Report to:	**Audit and Best Value Scrutiny Committee**
Date:	**4 March 2011**
By:	**Deputy Chief Executive and Director of Corporate Resources**
Title of report:	**External Audit Plan 2010/11**
Purpose of report:	**To inform the Committee of the content of the external audit plan for 2010/11**

RECOMMENDATION: The Committee is recommended to note and comment upon the External Audit Plan for 2010/11.

1. Financial Appraisal

1.1 The Plan confirms the core external audit fee as £206,350 charged by PKF. However this is reduced by two rebates received from the Audit Commission, the first for £13,783, relating to IFRS was known about at the time that the indicative fees were reported to this Committee, the second of £8,040 relates to the abolition of scored judgements for the Use of Resources assessment. There is also no charge from the Audit Commission for its inspection role following the abolition of the CAA. This gives a total net fee of £184,527 a reduction of c9% on the comparable fee for 2009/10. The Audit Commission is currently consulting on fee scales for 2011/12 but looks likely to set a spot fee of £185,715 for this Authority. In addition to these core fees, there are also charges for grant claim certification of c£17,000, charges for dealing with complaints or objections to the 2009/10 accounts expected to be c£7,000 and the National Fraud Initiative £1,875.

2. Supporting Information

2.1 The Plan sets out in more detail the work the external auditors will conduct in order to audit the Council's 2010/11 accounts. The Plan now reflects any relevant issues that have arisen as a result of the audit of the 2009/10 accounts and other work carried out by. The main risks identified by PKF are:

- Full implementation of International Financial Reporting Standards (IFRS);
- Significant financial pressures as a result of the local government grant settlement and service cost pressures;
- The correct accounting treatment for academy schools
- Revisions the Council's Controcc payments and contract management system;

2.2 A number of emerging risks are also identified for ongoing monitoring during the year (p6).

2.3 Officers will continue to liaise with PKF to ensure that their work is delivered as efficiently and effectively as possible, that changes to accounting requirements under IFRS are appropriately implemented and that internal and external audit plans are complementary and make best use of audit resources. The Plan will be reported to Cabinet for approval on 8 March..

SEAN NOLAN
Deputy Chief Executive and Director of Corporate Resources

Contact Officer Duncan Savage, 01273 482330

Local Member: All
BACKGROUND DOCUMENTS
None

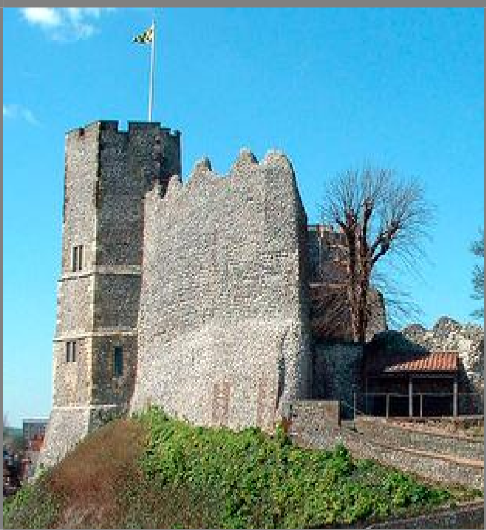
PKF

Accountants &
business advisers

East Sussex County Council

Audit Plan 2010/11

December 2010



Local Public Services

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Appendices

Code of Audit Practice and Statement of Responsibilities of Auditors and Audited Bodies

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission contains an explanation of the respective responsibilities of auditors and of the audited body. Reports and letters prepared by appointed auditors are addressed to members or officers. They are prepared for the sole use of the audited body and no responsibility is taken by auditors to any Member or officer in their individual capacity or to any third party.

Code of Audit Practice

Statement of Responsibilities

1 Executive summary

1.1 The purpose of this Audit Plan is to update our 2010/11 audit fee letter issued in March 2010 now that we have concluded our 2009/10 audit work.

Significant risks

1.2 Our audit is designed to respond to significant risks where we intend to focus additional audit effort in providing our opinion on the accounts and our value for money conclusion. These are summarised below and set out in detail in Appendix A:

Accounts

- the implementation of International Financial Reporting Standards (IFRS)

Value for money

- significant financial pressures as a result of the recession and service cost pressures, including the introduction of free personal care for older people and adults receiving community services; resulting in a £11.5 million savings requirement in 2010/11.

Fees

1.3 The audit fee for the year is £206,350, which remains the same as the fee proposed in our audit fee letter presented to the Audit and Best Value Scrutiny Committee in June 2010.

1.4 Our audit fee letter highlighted the scope of the use of resources assessment for the 2009/10 financial year (i.e the 31 March 2010 value for money conclusion) that is covered by this fee. Since that time, the new coalition Government has determined to abolish the Comprehensive Area Assessment and the scored use of resources assessment, with effect from the end of May 2010. As the majority of our work had been completed at the time of the announcement, there is no reduction in our 2010/11 audit fee as a result of this decision. However, as no scored assessment was delivered, the Audit Commission has decided to return some of the audit fees collected for the use of resources assessment. For county councils the rebate will be 3.5 per cent of the 2010/11 scale fees. This means that the Council is expected to receive a rebate in the region of £8,040 from the Audit Commission.

1.5 For the 2010/11 financial statements audit, the Audit Commission has given a 6 per cent rebate of audit fee to mitigate the increase in audit fee arising from the transition to IFRS. The rebate for the Council was £13,783.

1.6 The assumptions we have made in setting the audit fee are set out in section 4.

1.7 Grant fees for claims and returns for the year ended 31 March 2010 are in the process of being completed and the outturn fee, including our grants report which will be issued in January 2011, is expected to be £16,782. Based upon our experience of this most recent set of reviews of claims and returns, and additional requirements for auditing Employment Based Initial Teacher Training (EBITT) annual accounts, we anticipate fees for claims and returns for the year ended 31 March 2011 to be approximately £17,000, including a fee for the mandated grants report.

Key outputs

1.8 The key reports, opinions and conclusions from the audit will be:

Output	Expected timing
Accounts	
• Annual governance report • Audit opinion covering the financial statements • Opinion on the Whole of Government Accounts return	September 2011
Value for money	
• Annual governance report • Value for money conclusion	September 2011
Annual audit letter	November 2011
Grants	
Grants report	January 2012

2 Introduction

2.1 This Audit Plan sets out the audit work that we propose to undertake for the 2010/11 financial year. It has been drawn up from our risk based approach to audit planning and planning meetings held. The information and fees in this Plan will be kept under review and any significant changes will be reported to the Audit and Best Value Scrutiny Committee.

2.2 The context in which we deliver our audit is set out in Appendix B.

Assessing risks

2.3 We are committed to targeting work to 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 ensuring that our work is co-ordinated with the work of other regulators, and that our work helps you to improve.

2.4 Our risk assessment process focuses on the identification of significant financial and operational risks. For each of the significant risks identified, we consider the arrangements put in place to mitigate the risk and plan our work accordingly.

Clarity International Standards on Auditing

2.5 We would like to draw your attention to the fact that for the audit of financial statements for years ending on or after 15 December 2010 we are required to apply the clarified (or revised and redrafted) International Standards on Auditing (UK & Ireland) (ISAs). These have increased the number of requirements that have to be met when carrying out an audit and you are likely to notice a change in our approach to the audit of certain areas. Consequently we may require additional information from you or we may request information at a different stage of the audit process than has been the case in previous years.

Examples of areas where our approach to the audit may change as a result of the additional requirements of the clarified International Standards on Auditing include (but are not limited to):

- ***Materiality* –** we are required to set, not only a materiality level against which to evaluate the effect of identified misstatements on the audit but also a second level of materiality (known as "performance materiality") which is to be used when planning and performing the audit. This has to be set at a level lower than the materiality for the financial statements as a whole so as to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. The potential impact is that areas previously unaudited on the grounds of materiality may now fall within the scope of our audit work or more work may have to be done in certain areas to reflect the lower level of materiality on the extent of work.

- ***Related parties* –** whilst under the existing ISAs we were required to obtain an understanding of the related parties of the entity, including the controls that those charged with governance have in place over the identification and accounting for related parties, the clarified ISAs place a greater emphasis on a risk based approach to the consideration of this area. We use our understanding to assess the risk of material misstatement of the financial statements in respect of related parties and design further audit procedures accordingly. Our audit work on related parties will also include consideration of transactions that have occurred, if any, outside the normal course of business and in identifying any omitted related party relationships and transactions.

- ***Accounting estimates*** – we will consider all areas of the financial statements subject to accounting estimates and we are required to obtain a greater understanding about how those estimates have been determined and consider the effects of uncertainty in assumptions used. We will identify and assess the risks of material misstatement arising from the use of accounting estimates and will focus our work on areas where the risks of material misstatement are greatest. Our audit work on accounting estimates will also focus on identification of any possible instances of management bias.

Control environment

2.6 Under the existing ISAs we were required to report to those charged with governance any significant weaknesses in the control environment identified during the audit. The clarified ISAs place an increased emphasis on the need to communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis and, in addition, to report other deficiencies in internal control identified during the audit that are of sufficient importance to merit management's attention. As a result it may be necessary for us to produce additional reports to officers of weaknesses identified in the control arrangements at the Council, in addition to the reporting cycle to those charged with governance through the Audit and Best Value Scrutiny Committee.

3 Risk assessment

Significant financial statement audit risks

3.1 Our risk assessment has identified the following significant accounts audit risk that is likely to impact on our audit:

- Full implementation of International Financial Reporting Standards (IFRS) in local government from 2010/11 poses a risk that the Council may not appropriately apply IFRSs in the production of its financial statements, including restatement of prior year comparative figures. This could impact on the accuracy of a number of balances and income and expenditure totals and the completeness of disclosures within the financial statements.

3.2 In addition, International Standards on Auditing (UK and Ireland) presumes that a risk of management override of controls is present in all entities and requires us to respond to this risk by testing the appropriateness of accounting journals and other adjustments to the financial statements, reviewing accounting estimates for possible bias and obtaining an understanding of the business rationale of significant transactions that appear to be unusual. We are also required to consider the need to perform other additional procedures. It is considered that our standard audit procedures in reviewing journals and accounting estimates will be sufficient to cover this risk.

3.3 Following the introduction of the clarity international standards on auditing, we have re-assessed the triviality level applied to the audit of the Council and we have set a triviality level of £250,000 for the 2010/11 accounts audit. We will not report to you any matters arising below this level.

Updated value for money conclusion risk assessment

3.4 The following significant value for money risks were identified in our 2010/11 audit fee letter:

- There are significant financial pressures as a result of the recession and service cost pressures, including the introduction of free personal care for older people and adults receiving community services. The Council is required to achieve savings of £11.5 million in 2010/11 in order to deliver a balanced budget. There is a risk that the Council may not be able to achieve the required savings and efficiency improvements, which could impact on service delivery.
- The achievement of value for money in the Age Well Private Finance Initiative scheme,. However this risk is no longer present as the Council has decided to withdraw from the procurement process.

3.5 We have updated our value for money risk assessment for 2010/11 to also take into account:

- matters arising from the completion of the 2009/10 audit
- additional audit knowledge gained since our initial risk assessment which was included in our 2010/11 audit fee letter, presented to the Audit and Best Value Scrutiny Committee in June 2010
- the introduction of the Audit Commission's revised arrangements for the determination of the value for money conclusion (see Appendix B).

3.6 Our updated risk assessment has not identified any additional risks relating to our value for money conclusion.

Other issues

3.7 One of the Council's schools has become an academy school during 2010/11, meaning that it is therefore now funded by the Department for Education and is independent of local government control. The Council will need to determine the appropriate accounting treatment for the school's property, plant and equipment and ongoing capital expenditure, taking into account IFRIC 12 criteria for service concessions.

3.8 As a result of the Putting People First programme and the introduction of Self Directed Support and personal budgets for service users within Adult Social Care (ASC) from April 2010, the Council has updated its ASC direct payments system, ContrOCC, to manage the new requirements. We will review work done by Internal Audit in this area.

Emerging issues

3.9 There are some issues that we intend to maintain an ongoing review of during the course of the year. These are currently not significant issues, although they may become so as changes in circumstances arise. They include:

- significant reductions in the Council's grant settlement over the next few years as a result of the new coalition Government's Comprehensive Spending Review and consequent impact on the Council's medium term financial plans and 'Promise and Policy Steers'
- increased responsibilities with regard to the planning, commissioning and provision of NHS and adults' and children's social care services following the new Government's White Paper entitled *'Equity and Excellence: Liberating the NHS'* and the abolition of primary care trusts from April 2013
- impact on the Council's revenue support grant following the demise of South Downs Joint Committee and the formation of the South Downs National Park Authority from 1 April 2011
- transfer of the responsibility for concessionary fare travel from the East Sussex district and borough councils to East Sussex County Council from 1 April 2011; the Council will need to ensure that appropriate controls are established over the issue of concessionary bus passes and oversight of work carried out by MCL Transport Consultants Ltd.
- accounting treatment of two schools in Hastings that are due to become academies in 2011/12.

4 Fees and billing arrangements

Fees

4.1 As reported to you in our audit fee letter presented to the Audit and Best Value Scrutiny Committee in June 2010, the audit fee for the period April 2010 to March 2011 is **£206,350** plus VAT.

4.2 The fee is based on our understanding of audit requirements and risks at the time of drafting this Plan. If we need to make significant amendments to the audit fee during the course of the audit, we will first discuss this with the Director of Corporate Resources and then prepare a report outlining the reasons why the fee needs to change for discussion with the Audit and Best Value Scrutiny Committee.

Value for money conclusion work

4.3 When we presented our audit fee letter we highlighted the scope of the use of resources assessment for the 2009/10 financial year that is covered by this fee. Since that time the new Government has determined to abolish CAA and the scored use of resources assessment, with effect from the end of May 2010. As the majority of our work had been completed at the time of the announcement, there is no reduction in our 2010/11 audit fee as a result of this decision. However, as no scored assessment was delivered, the Audit Commission has decided to return some of the audit fees collected for the use of resources assessment. For county councils the rebate will be 3.5 per cent of the 2010/11 scale fees. This means that the Council is expected to receive a rebate in the region of £8,040 from the Audit Commission.

IFRS

4.4 For the 2010/11 financial statements audit, the Audit Commission has given a 6 per cent rebate of audit fee to mitigate the increase in audit fee arising from the transition to IFRS. The rebate for the Council was £13,783. The total returned to local government bodies, including fire and rescue authorities, was almost £5 million.

Grants certification

4.5 Audit fees for certification of grant claims and returns are based on the Audit Commission’s grade related rates as set out in the *Work Programme and Fee Scales* on the basis of hours incurred. Grant fees for claims and returns for the year ended 31 March 2010 are in the process of being completed and the estimated outturn fee is £16,872. The Audit Commission has mandated that, on an annual basis, an overall assessment of every authority’s grants control environment be carried out and a report issued to “those charged with governance” covering the grants work undertaken. The fee for this additional work, which was not included in the Fees and Work Programme document, is estimated at £1,000 and is included in the £16,872 estimate for our grants certification work for the year ended 31 March 2010.

4.6 Based upon our experience of this most recent set of reviews of claims and returns, we anticipate fees for claims and returns for the year ended 31 March 2011 to be approximately **£17,000**, including a fee for the mandated grants report.

Fee summary

4.7 The table below summarises proposed audit fees for the year, as well as the 2009/10 outturn fee compared to the planned fee:

	2009/10		2010/11	
Audit area	**Planned fee**	**Actual fee**	**Planned indicative fee**	**Planned revised fee**
Financial statements, including WGA	125,850	137,850	145,375	145,375
Use of Resources/VFM Conclusion	58,350	58,350	60,975	60,975
Total Code audit fee	**184,200**	**196,200**[1]	**206,350**[2]	**206,350**
Certification of claims and returns for the financial year ended 31 March 2011, including grants report	17,000	16,872	17,000	17,000

1 Agreed increase in fee regarding PFI schemes

2 Increase relates to the implementation of IFRS, inflation and some ongoing work on PFI schemes

4.8 As well as the audit fees identified above, the following fees are separately billable:

Work	2009/10 Actual	2010/11 Estimate	Billing arrangement
Questions and objections	6,728	TBA	Should any arise, time spent dealing with questions and objections will be billed separately. Where possible we will provide an estimate of the likely time required to respond to the matters before starting the work.

4.9 The fees detailed above are based on the following assumptions:

- Internal Audit will have completed its systems testing in accordance with the plans and agreed timetable, and to an adequate standard so that we are able to place full reliance on this work
- There are no significant changes to your main financial systems. Procedures or internal controls
- you will provide the information requested in our records required listing in accordance with agreed deadlines and that there will be no significant departures from the timetable
- you will ensure that audit reports are responded to promptly and the implementation of recommendations by the due date is actively monitored
- there are no major changes to the content of government department grant instructions.

4.10 The fee assumes efficient co-operation as set out above and is set at the minimum level to carry out the audit. We reserve the right to increase fees should the above assumptions not be met or where we encounter unexpected problems, or where issues arise, causing significant additional work. Time spent dealing with problems or issues arising is usually that of senior people and hence the cost will necessarily often be disproportionate to the original fee.

Billing arrangements

4.11 Your Code audit fee is being billed in 4 equal instalments of £51,587.50 from June 2010.

5 Audit arrangements

Timetable

5.1 The following outline timetable shows the expected dates planned for key fieldwork elements of the audit to commence:

Output	Timing	Reports
Accounts		
Review of internal controls	11 April 2011	September 2011
Audit opinion and annual governance report on the financial statements	4 July 2011	September 2011
Opinion on the Whole of Government Accounts return	4 July 2011	September 2011
Value for money		
Value for money conclusion	February 2011	September 2011
Annual reporting		
Annual audit letter	N/A	November 2011
Grants		
Grants report for claims and returns for the year ended 31 March 2011	July 2011	January 2012

5.2 We will agree specific dates for our visits with officers in advance of each part of our programme, and we will work closely with officers during the year to ensure that all key deadlines are met. We will also meet regularly with senior officers to discuss progress on the audit and obtain an update on relevant issues.

Communication

5.3 Auditing Standards require auditors to communicate relevant matters relating to the audit to “those charged with governance”. Relevant matters include issues on auditor independence, audit planning information and findings from the audit.

5.4 We have included in Appendix C to this Plan a statement to the Audit and Best Value Scrutiny Committee setting out the Audit Commission’s objectivity and independence guidelines and giving our confirmation that we have complied with those guidelines.

5.5 Following our audit of the financial statements we will report to the Audit and Best Value Scrutiny Committee on the findings from our audit.

Quality of service

5.6 We aim to provide a high quality of service to you at all times. If, for any reason or at any time, you would like to discuss how we might improve the service, or if you are in any way dissatisfied, please contact your engagement partner in the first instance. Alternatively you may wish to contact our Managing Partner, Martin Goodchild. Any complaint will be investigated carefully and promptly.

5.7 If you are not satisfied you may take up the matter with the Institute of Chartered Accountants in England and Wales (“ICAEW”).

5.8 In addition, the Audit Commission’s complaints handling procedure is detailed in their leaflet “How to complain: What to do if you want to complain about the Audit Commission or its appointed auditors”, which is available on their website http://www.audit – commission.gov.uk/complaints.

Appendix A: Risk assessment

Value for money

	Audit risk identified from planning	Relevant UoR KLOE	Audit response
Use of Resources			
1	*There are significant **financial pressures** as a result of the recession and service cost pressures, including the introduction of free personal care for older people and adults receiving community services. The Council is required to achieve savings of £11.5 million in 2010/11 in order to set a balanced budget. There is a risk that the Council may not be able to deliver the required savings and efficiency improvements may have an impact on the Council's service delivery.*	Financial resilience	*The Council's financial position will be regularly monitored during the course of our planning and audit work, and we will focus on the process and outcomes of the Council's plans for delivering efficiencies in our value for money conclusion work.*

Italics = reported in fee letter presented to the Audit and Best Value Scrutiny Committee on 2 June 2010

Accounts

	Audit risk identified from planning	Financial Statement Area & Assertion	Audit response
1	The introduction of IFRS as the financial reporting framework for local authorities, with a transition date of 1 April 2009, requires a review of material classes of transactions, balances and disclosures where the accounting treatment differs from that previously recognised under the UK GAAP based SORP. This requires restatement of the opening balances at 1 April 2009, restatement of the 2009/10 accounts and review of the correct accounting treatement of transactions in 2010/11. There is a risk that the Council may not appropriately apply IFRSs in the production of its financial statements, including restatement of prior year comparative figures, which could impact on the accuracy of a number of balances and income and expenditure totals and the completeness of disclosures within the financial statements. At this stage, the following areas have been identified as being likely to impact on the accounting treatment of material classes of transactions, balances and disclosures: • recognition of lease type arrangements not previously recognised as leases under IFRIC 12 (service concessions) and IFRIC 4 (lease arrangements) • assessment of operating leases and finance leases against relevant qualitative criteria and the separation of land and building elements of lease arrangements under IAS 17 (Leases) • review of valuation policies and component accounting for assets under IAS 16 (Property, plant and equipment) • review of the treatment of reversal of prior impairments of property, plant and equipment (which is clarified in IAS 16) • review of the treatment of impairments resulting from a clear consumption of economic benefits under IAS 36 (Impairments) • calculation of employee benefits under IAS 19 (Employee benefits) • revenue recognition policies for government grants and other contributions against the tests or deferral of income under IPSAS 23 • review of group accounting requirements under IFRS which focuses on ability to control as opposed to actual control • operating segment disclosures under IFRS 8 (Operating segments).	The risk impacts on a number of balances, income and expenditure totals and disclosures, including in particular: • Existence and completeness of property, plant and equipment and finance lease liabilities • Accuracy of depreciation charge for property, plant and equipment • Accuracy of impairment charges to expenditure and credits for reversal of prior impairments of property, plant and equipment; and existence of the revaluation reserve balance • Existence and completeness of annual leave liabilities and expenditure • Existence/occurrence and completeness of grant income and capital grants receipts in advance balances and donated asset reserve balance • Completeness of balances and transactions under group accounting • Accuracy and classification of operating segment disclosures • Presentation of the financial statements and disclosure requirements	We are planning to review the restatement of the 2009/10 accounts prior to the audit of the 2010/11 accounts. This review will identify any further issues with regards to the proper implementation of IFRS. Detailed testing will then be completed during the final accounts work on the 2010/11 accounts.

Appendix B: Our responsibilities

Accounts

The Code requires us to provide an opinion on whether your financial statements are "true and fair" and have been prepared properly, in accordance with relevant legislation and applicable accounting standards.

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
- consider the robustness of your accounts preparation processes
- undertake analytical procedures, test transactions and balances and consider the adequacy of the disclosures in your financial statements.

Financial statements

We will consider the adequacy of your arrangements for closing down the ledger and producing accurate, timely and comprehensive financial statements and supporting working papers. We will provide officers with a detailed list of schedules and working papers required for the audit.

We will review the appropriateness and consistency of application of the accounting policies adopted by the Council and ensure that these are consistent with the *Code of Practice on Local Authority Accounting in the United Kingdom 2010* (the Code).

We will report to you significant qualitative aspects of the accounting practices including the application of the Code or other significant matters relevant to the financial reporting process.

We will also report uncorrected misstatements and material uncertainties relating to going concern.

We will read the other information included in the financial statements and, if appropriate the annual report, to ensure this is consistent, complete and not misleading based on our overall knowledge. We will review your annual governance statement to assess whether it has been presented in accordance with relevant guidance, is adequately supported, that an effectiveness review has been completed, and it is consistent, complete and not misleading based on our overall knowledge.

We will report to you significant matters discussed, or subject to correspondence with management or other employees; and also any significant difficulties that we encountered during the course of the audit.

We will seek written representations from the Council or from other parties to acknowledge and understand the responsibilities for preparing the financial statements, for the internal controls necessary to enable to preparation of the financial statements that are free from material misstatement whether due to fraud or error, and that we have been provided with access to all information of which you are aware of that is relevant to the preparation of the financial statements.

Where we propose any modifications to the audit opinion or emphasis of matter paragraphs in the auditors' report, we will report this to you along with the reasons for the modifications.

Internal controls and significant financial systems

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.

Where the audit intends to rely on identified controls to reduce risk or the level of detailed testing the auditor must also undertake tests of the operating effectiveness of the relevant controls. The key financial systems upon which the accounts are based will therefore require additional testing and review in order to arrive at our opinion on the financial statements.

Your significant financial systems are:

- Main accounting
- Cash and bank
- Payments and creditors
- Income and debtors
- Payroll and employment costs
- Investments and investment income
- Fixed assets
- Carepay (Children's services)
- SPOCC (Supporting people)
- Trapeze (passenger transport)
- Abacus income (adult social care)
- Abacus payments / ContrOCC (adult social care)
- Information technology

We will report to management any deficiencies in internal control identified during the audit. Where we identify significant deficiencies in internal control identified during the audit we will also report those to those charged with governance.

Working with Internal Audit

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

Fraud risk assessment

We have a responsibility to consider specifically the potential risk of material misstatement of your financial statements as a result of fraud and error, including the risk of fraudulent financial reporting.

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" (the Audit Committee).

We will make appropriate enquiries and review the counter fraud arrangements in place 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.

For all 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.

Whole of government accounts (WGA)

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. Our work involves ensuring consistency between the audited accounts and the consolidation pack, and the agreement of balances with other bodies.

Value for money conclusion

The Code requires auditors to issue a conclusion on whether the audited body has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. This is known as the value for money (VFM) conclusion.

We will issue an overall conclusion on whether or not proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources (the "value for money (or VFM) conclusion"). The Commission has reviewed its approach to auditors' VFM work so that from 2010/11 auditors will give their statutory VFM conclusion based on the following two reporting criteria:

- The organisation has proper arrangements in place for securing financial resilience.
- The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

The focus of the criteria for 2010/11 are:

- The organisation has robust systems and processes to manage financial risks and opportunities effectively, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.
- The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

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

Local risk-based work

Local risk-based work is proposed to address audit risks relating to the accounts opinion or Value for Money Conclusion where normal levels of work are considered insufficient to fully address risk exposures. Specific pieces of work in respect of 2010/11 are set out in Appendix A.

Appendix C: Communication with those charged with governance

To: Audit and Best Value Scrutiny Committee and the Governance Committee, East Sussex County Council

Auditors appointed by the Audit Commission are subject to the *Code of Audit Practice* (the Code) which includes the requirement to comply with International Standards on Auditing (ISA) when auditing the financial statements. ISA (UK & Ireland) 260 – Communication with those charged with governance requires auditors to communicate to those charged with governance, at least annually, all relationships that may bear on the firm's independence and the objectivity of the audit engagement partner and audit staff.

The revised ISA does not define 'those charged with governance' as there are such a diverse range of arrangements across all types of entity. However it does state that "The auditor shall determine the appropriate person(s) within the entity's governance structure with whom to communicate." In the case of East Sussex County Council it has been agreed that the appropriate addressees of communications from the auditor to those charged with governance are the Audit and Best Value Scrutiny Committee and the Governance Committee.

Auditors are required by the Code to:

- carry out their work with independence and objectivity
- exercise their professional judgement and act independently of both the Commission and the audited body
- maintain an objective attitude at all times and not act in any way that might give rise to, or be perceived to give rise to, a conflict of interest
- resist any improper attempt to influence their judgement in the conduct of the audit.

In addition, the Code specifies that auditors, or any firm with which an auditor is associated, should not carry out work for an audited body, which does not relate directly to the discharge of the auditors' functions if it would impair the auditors' independence or might give rise to a reasonable perception that their independence could be impaired. If auditors are satisfied that performance of such additional work will not impair their independence as auditors, nor be reasonably perceived by members of the public to do so, and the value of the work in total in any financial year does not exceed a *de minimis* amount (currently the higher of £30,000 or 20% of the annual audit fee), then auditors (or, where relevant, their associated firms) may undertake such work at their own discretion. If the value of the work in total for an audited body in any financial year would exceed the *de minimis* amount, auditors must obtain approval from the Commission before agreeing to carry out the work.

The Code also states that the Commission issues guidance under its powers to appoint auditors and to determine their terms of appointment. The *Standing Guidance for Auditors* includes several references to arrangements designed to support and reinforce the requirements relating to independence, which auditors must comply with. These are as follows:

- any staff involved on Commission work who wish to engage in political activity should obtain prior approval from the Engagement Partner
- audit staff are expected not to accept appointments as lay school inspectors
- firms are expected not to risk damaging working relationships by bidding for work within an audited body's area in direct competition with the body's own staff without having discussed and agreed a local protocol with the body concerned
- auditors are expected to comply with the Commission's statements on firms not providing personal financial or tax advice to certain senior individuals at their audited bodies, auditors' conflicts of interest in relation to PFI procurement at audited bodies, and disposal of consultancy practices and auditors' independence

- auditors appointed by the Commission should not accept engagements which involve commenting on the performance of other Commission auditors on Commission work without first consulting the Commission
- auditors are expected to comply with the Commission's policy for both the Partner and the second in command (Manager) to be changed on each audit at least once every five years
- audit suppliers are required to obtain the Commission's written approval prior to changing any Audit Partner in respect of each audited body
- the Commission must be notified of any change of second in command within one month of making the change. Where a new Partner or second in command has not previously undertaken audits under the Audit Commission Act 1998 or has not previously worked for the audit supplier, the audit supplier is required to provide brief details of the individual's relevant qualifications, skills and experience.

Statement by the appointed auditor

In relation to the audit of the financial statements for East Sussex County Council for the financial year ending 31 March 2010, we are able to confirm that the Commission's requirements in relation to independence and objectivity, outlined above, have been complied with.

Under the requirements of ISA (UK & Ireland) 260 – Communication with those charged with governance, we are not aware of any relationships that may bear on the independence and objectivity of the audit engagement partner and audit staff which are required to be disclosed.