No significant difficulties were encountered during the course of our audit and we would like to take this opportunity thank the finance team for their assistance during the audit.

8 UNCERTAINTIES, RISKS, EXPOSURES, JUDGEMENTAL ISSUES AND GOING CONCERN

There are no further matters that we wish to bring to the attention of the committee.

Going concern

Given the ongoing funding received from the National Assembly for Wales, we are satisfied that we can agree with the Directors that there are appropriate grounds for concluding that the WAO remains a going concern.

9 FEES

We confirm that the fees charged during the year in respect of services performed for Wales Audit Office are consistent with those contained within our Audit Plan submitted to you and dated 27 February 2019.

10 INDEPENDENCE

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 dated 27 February 2019.

APPENDIX A - DRAFT LETTER OF REPRESENTATION

RSM UK Audit LLP
Third Floor
One London Square
Cross Lanes
Guildford
Surrey
GU1 1UN

Dear Sirs

Audit of Financial Statements – Year ended 31 March 2019

We confirm to the best of my knowledge and belief and having made appropriate enquiries of other senior executives of the Wales Audit Office, the following representations given to you in connection with your audit of the financial statements for the period ended 31 March 2019.

The following representations reflect circumstances up to the date of this letter, on which the financial statements were approved, and management's knowledge and intentions regarding the future of the Wales Audit Office.

Responsibility for financial statements

We acknowledge our responsibilities under the Public Audit (Wales) Act 2013 and Treasury Directions made in accordance with that Act for maintaining adequate accounting records and for preparing financial statements in accordance with the applicable accounting framework that give a true and fair view and for making accurate representations to you.

We confirm that we have taken all the steps we ought to have taken in order to make ourselves aware of any relevant audit information and to establish that it has been communicated to the auditors. We confirm that, as far as we are aware, there is no relevant audit information of which the auditors were unaware.

Availability of information

All the accounting records have been made available to you for the purpose of your audit and all transactions undertaken by the Wales Audit Office have been properly reflected and recorded in the accounting records. All other records and related information have been made available to you, including the minutes of all committee meetings, which are a complete and authentic record of the proceedings at those meetings. I have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud

Related party transactions

We have disclosed to you the identity of the related parties and all related party relationships and transactions of which I am aware. There were no transactions with the WCF and with the audited bodies other than those in the ordinary course of business (fees) requiring disclosure in the financial statements. There were no other transactions with related parties requiring disclosure during the year.

Use of funds and regularity

- We acknowledge our responsibility, as specified by the Public Accounts Committee of the National Assembly under the Public Audit (Wales) Act 2013, for ensuring that expenditure disbursed and income received is applied for the purposes intended by Parliament and the National Assembly for Wales and that the financial transactions conform to the authorities which govern them.
- To the best of our knowledge and belief we confirm that, in all material respects, the expenditure disbursed and income received during the year ended 31 March 2019 have been applied to purposes intended by Parliament and the National Assembly for Wales and the financial transactions conform to the authorities which govern them.
- Neither the board nor the senior management team have knowingly authorised a course of action, the financial impact of which was that transactions infringe the requirements of regularity.
- All transactions undertaken by the Wales Audit Office have been properly reflected and recorded in the accounting records.
- There were no events of which we are aware which involve suspected non-compliance with the framework of authorities which govern the running of the Office.

Assets

1. General

All assets included in the Statement of Financial Position belong to the Wales Audit Office and except as disclosed in the accounts were free from any charge. All non-current assets belonging to the Wales Audit Office are included.

2. Impairment of non-current assets

Each non-current asset is worth to the Wales Audit Office at least the amount at which it is included in the Statement of Financial Position, either through continued use by the Wales Audit Office or through the opportunity for sale on the open market.

Liabilities

1. General

All known liabilities of the Wales Audit Office at 31 March 2019 have been included in the balance sheet. All secured liabilities are disclosed.

2. Contingent liabilities

There were no contingent liabilities at the balance sheet date. All guarantees or warranties or other financial commitments have been fully disclosed in the financial statements. There were no known actual or possible litigation and claims whose effect should be considered when preparing the financial statements.

We confirm we have disclosed to you all banking and financing arrangements including related contracts and hedging products. We confirm that no tax avoidance schemes were used by the Wales Audit Office.

Accounting estimates

We confirm that all significant assumptions used in making accounting estimates, including where applicable those measured at fair value, are reasonable in the circumstances, and appropriately reflect our intentions and our ability to carry out the specific courses of action necessary to justify the accounting estimates and disclosures. The disclosures in the financial statements relating to accounting estimates are complete and appropriate.

We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

We further confirm to you that the estimated value of the dilapidations provisions are, to the best of our knowledge, an accurate assessment of the expected value to return the three properties back to their original state. We hereby confirm to you that the value of the dilapidations provisions in total is £622,000.

We confirm directly to you that the estimated amount which may become payable to a third party supplier for work performed to 31 March 2019 is £89,000. Furthermore, we consider that it is appropriate to make a further provision of £20,000 to reflect additional costs that will be incurred in finalising certain work undertaken by this supplier in prior years.

We are aware of an ongoing claim, where the resolution is uncertain. Given the uncertainties that have been identified, we consider it appropriate to include an accrual for £50,000 to reflect the estimated cost of resolving this claim.

Commitments

All commitments of the Wales Audit Office of a material amount, whether of a capital or revenue nature, have either been provided for or noted in the financial statements as appropriate. An adequate provision has been made for any losses, which may be expected to result there from, or from events which had occurred before 31 March 2019.

Remuneration report

All amounts paid to members of the Wales Audit Office Management committee have been appropriately included in the Remuneration Report.

All items of personal expenditure paid by the Wales Audit Office on the Management committee's behalf have either been reimbursed by the individuals concerned or have been treated as benefits in kind.

The benefits in kind in respect of the PAYE settlement will be met by the Wales Audit Office. This has been fully disclosed in the remuneration report.

No member of the Management committee or their connected persons had any indebtedness (or agreement concerning indebtedness) to the Wales Audit Office at 31 March 2019 or at any time during the year.

Governance Statement

We confirm the Governance Statement within the Annual Report fairly reflects the Wales Audit Office's current position in relation to our compliance with internal control requirements set out in HM Treasury's guidance.

Fraud and regulation

We acknowledge that the responsibility for the detection of fraud, error and non-compliance with laws and regulations rests with me. We confirm that we are not aware of any known or suspected frauds, error and non-compliance, involving

management, employees or third parties which may have a material effect on the financial statements. We confirm that, insofar as we are able to determine, in my opinion the financial statements are not materially misstated as a result of fraud.

In particular we confirm that the Wales Audit Office has made full disclosure of actual or suspected fraud brought to our attention by employees, former employees and other external parties.

We confirm that there has been no possible or actual instance of non-compliance with those laws and regulations which are central to the Wales Audit Office's ability to conduct its business, except as explained to you and as disclosed in the financial statements.

Events subsequent to the date of the Statement on Financial Position

There were no events, transactions or discoveries since the Statement of Financial Position date which:

- would have a material effect on the financial statements, or
- are of such importance to users of the financial statements that they should be disclosed in the financial statements.

Yours faithfully

Signed on behalf of the board of Wales Audit Office

Auditor General Wales & Accounting Officer

APPENDIX B - UPDATED FINANCIAL REPORTING DEVELOPMENTS

There are no additional matters from those reported within our Audit Plan.