External Audit Report 2017/18

East Sussex County Council

—

13 July 2018

Content

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This report is addressed to East Sussex County Council (the Authority) and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. PSAA issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on PSAA's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Joanne Lees, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers (0207 694 8981, andrew.sayers@kpmg.co.uk). After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3H.

Important notice

This report is presented in accordance with our PSAA engagement. Circulation of this report is restricted. The content of this report is based solely on the procedures necessary for our audit. This report is addressed to East Sussex County Council (the Authority) and has been prepared for your use only. We accept no responsibility towards any member of staff acting on their own, or to any third parties. The National Audit Office (NAO) has issued a document entitled Code of Audit Practice (the Code). This summarises where the responsibilities of auditors begin and end and what is expected from the Authority. External auditors do not act as a substitute for the Authority's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

Basis of preparation: We have prepared this External Audit Report (Report) in accordance with our responsibilities under the National Audit Office Code of Audit Practice (the Code) and the terms of our Public Sector Audit Appointments Ltd (PSAA) engagement.

Purpose of this report: This Report is made to the Authority's Audit Committee in order to communicate matters as required by International Audit Standards (ISAs) (UK and Ireland) and other matters coming to our attention during our audit work that we consider might be of interest and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone (beyond that which we may have as auditors) for this Report or for the opinions we have formed in respect of this Report.

Limitations on work performed: This Report is separate from our audit opinion and does not provide an additional opinion on the Authority's financial statements nor does it add to or extend or alter our duties and responsibilities as auditors. We have not designed or performed procedures outside those required of us as auditors for the purpose of identifying or communicating any of the matters covered by this Report. The matters reported are based on the knowledge gained as a result of being your auditors. We have not verified the accuracy or completeness of any such information other than in connection with and to the extent required for the purposes of our audit.

Status of our audit: Our audit is still in progress, and we will provide an oral update on the status of our audit at the Audit Committee meeting. The following work is ongoing:

- Non pay expenditure testing
- Final sample and transactional testing
- Review of disclosures within the financial statements
- Whole of Government Accounts ("WGA")
- Final review and closedown procedures
- Receipt of the signed management representation letter

Summary

Financial statements audit – see section 2 for further details

Subject to all outstanding queries and procedures being satisfactorily resolved we intend to issue an unqualified audit opinion on the Authority's financial statements for the deadline of 31 July 2018, following the Audit Committee adopting them and receipt of the management representations letter.

We have completed our audit of the financial statements. We have read the Narrative Report and reviewed the Annual Governance Statement (AGS). Our key findings are:

- There are no adjusted or unadjusted audit differences.
- We agreed presentational changes to the accounts with the Finance Team, mainly related to compliance with the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2017/18.
- In addition to our routine requests we are asking for management representations over the following, which are explained in section 2:
  – The valuation of land and buildings as at 31 March 2018 is materially appropriate, and that the use of a contingency provision is appropriate for the needs of the Council's estate;
  – The Council is satisfied that the instructions issued to the valuer are complete and accurate to ensure a materially appropriate valuation;
  – That there have been no contractual variations in respect of the Council's PFI assets; and
  – That it is appropriate to continue to record 20 Voluntary Controlled ("VC") schools on the Council's balance sheet at 31 March 2018
- We will report that your Annual Governance Statement ("AGS") complies with delivering Good Governance guidance issued by CIPFA / SOLACE in April 2016.
- We reviewed the Narrative Report and have no matters to raise with you.
- We did not receive any queries or objections from local electors this year, though we continue to undertake work on the LOBO objection raised during 2016/17.

We are now in the completion stage of the audit. We intend to issue our 2017/18 Annual Audit Letter in August 2018. The audit cannot be formally concluded and an audit certificate issued as we are considering elector queries relating to 2016/17. Until we have completed our consideration of these, we are unable to certify that we have completed the audit of the accounts in accordance with the requirements of the Local Audit and Accountability Act 2014.

Value for money – see section 3 for further details

Based on the findings of our work, we have concluded that the Authority has adequate arrangements to secure economy, efficiency and effectiveness in its use of resources. We therefore anticipate issuing an unqualified value for money conclusion for the deadline of 31 July 2018.

Summary

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- Significant difficulties encountered during the audit;
- Significant matters arising from the audit that were discussed, or subject to correspondence with management;
- Other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and
- Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, public interest reporting, questions / objections, opening balances, etc.).

We have a duty to consider whether to issue a report in the public interest about something we believe the Authority should consider, or if the public should know about.

We have not identified any matters that would require us to issue a public interest report. In addition, we have not had to exercise any other audit powers under the Local Audit & Accountability Act 2014.

There are no other matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority's 2017/18 financial statements.

We have made one new recommendation as a result of our 2017/18 work, which relates to the the use of a contingency provision within the PPE valuation. Full details are given in appendix 1.

We undertake other grants and claims work for the Authority that does not fall under the PSAA arrangements. These grants are summarised below:

- Teacher's Pensions return 2017/18
- National College of Teaching and Leadership return 2017/18

The fees for this work is explained in section two.

Financial statements audit

We audit your financial statements by undertaking the following:

	Accounts production stage		
Work Performed	**Before**	**During**	**After**
1. Business understanding: review your operations	✓	✓	–
2. Controls: assess the control framework	✓	–	–
3. Prepared by Client Request (PBC): issue our prepared by client request	✓	–	–
4. Accounting standards: agree the impact of any new accounting standards	✓	✓	–
5. Accounts production: review the accounts production process	✓	✓	✓
6. Testing: test and confirm material or significant balances and disclosures	–	✓	✓
7. Representations and opinions: seek and provide representations before issuing our opinions	✓	✓	✓

We have completed the first six stages and report our key findings below:

1. Business understanding	In our 2017/18 audit plan we assessed your operations to identify significant issues that might have a financial statements consequence. We confirmed this risk assessment as part of our audit work. We provide an update on each of the risks identified later in this section.
2. Assessment of the control environment	We assessed the effectiveness of your key financial system controls that prevent and detect material fraud and error. We found that the financial controls on which we seek to place reliance are operating effectively. We have not made any recommendations regarding the Council's control environment during the year. We reviewed work undertaken by your internal auditors, in accordance with ISA 610 and used the findings to inform our work. We have chosen not to place reliance on their work due to the approach we adopted for the financial statements audit.
3. Prepared by client request (PBC)	We produced the PBC to summarise the working papers and evidence we ask you to collate as part of the preparation of the financial statements. We discussed and tailored our request with the Head of Finance and this was issued as a final document to the finance team. This resulted in audit working papers which were of appropriate quality for the purposes of the audit.

Financial statements audit

4. Accounting standards	We work with you to understand changes to accounting standards and other technical issues. For 2017/18 these changes related to: • The introduction of introduce key reporting principles for the Narrative Report; • Updates to section 3.4 (Presentation of Financial Statements) to clarify the reporting requirements for accounting policies and going concern reporting; and • Amendments to section 6.5 (Accounting and Reporting by Pension Funds) to require a new disclosure of investment management transaction costs and clarification on the approach to investment concentration disclosure.
5. Accounts Production	We received complete draft accounts by 31 May 2018 in accordance with the deadline. The accounting policies, accounting estimates and financial statement disclosures are in line with the requirements of the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18. This is the fourth year that the Authority has completed its accounts and audit process to an accelerated deadline, and we consider that the overall process for the preparation of your financial statements is adequate. We thank Finance for their cooperation throughout the visit which allowed the audit to progress and complete within the allocated timeframe.
6. Testing	We have summarised the findings from our testing of significant risks and areas of judgement in the financial statements on the following pages. We have identified presentational changes to the accounts which we have presented in appendix 2.
7. Representations	You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud. We provided a draft of this representation letter to the Chief Financial Officer on 3 July 2018. We draw attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us. We are asking Management to provide specific representations on: • The valuation of land and buildings as at 31 March 2018, and that the use of a contingency provision is appropriate for the needs of the Council's estate; • The Council is satisfied that the instructions issued to the valuer are complete and accurate to ensure a materially appropriate valuation; • That there have been no contractual variations in respect of the Council's PFI assets; and • That it is appropriate to continue to record 20 VC schools on the Council's balance sheet at 31 March 2018

Financial statements audit

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

— Significant difficulties encountered during the audit;

— Significant matters arising from the audit that were discussed, or subject to correspondence with Management;

— Other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and

— Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, opening balances, public interest reporting, questions/objections, etc.).

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority's 2017/18 financial statements.

To ensure that we provide a comprehensive summary of our work, we have over the next pages set out:

- The results of the procedures we performed over the valuation of land and buildings, and the pensions assets and liability, which were identified as significant risks within our audit plan and which will form a part of our audit opinion;
- The results of our procedures to review the required risks of the fraudulent risk of revenue recognition and management override of control; and
- Our view of the level of prudence applied to key balances in the financial statements.

Financial statements audit

Significant audit risks

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error in relation to the Authority.

SIGNIFICANT audit risk	Account balances affected	Summary of findings
Pension assets and liabilities	Net pensions liability: £409.8m	The net pension liability represents a material element of the Authority's balance sheet. The Authority is the administering authority of East Sussex County Council Pension Fund, which had its last triennial valuation completed as at 31 March 2016. This forms an integral basis of the valuation as at 31 March 2018. In our *External Audit Plan 2017/18*, we identified the pensions liability as a significant risk, and since then have also identified the pension assets as a significant risk. The valuation of the Local Government Pension Scheme relies on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which results in the Authority's overall valuation. There are financial assumptions and demographic assumptions used in the calculation of the Authority's valuation, such as the discount rate, inflation rates, mortality rates etc. The assumptions should also reflect the profile of the Authority's employees, and should be based on appropriate data. The basis of the assumptions is derived on a consistent basis year to year, or updated to reflect any changes. There is a risk that the assumptions and methodology used in the valuation of the Authority's pension obligation are not reasonable. This could have a material impact to net pension liability accounted for in the financial statements. • As part of our work we reviewed the controls that the Authority has in place over the information sent to the Scheme Actuary, including the Authority's process and controls with respect to the assumptions used in the valuation. We also evaluated the competency, objectivity and independence of the actuary, Hymans Robertson. • We reviewed the appropriateness of the key assumptions included within the valuation and involved a KPMG Actuary to provide a specialist assessment of those assumptions. We also reviewed the methodology applied in the valuation by Hymans Robertson. • In addition, we reviewed the overall Actuarial valuation and considered the disclosure implications in the financial statements. • In order to determine whether the net pension liability has been appropriately accounted for we also considered the valuation of pension assets. As part of our audit of the Pension Fund we gained assurance over the overall value of fund assets. We have no other matters to raise with you as a result of this work.

Financial statements audit

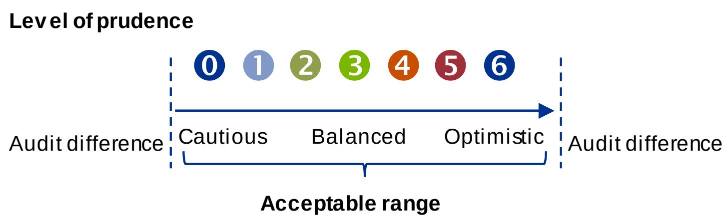
SIGNIFICANT audit risk	Account balances affected	Summary of findings
Valuation of land and buildings	Land and buildings: £373.5m	The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Authority has adopted a rolling revaluation model which sees all land and buildings revalued over a three year cycle. As a result of this, however, individual assets may not be revalued for two years. This creates a risk that the carrying value of those assets not revalued in year differs materially from the year end fair value. • We reviewed the revaluation basis and considered its appropriateness. We engaged KPMG's valuation experts to undertake an assessment of the valuation. • We reviewed the approach that the Authority adopted to assess the risk that assets not subject to valuation were materially misstated and considered the robustness of that approach. • In relation to those assets which have been revalued during the year we reviewed the accounting entries made to record the results of the revaluation in order to ensure that they were appropriate. • We reviewed the Council's impairment review undertaken against the impairment triggers set out in the CIPFA Code to satisfy there have been no significant impairments in 2017/18. • We considered the basis on which school assets were recorded on the Council's balance sheet • We also assessed the valuer's qualifications, objectivity and independence to carry out such valuations and reviewed the methodology used (including testing the underlying data and assumptions). During our review of the Council's land and buildings valuation, it was identified that the valuer Montagu Evans has included a contingency provision of 5% of each revalued specialised asset, of a total value of £13.6m. The use of a contingency provision is typically to act as a buffer against delays in the construction process of a new asset, which some valuers now consider to be inconsistent with the "instant build" methodology adopted by the CIPFA Code and the FReM. Current guidance issued by the Royal Institute of Chartered Surveyors (RICs) *UKGN 2 Depreciated replacement cost method of valuation for financial reporting* does not expressly prohibit the use of a contingency provision. However, we do note that there is currently a RICs consultation ongoing regarding this guidance note, and the consultation draft does state that a contingency provision should not be used where the instant build method is deployed. This is an area of judgement and it is not currently disallowed when using the instant build approach. However, we have raised a recommendation that the Council should consider the appropriateness of the inclusion of this provision going forward, in light of the new guidance due to be published.

Financial statements audit

Risks that ISAs require us to assess in all cases	Why	Our findings from the audit
Fraud risk from revenue recognition	Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. In our External Audit Plan 2017/18 we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.	In our External Audit Plan 2017/18 we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue. This is still the case. Since we have rebutted this presumed risk, there has been no impact on our audit work.
Fraud risk from management override of controls	Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we carry out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual. We have not identified any specific additional risks of management override relating to this audit.	There are no matters arising from this work that we need to bring to your attention.

Judgements in your financial statements

We consider the level of prudence in key judgements in your financial statements. We summarise our view below using the following scale:



Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Creditor Accruals	3	3	£43.7m	The Authority recorded creditor accruals of £43.7m for 2017/18. In most cases, the Authority will make significant judgements when calculating estimates for accruals, as information about actual amounts owed were not available at 31 March 2018. Accruals are based on estimates and judgements of historical trends and anticipated outcomes. At the end of each accounting period, Management reviews outstanding items and estimates the amounts to be accrued. Any variation between the estimate and the actual is recorded under the relevant heading in the accounts in the subsequent financial period. Our procedures focussed on considering the nature of accruals, selected on a sample basis, and whether the Authority has calculated the accrual using relevant supporting documentation and reasonable assumptions. In addition we have undertaken a retrospective review of accruals made in 2016/17 and agreed them to subsequent expenditure transactions in 2017/18, to support the accuracy of methodologies to accrue expenditure. All of the items tested could be agreed to appropriate supporting evidence, and based on this review we are satisfied that the estimates made in the accruals process are reasonable and balanced. We have no matters to raise with you in respect of this work.

Financial statements audit

Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Valuation of land and buildings	1	3	£373.5m	The Authority utilise an external valuer, Montagu Evans, to value their land and buildings. All land and buildings are measured initially at cost, representing the cost directly attributable to acquiring or constructing the asset and bringing it to the location and condition necessary for it to be capable of operating in the manner intended. All assets are subsequently measured at fair value, as part of a rolling revaluation programme which ensures that all assets are revalued within a 3 year period. Land and buildings are valued at fair value, determined as the amount that would be paid for the asset in its existing use (existing use – EUV). These methods are in line with the Code of Practice on Local Authority Accounting 2017/18 and the RICS Red Book. Our audit work has included a detailed consideration of the valuation basis used and review of the Montagu Evans valuation reports by KPMG's valuer. We have also considered the appropriate valuation basis of 20 VC schools which are recorded on the Council's balance sheet. On page 10, we have set out our findings in relation to the Council's inclusion of a contingency provision, as a key area of judgement. We consider inclusion of this provision to be optimistic within our acceptable range of prudence. We have raised a recommendation that management consider the appropriateness of the inclusion of this contingency provision in future years, in light of new guidance that is due to be published.
Net pension liability	3	3	£409.8m	The Authority continues to use Hymans Robertson to provide actuarial valuations in relation to the assets and liabilities recognised as a result of participation in the Local Government Pension Scheme. Due to the overall value of the pension assets and liabilities, small movements in the assumptions can have a significant impact on the overall valuation. We obtained the data provided to the actuary and sample tested the data back to the systems and reports from which it was derived to ensure the accuracy of this data. We also reviewed the information provided to actuaries for IAS 19 calculation and sample tested the data back to supporting evidence. We have no matters to raise with you in respect of this work.

Financial statements audit

Narrative report of the Authority

We have reviewed the Authority's narrative report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.

Queries from local electors

We did not receive any questions or objections from members of the public this year. However, as noted previously, we continue to respond to one objection raised during the 2016/17 audit.

Audit certificate

In order for us to issue an audit certificate, we are required to have completed all our responsibilities relating to the financial year. We are not in a position to issue our audit certificate with the audit opinion as:

— As previously noted we have an ongoing objection outstanding.

— HM Treasury has recently issued its guidance for completing the WGA and issued the consolidation packs that authorities need to complete. The audit deadline is 31 August 2018.

Whole of Government Accounts (WGA)

As above, the audit deadline is 31 August 2018. Work will take place on this in late July/August and we will report back to you if there are any significant issues arising.

Other grants and claims work

We undertake other grants and claims work for the Authority that does not fall under the PSAA arrangements. The status of our grants and claim work is presented below:

- Teacher's Pensions return 2017/18
- National College of Teaching and Leadership return 2017/18

Audit fees

Our fee for the audit was £83,572 excluding VAT (£83,572 excluding VAT in 2016/17). This fee was in line with that highlighted in our audit plan approved by the Audit Committee in March 2018. There is also an ongoing objection as noted above. Work is ongoing in relation to this and a fee will be agreed with management and the PSAA through the PSAA fee variation process.

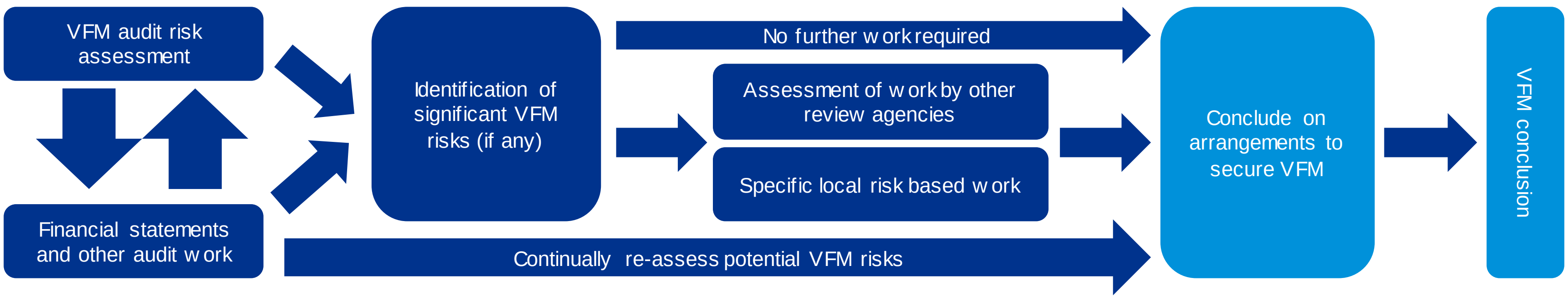
We will complete non-audit work at the Authority in year on two grant claim certifications totalling fees of £6k (2016/17: £6k), and have included in appendix 4 confirmation of the safeguards that have been put in place to preserve our independence.

Value for money

The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the authority 'has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources'.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to 'take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor's judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body's arrangements.'

We follow a risk based approach to target audit effort on the areas of greatest audit risk as summarised below:



We did not identify any significant VFM risks in 2017/18. We are satisfied that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2018, based upon the criteria of informed decision making, sustainable resource deployment and working with partners and third parties.

Recommendations raised and followed up

We detail below the one recommendation arising from our 2017/18 financial statements audit. We note there were no recommendations arising during our 2016/17 audit which required follow up.

Priority rating for recommendations					
1	Priority one: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	2	Priority two: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	3	Priority three: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

#	Risk	Recommendation	Management Response / Officer / Due Date
Financial statements			
1	2	**Use of a contingency provision within the land and buildings valuation** During our review of the Council's land and buildings valuation, it was identified that the valuer Montagu Evans has included a contingency provision of 5% of each revalued specialised asset, of a total value of £13.6m. Whilst current guidance on the subject does not expressly prohibit the use of a contingency provision for such assets, a number of valuers have moved away from using such provisions now as they are considered inconsistent with the instant build approach. Moreover, there is currently a RICs consultation ongoing regarding the guidance for specialised asset valuations, which states that a contingency provision should not be used where the instant build method is deployed. We recommend therefore that the Council review its need for a contingency provision in light of the new guidance as it is published, to ascertain if a contingency provision is appropriate and allowable in future years.	**Accepted** Pre the 2018/19 closure of account closure process, the Council (in consultation with our valuer) will review its need for a contingency provision as soon as the new Royal Institute of Chartered Surveyors (RICs) guidance is published. **Responsible officer** Ola Owolabi, Head of Pensions **Due date** 31 May 2019

Materiality and reporting of audit differences

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects:

- Material errors by **value** are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements;
- Errors which are material by **nature** may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff; and
- Errors that are material by **context** are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our External Audit Plan 2017/18, presented to you in March 2018. Materiality for the Authority's accounts was set at £9.9 million which equates to around 1% of gross expenditure.

We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any misstatements of lesser amounts to the extent that these are identified by our audit work. Under *ISA 260*, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. *ISA 260* defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. *ISA 450* requires us to request that uncorrected misstatements are corrected.

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £495k for the Authority.

Where management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit Committee to assist it in fulfilling its governance responsibilities.

Audit differences

Audit differences

Under UK auditing standards (ISA (UK&I) 260) we are required to provide the Audit Committee with a summary of unadjusted audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are 'clearly trivial', which are not reflected in the financial statements. In line with ISA (UK&I) 450 we request that you correct uncorrected misstatements. However, they will have no effect on the opinion in our auditor's report, individually or in aggregate. As communicated previously with the Audit Committee, details of all adjustments greater than £495K are shown below.

Unadjusted audit differences

We are pleased to report there are no unadjusted audit differences.

Adjusted audit differences

We are pleased to report there are no unadjusted audit differences.

Presentational adjustments

We identified presentational adjustments required to ensure that the Authority's financial statements for the year ending 31 March 2018 are fully compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2017-18 ('the Code').

#	Basis of audit difference
1	**Note 39 Related Parties:** our audit identified that this note under disclosed related party transactions between the Council and those bodies for whom Councillors have significant influence or control over. These have been amended in the revised financial statements.
2	**Note 44 Defined Benefit Pension Schemes:** our audit identified that the draft accounts disclosed £37m of employer pension contributions within the narrative of this note, however this should have been £34m. This has been updated in the revised financial statements.

Audit independence

ASSESSMENT OF OUR OBJECTIVITY AND INDEPENDENCE AS AUDITOR OF EAST SUSSEX COUNTY COUNCIL

Professional ethical standards require us to provide to you at the conclusion of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code of Audit Practice, the provisions of Public Sector Audit Appointments Limited's ('PSAA's') Terms of Appointment relating to independence, the requirements of the FRC Ethical Standard and the requirements of Auditor Guidance Note 1 - General Guidance Supporting Local Audit (AGN01) issued by the National Audit Office ('NAO') on behalf of the Comptroller and Auditor General.

This Statement is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses: general procedures to safeguard independence and objectivity; breaches of applicable ethical standards; independence and objectivity considerations relating to the provision of non-audit services; and independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners, Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through: instilling professional values; communications; internal accountability; risk management; and independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

Appendix 4

Audit independence

Independence and objectivity considerations relating to the provision of non-audit services

We have considered the fees charged by us to the authority for professional services provided by us during the reporting period. We have detailed the fees charged by us to the authority for significant professional services provided by us during the reporting period, as well as the amounts of any future services which have been contracted or where a written proposal has been submitted. Total fees charged by us for the period ended 31 March 2018 can be analysed as follows:

	2017-18 £	2016-17 £
Audit of the Authority	83,572	83,572
Total audit services	**83,572**	**83,572**
Allowable non-audit services	0	0
Audit related assurance services	6,000	6,000
Mandatory assurance services	0	0
Total Non Audit Services	**6,000**	**6,000**

We are required by AGN 01 to limit the proportion of fees charged for non-audit services (excluding mandatory assurance services) to 70% of the total fee for all audit work carried out in respect of the Authority under the Code of Audit Practice for the year. The ratio of non-audit fees to audit fees for the year was 1:14. We do not consider that the total of non-audit fees creates a self-interest threat since the absolute level of fees is not significant to our firm as a whole. We confirm that all non-audit services were approved by the Audit Committee. During 2017/18 we have also undertaken work on an objection received from an elector. This work is ongoing and the fee for this work will be agreed upon conclusion of the work.

Facts and matters related to the provision of non-audit services and the safeguards put in place that bear upon our independence and objectivity, are set out in the table below:

Description of scope of services	Principal threats to independence and Safeguards applied	Basis of fee	Value of services delivered in the year ended 31 March 2018 £	Value of services committed but not yet delivered £
Audit-related assurance services				
Grant Certification – Teachers Pensions Return and National College of Teaching and Leadership Return	The nature of these audit-related services is to provide independent assurance on each of these returns. As such we do not consider them to create any independence threats.	Fixed Fee	6,000	0

Appendix 4
Audit independence

Independence and objectivity considerations relating to other matters

There are no other matters that, in our professional judgment, bear on our independence which need to be disclosed to the Audit Committee.

Confirmation of audit independence

We confirm that as of the date of this report, in our professional judgment, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This report is intended solely for the information of the Audit Committee of the authority and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

KPMG LLP

13 July 2018

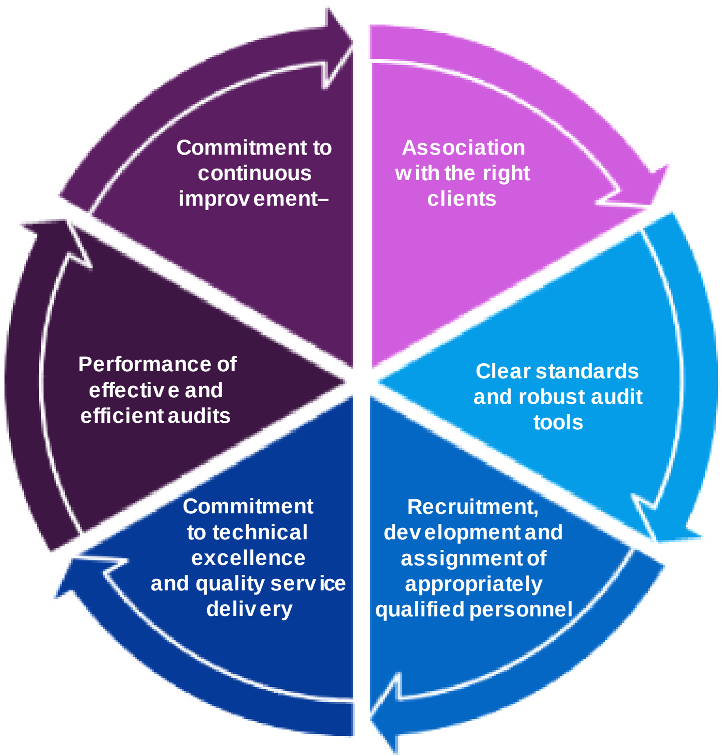
Appendix 5

Audit quality framework

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion. To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework

- Comprehensive effective monitoring processes
- Proactive identification of emerging risks and opportunities to improve quality and provide insights
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

- Select clients within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management



- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Relationships built on mutual respect
- Insightful, open and honest two way communications

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- Independence policies

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members and specialists

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