

Report to: **Audit and Best Value Scrutiny Committee**

Date: **12 June 2007**

By: **Deputy Chief Executive and Director of Corporate Resources**

Title of report: **External Audit and Inspection Plans 2007/08**

Purpose of report: **To appraise the Committee of the External Audit and Inspection Plans**

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**RECOMMENDATION: The Committee is recommended to consider the External Audit and Inspection Plans for 2007/08.**

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## **1. Financial Appraisal**

1.1 The proposed audit and inspection fee for 2007/08 is £267,504. This comprises £191,420 for core audit and inspection services which represents an increase of 6.64% on last year and will be contained within the overall CRD budget. This includes a charge for Whole of Government Accounts (WGA) work of £3,000 for which there was no charge in previous years. The Audit Commission will also charge a one-off fee of £76,084 for the Corporate Assessment – there is no budget provision for this amount, but it is intended to contain this within the overall CRD budget. The Audit Commission (to 31 October 2007) and PKF (from 1 November 2007) will also charge fees of approximately £60,000 for the certification of grant claims which are paid directly by the department claiming the relevant grants. This is lower than in previous years due to the raising of the de minimis levels. Additional fees are charged for the National Fraud Initiative. The overall trend for fees nationally to increase ahead of the increase in grant settlements continues to be of concern and has been raised with the Audit Commission. However, at a local level the Council's risk based fee "discount" has remains at a similar level to last year at 23% (24% in 2006/07) which is close to the maximum allowed of 30% and reflects positively on the control environment, the work of internal audit and the quality of the final accounts.

## **2. Supporting Information**

2.1 Attached is the Audit and Inspection Plan for 2007/08 which has been drafted in consultation with officers and will be considered by Cabinet on 10 July. There has also been consultation with the Council's internal audit service to ensure that the plans of internal and external audit are complimentary and make best use of audit resources. This is the first plan prepared by the Council's new external auditors PKF and includes work to be carried out by both PKF and the Audit Commission, in their ongoing role as the Council's Relationship Manager during the year.

2.2 In summary, the proposed work for this year focuses on:

- The Corporate Assessment (AC);
- Relationship Management and Direction of Travel Assessment (AC)
- CPA Use of Resources Assessment 2007 (AC);
- Data Quality and BVPI / BVPP assessment (PKF);
- Audit of the Accounts and Core Financial Systems review (PKF);
- Certification of grant claims (AC/PKF).

The main risks identified by the external auditors are set out in Appendix A. There are no proposals for any voluntary improvement work within this years plan.

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Accountants &  
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# **East Sussex County Council**

## **Annual Audit and Inspection Plan**

May 2007

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### APPENDICES

- A Risk Planning Matrix**
- B Improvement Priorities**
- C Communication to Those Charged With Governance**

# 1 Executive summary

## Work scope

- 1.1 The scope of the audit is determined by the Audit Commission's "Code of Audit Practice", which covers two key areas – Accounts and "Use of Resources". The detailed Code audit approach is unchanged from 2006/07.

## Key audit risk areas

- 1.2 These are set out in more detail in Appendix A, and include:
- the need to make significant future cost savings over the next three years
  - new arrangements to deal with demand pressure within Adult Social Care including joint arrangements with Health
  - financial resource risks arising from waste disposal arrangements
  - significant changes in the Statement of Recommended Practice for 2007/08
  - the future development of the waste PFI scheme and possible future financial impact of LATS.

## Fees

- 1.3 Overall fees have shown an increase on the previous year, this being primarily a result of an inflationary increase and the Corporate Assessment. The discount from the mid point of the Audit Commission fee scales is 23%, which is the same as last year after adjustment for the WGA fee (see para 7.4).
- 1.4 The fee noted below for 2007/08 includes an amount in respect of work on the 2007 use of resources assessment which is being completed by the outgoing auditor in light of the impact on the 2006/07 opinion on the Statement of Accounts.

	2006/07	2007/08
Audit	165,000*	<b>175,000</b>
Inspection	14,500	<b>92,504</b>
<b>Total audit and inspection</b>	179,500	<b>262,504</b>

\* does not include whole of Government Accounts fee

## Key outputs

- 1.5 The key audit and inspection outputs for Members will be:

Output	Expected timing	Completed by
Audit and Inspection Plan	May 2007	PKF
Report on use of resources	December 2007	Audit Commission
Use of Resources assessment scores	December 2007	Audit Commission
ISA 260 Report on the 2007/08 Accounts	September 2008	PKF
Auditor's Opinion, covering: <ul style="list-style-type: none"> <li>• Statement of Accounts</li> <li>• Use of Resources conclusion</li> <li>• BVPP</li> </ul>	September 2008	PKF

Direction of Travel statement	[December 2008]	Audit Commission
Annual Audit and Inspection Letter	December 2008	Audit Commission

## 2 Introduction

- 2.1 This joint audit and inspection plan sets out the audit and inspection work proposed to be undertaken in 2007/08 by PKF and the Audit Commission.
- 2.2 This Plan has been drawn up from our risk based approach to audit planning and planning meetings held with you. It includes the Audit Commission's elements of the co-ordinated and proportionate audit and inspection programme.
- 2.3 As the accounts audit for 2006/07 has not yet been completed, the audit planning process for 2007/08, including the risk assessment, will continue as the year progresses, and the information and fees in this Plan will be kept under review and updated as necessary. Any significant changes to the Plan will be reported to the Audit and Best Value Scrutiny Committee.
- 2.4 The Relationship Manager will be responsible for overseeing the inspection work and liaison with other inspectorates.
- 2.5 Set out below are some key details related to the process supporting the preparation of this Audit Plan.

### Work of the Auditors - PKF

- 2.6 The work of the auditors that is covered by this Plan can be summarised as follows:
- review of the core financial systems used in preparing the accounts to 31 March 2008
  - review of the financial accounts prepared for the year ending 31 March 2008
  - review of the BVPP, and supporting BVPIs, as published in June 2007
  - work on use of resources issues for the period 1 April 2007 to 31 March 2008, including the scored judgements and data quality work.
- 2.7 Our principal objective as your appointed auditor is to carry out an audit that is tailored to focus on the specific financial and use of resources risks you face and meets the requirements of the Code.

### Inspection work – Audit Commission

- 2.8 This Plan also sets out the inspection work that is proposed in 2007/08, which links to your improvement priorities, as summarised under section 5 of this Plan and in Appendix B.
- 2.9 Discussions have been, and will continue to be, held between auditors and inspectors to ensure that the audit and inspection work in this Plan continues to be co-ordinated and targeted at your key areas for improvement.

### Assessing risks

- 2.10 We are committed to targeting our work where it will have the greatest effect based upon assessments of risk and performance. This means planning our audit work to address areas of risk relevant to our audit responsibilities and reflecting this in the audit fees. It also means making sure that our work is co-ordinated with the work of inspectors and other regulators and that our work helps you to improve.
- 2.11 Our risk assessment process starts with the identification of the significant financial and use of resources risks applying at the Council with reference to:
- our cumulative knowledge of the Council
  - planning guidance issued by the Audit Commission

- the specific results of previous and ongoing audit work
- discussions with Council officers
- liaison with internal audit
- the results of other review agencies' work where relevant.

2.12 For each of the significant risks identified in relation to our use of resources work, we consider the arrangements put in place by the Council to mitigate the risk and plan our work accordingly.

## 3 Accounts

3.1 The Code of Audit Practice requires us to provide an opinion on whether your Statement of Accounts “presents fairly” your financial position, and has been prepared properly, in accordance with relevant legislation and applicable accounting standards.

3.2 In carrying out this work we consider:

- the extent to which your accounting and internal control systems are a reliable basis from which to prepare the Accounts
- the robustness of your Accounts preparation processes.

3.3 We also undertake analytical procedures, test transactions and balances and consider the adequacy of the disclosures in your Accounts.

### Internal controls and key financial systems

3.4 International Standards on Auditing (UK and Ireland) require auditors to obtain a detailed understanding of an organisation, its environment, risk assessment processes, the information systems, internal controls, and monitoring activities. This must be sufficient to identify and assess the risks of material misstatement of the financial statements whether due to fraud or error and be sufficiently well documented to enable the auditor to design and perform further audit procedures based on identified risks.

3.5 This requires additional work to be undertaken to identify and understand the internal controls, evaluate the design of the control and determine whether it has been implemented. The evaluation of the design of a control involves considering whether it, individually or in combination with other controls, is capable of effectively preventing, or detecting and correcting, material misstatements.

3.6 Where the audit intends to rely on identified controls to reduce risk or the level of substantive testing otherwise required, the auditor must also undertake tests of the operating effectiveness of the relevant controls. The core financial systems upon which the Accounts are based will therefore require additional testing and review in order to arrive at our opinion on the Statement of Accounts.

### *Working with Internal Audit*

3.7 The Audit Commission expects that appointed auditors and Internal Audit departments have been working together to ensure that audit work is most effectively targeted in well-managed authorities, thereby minimising duplication and the overall level of audit resource input.

3.8 We have planned the 2007/08 audit on the basis that we will be able to place full reliance on the work of Internal Audit, and the relevant areas of this coverage are set out in our fee assumptions at paragraph 7.4. This assumption is based upon the preliminary discussions with both your current auditors in respect of arrangements for 2006/07, the Internal Audit service regarding proposed work for 2007/08 and our consideration of your Statement on Internal Control in your 2005/06 accounts.

### Fraud risk assessment

3.9 Under ISA240, we have a responsibility to consider specifically the potential risk of material misstatement of your Statement of Accounts as a result of fraud and error, including the risk of fraudulent financial reporting.

3.10 The primary responsibility for ensuring that your internal control frameworks are robust enough to prevent and detect fraud and corrupt practices lies with management and ‘those charged with governance’.



- 3.11 In order to identify the fraud risks, and the controls you have put in place on which we will seek to place reliance to mitigate those risks, we will:
- discuss your anti fraud and corruption arrangements with officers and 'those charged with governance'
  - consider the extent to which the work of Internal Audit is designed to detect material misstatements in the Accounts arising through fraud
  - make inquiries regarding instances of actual fraud you have identified
  - consider any material unusual or unexpected relationships that have been identified in performing analytical procedures.
- 3.12 For all residual fraud risks, and for any actual frauds that have been identified and we have been informed of, we will consider the possible impact on your Accounts and our audit programme.

### Accounts preparation

- 3.13 We will consider the adequacy of your arrangements for closing down the ledger and producing an accurate, timely and comprehensive Statement of Accounts and supporting working papers. We will, adequately in advance of the final audit, provide officers with a detailed list of schedules and working papers required for the audit.

### Statement on Internal Control

- 3.14 We will review your Statement on Internal Control to assess whether it has been presented in accordance with guidance, is adequately supported by an assurance framework, that an effectiveness review has been completed, and it is consistent, complete and not misleading based on our overall knowledge.

### Whole of Government Accounts (WGA)

- 3.15 As part of the WGA process we are required to review and report on the consolidation pack you have prepared for submission. The actual procedures to be performed have been developed by the Audit Commission in discussion with the National Audit Office and for Band 2 Authorities, of which you are one, focuses on ensuring consistency between the audited accounts and the consolidation pack, and the agreement of balances with other bodies.

### Key accounts risks

- 3.16 We have not included a detailed risk assessment for our audit of the Accounts as the specific risks may not become apparent until after completion of the 2006/07 audit. If necessary we will issue a separate update to this audit plan for issues in respect of the audit of the financial statements in November 2007. However, at this stage we are aware of the following risks that are likely to impact on our audit of the financial statements:
- compliance with the SORP 2007 including changing the Fixed Asset Restatement Reserve into a UK GAAP compliant Revaluation Reserve, new accounting treatment for Local Area Arrangements and accounting for Charities as group accounts
  - the business transformation programme in adult social care which includes updates to the AEGIS system
  - the use of the outsourcing partner Serco which includes some processing responsibilities may mean that the financial data derived are not subject to the same controls as ESCC systems and may therefore require additional audit review
  - the Age Well Adult Social Care Private Finance Initiative scheme which is likely to require review and agreement of the proposed accounting treatment.

- 3.17 In addition there are some emerging issues and other factors affecting the Accounts compilation process on which we intend to maintain an ongoing review during the course of the year. These are currently not significant issues, although they may become so as changes in circumstances arise. They include:

Issue	Potential risk
High Weald AONB.	We are awaiting on the Audit Commission's Audit Policy and Appointments Department assessment of whether this is a joint committee audit that requires a Full Code of Audit Practice Audit.
South Downs Joint Committee.	This Joint Committee currently requires a Full Code of Audit Practice Audit. This may require a full audit plan further to a regularity audit.
Single Status Pay	Equal pay under the Single Status Agreement should be implemented by the 31 March 2007 ensuring all current and backdated pay no longer contains inequalities based on sexual discrimination.
International Financial Reporting Standards (IFRS)	Following the Chancellor's budget, the current timetable for full IFRS implementation is the 2008/09 accounts. This may require the accounts for 2007/08 and 2006/07 to be restated to ensure IFRS compliance.

- 3.18 There are some other factors that will impact on the completion of work at the final accounts stage. These are not of significance for the Council, and have no direct fee impact, but are issues to be aware of in terms of their potential impact on audit timings. They include:

Issue	Potential risk
East Sussex Fire Authority (ESFA)	The Audit Commission are continuing as the External Auditors of ESFA. As ESFA use SAP as their financial ledger, therefore, the AC will need to place reliance on the SAP system. We may need to carry out further work to be able to provide the Audit Commission with the appropriate reliance.
Pension Fund	As the auditor for the East Sussex Pension Fund, we will have to perform sufficient work to provide assurance on pension disclosures to the auditors of the other admitted bodies in advance of their audit timetable.

## 4 Use of Resources

4.1 The Code requires us to:

- be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources (value for money conclusion)
- be satisfied that there are adequate arrangements in place for collecting, recording and publishing performance information
- audit your Best Value Performance Plan.

### Value for money conclusion

4.2 In reaching the value for money conclusion the Code requires auditors to have regard to a standard set of relevant criteria issued by the Audit Commission.

4.3 In meeting this responsibility we will review evidence that is relevant to the Council's corporate performance management and financial management arrangements. Where relevant work has been undertaken by other regulators we will normally place reliance on their reported results to inform our work.

4.4 We will also follow up our work from previous years to assess progress in implementing agreed recommendations.

### Use of Resources assessment

4.5 The Audit Commission has specified that auditors will complete a use of resources assessment for 2007/08. The assessment focuses on the importance of having sound and strategic financial management to ensure that resources are available to support the Council's priorities and improve services.

4.6 The work required to arrive at the use of resources assessment is fully aligned with that required to arrive at the auditor's value for money conclusion.

4.7 A score of 1 to 4 will be given, based on underlying key lines of enquiry, for each of the following themes:

Theme	Description
Financial reporting	Preparation of financial statements External reporting
Financial management	Medium-term financial strategy Budget monitoring Asset management
Financial standing	Managing spending within available resources
Internal control	Risk management System of internal control Probity and propriety
Value for money	Achieving value for money Managing and improving value for money

4.8 This assessment will focus on the progress made since the last assessment as well as changes to specific criteria. Due to a change in the timetable for completion of this work, and its direct relevance to the Value for Money conclusion that relates to the 2006/07 financial year, the outgoing auditors will perform and report this work.

4.9 There are a number of modifications to the individual criteria, with several of the non-bold criteria now becoming bold (and assuming "must have" status). These changes may have an

impact on the scores for each of the themes above, as well as on the overall assessment score for the Council.

- 4.10 Details of the scores and judgements will be reported to the Council. The scores will be accompanied, where appropriate, by recommendations as to what the Council needs to do to improve its services. The auditor's scores are reported to the Commission and are used as the basis for its overall use of resources judgement for the purposes of Comprehensive Performance Assessment (CPA).

### **Best Value Performance Information – Data Quality**

- 4.11 The Audit Commission has specified that auditors will be required to undertake audit work in relation to data quality. This is based on a three-stage approach covering:
- Stage 1 – review of overall management arrangements to secure data quality
  - Stage 2 – completeness check of reported performance information
  - Stage 3 – data quality spot check and in-depth review of specified performance indicators.
- 4.12 The work at stage 1 will link to our review of the Council's arrangements to secure data quality as required for our value for money conclusion and, together with the results of stage 2, will inform the risk assessment for the detailed spot check work to be undertaken at stage 3. It is expected that between 4 and 6 indicators will be subject to in-depth review at a County Council.

### **Best Value Performance Plans (BVPPs)**

- 4.13 We will consider and report on whether you have complied with statutory requirements in respect of the preparation and publication of your BVPP, including specified performance information and associated targets.

### **Key use of resources risks**

- 4.14 We have included in Appendix A our assessment of the risks relevant to our Use of Resources audit work and our planned response to those risks. The key risks are:
- the need to realise significant further savings in the light of likely future funding and Council Tax levels without impacting on policy development and service quality
  - obtaining best use of resources in adult social care in response to demand led pressure on services – including developing further joint arrangements with health bodies and transforming internal processes.
  - dealing with risks arising from the future development of the waste PFI Project and the potential financial impact of the Landfill Allowance Trading Scheme (LATS)
  - the new Age Well Private Finance Initiative scheme and the process by which the Council will ensure it is achieving value for money
  - arrangements for the use of resources and financial management control over East Sussex Local Area Agreement
  - ESCC have a Section 31 agreement with the new Primary Care Trusts (PCTs) and there is a need to ensure appropriate financial management and governance arrangements are in place over pooled budgets.

## 5 Audit Commission CPA and Inspection

- 5.1 The Audit Commission's CPA and inspection activity is underpinned by the principle of targeting our work where it will have the greatest effect, based upon assessments of risk and performance.
- 5.2 The Council's CPA category is therefore a key driver in the Commission's inspection planning process. For CPA 2006, the Council was categorised as 3 stars. A key element of CPA is the corporate assessment. All county councils and single tier authorities are required to have a corporate assessment once in the period 2005 to 2008, using the principles set out in the comprehensive assessment framework, *CPA – the Harder Test*. The Council will have a corporate assessment and joint area review – an inspection of services for children and young people – in June 2007. Other inspection activity consists of relationship management time and an annual direction of travel assessment.
- 5.3 The table at Appendix B summarises the agreed audit and inspection response to these priorities

## 6 Grant Claims

6.1 As agents of the Audit Commission we are required to express an opinion on certain grant claims submitted by the Council. There are de-minimis arrangements in place for the certification of claims, which are:

- amounts below £100,000 will not be certified
- amounts between £100,000 and £500,000 will be subjected to limited audit testing to agree form entries to underlying records, but the eligibility of expenditure will not be tested
- amounts above £500,000 will be audited in accordance with the outcome of a control environment risk assessment.

6.2 The outgoing Auditors, the Audit Commission, will undertake the audit of Grant Claims for the period ended 31 March 2007. They will audit all Grant Claims received by the 31<sup>st</sup> October 2007. From the 1<sup>st</sup> November 2007 any Grant Claims completed will be subject to audit by PKF.

6.3