

Report to: **Cabinet**

Date: **5 July 2010**

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

Title of report: **External Audit and Inspection Fee Letters 2010/11**

Purpose of report: **To advise the Cabinet of the fees and high level work plans proposed by the Council's external auditors PKF and the Audit Commission.**

---

## **RECOMMENDATIONS**

**The Cabinet is recommended to approve the External Audit and Inspection Fee Letters for 2010/11.**

---

### **1. Financial Appraisal**

1.1 The proposed audit and inspection fee for 2010/11 is £210,860, a rise of 4.1% over the comparable fee for 2009/10 (£202,493) and this will be funded from within existing budgets. The fee consists of two main elements: the inspection fee of £18,293 charged by the Audit Commission (no change from 2009/10); and the audit fee of £192,567 charged by PKF (an increase of 4.5% on 2009/10 fee of £184,200). The external audit fee already takes into account the £13,783 rebate agreed by the Audit Commission in relation to planned work on IFRS implementation. The risk discount included in the audit fee now stands at 11% below the scale fee. This reflects a significant reduction in the risk discount over the last two years from 22% (2008/09) and 17% (2010/11). It is the case that the Audit Commission has reduced the maximum level of risk discount available within the fee structure from 30% to 20% this year (and further to 10% in 2012/13), a move which the Council vigorously opposed in its response to the Commission's fee consultation. Our external auditors have noted in their fee letter that with the exception of IFRS they have assumed that there has been no change to the general level of risk for the Council and have not given a specific reason for the further reduction in the risk discount. PKF have, however, agreed to review the extent of internal audit work which they require in order to support their opinion on the accounts to see if compensating reductions can be identified.

1.2 In addition to the audit and inspection fee there will be additional charges for: verifying correct accounting treatment for PFI schemes under IFIC 12 (this forms an addition to the 2009/10 audit fee but will be charged in 2010/11 when the work is carried out); grant claim certification (£17,000); and the National Fraud Initiative 2010 (c£1,875). PKF will also make additional charges for dealing with complaints or objections to the accounts and this will include final fees for work on complaints regarding the Waste PFI contract. Fees for complaints and objections work have totalled £52,009.90 over the last two financial years.

### **2. Supporting Information**

2.1 There is no longer a single audit and inspection plan reflecting the work of the Audit Commission and the Council's external auditors PKF. Instead there are separate fee notes produced at the beginning of the financial year (copies attached as Appendices A and B) and a more detailed external audit plan which will be produced in December 2010 and will reflect any risks and issues arising from the audit of the 2009/10 accounts. The fee letters were considered by Audit and Best Value Scrutiny Committee on 2 June.

2.2 Since the fee letters were received the Government and the Audit Commission have announced the ending of the Comprehensive Area Assessment (CAA) regime, with immediate effect. It is not yet clear what may be put in its place or what changes the Commission will make to its fee scales as a result. Whilst officers will press for appropriate reductions in fees, it is

possible that there will be limited impact in 2010/11 as PKF have already carried out the majority of their work on the use of resources assessment as indicative scores had to be submitted by 21 April 2010. Further reports will be made to Cabinet and ABVSC once the situation becomes clearer and if fee letters are reissued.

2.3 Officers will continue to liaise with both the Commission and PKF to ensure that their work is delivered as efficiently and effectively as possible and that internal and external audit plans are complementary and make best use of audit resources.

2.4 External audit arrangements for the Pension Fund are now dealt with separately and will be reported to the Governance Committee in due course.

BECKY SHAW – Chief Executive

SEAN NOLAN - Deputy Chief Executive and Director of Corporate Resources

Contact Officers Duncan Savage, 01273 482330

Jane Mackney, 01273 482146

**Our ref: SP/NC**

April 2010

Ms Becky Shaw  
 Chief Executive  
 East Sussex County Council  
 County Hall  
 St Anne's Crescent  
 Lewes  
 East Sussex  
 BN7 1UE

Dear Becky

**Annual inspection fee 2010/11**

I am writing to confirm the assessment and inspection work that we propose to undertake for the 2010/11 financial year at East Sussex County Council. The inspection fee:

- is based on the risk-based approach to inspection planning as set out in the Comprehensive Area Assessment (CAA) framework and associated guidance; and
- reflects only the Audit Commission's inspection work, excluding any audit fees. Your appointed auditor, PkF, will be writing to you separately on fees for audit work.

CAA will deliver a more proportionate and risk based approach to inspection, targeting only high risk services and outcomes for inspection where alternative improvement activity is not appropriate. The inspection plan will be reviewed and updated as necessary.

The total indicative fee for inspection for 2010/11 is £18,293 and is shown in the table below. The inspection fee has been set in accordance with the Audit Commission's work programme and scales of fees 2010/11. No Audit Commission inspection is currently proposed.

**Assessment and inspection work plan and fee**

Assessment / inspection activity	Planned fee for 20010/11
Area assessment - local partnership	n/a (CLG grant funded)
Managing performance theme of organisational assessment	18 293

<b>Total inspection fee</b>	£18,293
-----------------------------	---------

If I need to make any significant amendments to the inspection plan and fee during the course of the year, I will first discuss this with you and then confirm in writing outlining the reasons for the change, including the proposed scope for the work.

The above fee excludes any work you requested and the Commission has agreed to undertake using its advice and assistance powers.

If you have any questions regarding this letter, please contact me in the first instance. Alternatively you may wish to contact the Neil Childs, Head of Operations.

Yours sincerely

Sandra Prail  
Comprehensive Area Assessment Lead

cc Director of Corporate Resources

Sean Nolan  
East Sussex County Council  
County Hall  
St Anne's Crescent  
Lewes  
East Sussex  
BN7 1UE

Our ref: 4008879/RB/JC

[Date]

Dear Sean

## **Annual Audit Fee 2010/11 and Update to 2009/10 Fee**

### **2009/10 fee update**

The planned Code audit fee for 2009/10 was £184,200. This fee was quoted in July 2009 before it was confirmed that IFRIC 12 would be introduced by the 2009 Statement of Recommended Accounting Practice (SORP) for the 2009/10 financial statements. IFRIC 12 applies International Financial Reporting Standards (IFRS) rules on Private Finance Initiative (PFI) schemes. The Audit Commission's fee guidance for 2010/11 states that "The proposed scales of fees do not include provision for review of the accounting treatment of PFI schemes. The scope, and therefore the costs, of such reviews will depend upon the nature and complexity of the scheme and may need to be reflected in a variation to the scale fee".

We are proposing an additional fee currently estimated at £7,000 in respect of audit work to be carried out in verifying that the waste and schools PFI schemes have been appropriately accounted for in accordance with IFRIC 12. The planned Code fee for 2009/10 has therefore increased to £191,200.

There is a further change to the fees that we reported in our 2009/10 Annual Audit Plan in respect of fees charged for the certification of grant claims and returns. The fee has decreased from the estimated £18,500 to £16,980. The final fee includes £15,480 for the certification of individual claims and returns and £1,500 for the grants report.

### **2010/11 indicative fee**

Further to our discussions with officers at the Council, we are writing to confirm the audit work that we propose to undertake for the 2010/11 financial year at East Sussex County Council. The fee:

- is based on the risk-based approach to audit planning as set out in the Code of Audit Practice and work mandated by the Audit Commission for 2010/11
- reflects only the audit element of our work, and specifically excludes any inspection and assessment fees. Your Comprehensive Area Assessment Lead will be writing to you separately on these fees on behalf of the other inspectorates.

As we have not yet completed our audit for 2009/10, the audit planning process for 2010/11, including the risk assessment, will continue as the year progresses and fees will be reviewed and updated as necessary.

The total indicative fee for the Code audit for 2010/11 is £206,350.

The Audit Commission has published its work programme and scales of fees 2010/11. The scale fee for East Sussex County Council is £231,830 and the Audit Commission has indicated that the scale fee represents the Audit Commission's estimate of the fee required to complete an audit where the audited body has no significant audit risks and where there is a sound control environment. This is a change in emphasis from the Audit Commission, indicating that the expected fee is the scale fee. In exceptional circumstances, for 2010/11 a fee in the range of 25 per cent upwards and 20 per cent downwards may be acceptable. This is in a range of £289,787 and £185,464 in the case of East Sussex County Council. The total Code fee proposed for 2010/11 is 11 per cent below the scale fee.

The audit fee quoted above for 2010/11 includes a charge for the introduction of IFRS. The transition will result in an increased level of work for auditors, particularly in the first year when both the outturn figures and the restated comparatives will need to be audited. However, the Audit Commission will subsidise the Council for this increased cost by refunding the Council £13,783.

The proposed net fee to the Council for 2010/11, after deducting the IFRS subsidy, is £192,567.

A summary of the proposed 2010/11, and comparison to the 2009/10 fee, is shown in the table below:

<b>Audit area</b>	<b>Planned fee 2010/11</b>	<b>Revised fee 2009/10</b>	<b>Original planned fee 2009/10</b>
Financial statements, including WGA	145,375	132,850	125,850
Use of Resources/VFM Conclusion including risk based work	60,975	58,350	58,350
<b>Total Code audit fee</b>	<b>206,350</b>	<b>191,200</b>	<b>184,200</b>
Less: IFRS subsidy	(13,783)	-	-
<b>Code audit fee less subsidy</b>	<b>192,567</b>	<b>191,200</b>	<b>184,200</b>
<b>Certification of claims and returns*</b>	17,000	16,980	18,500

\* Planned fee for 2010/11 relates to the certification of grant claims and returns for the year ended 31 March 2010. The certification fee for 2009/10 is the actual fees for the year ended 31 March 2009.

Your audit fee for 2010/11 will be billed in 4 equal instalments of £51,587.50 from June 2010.

With the exception of the introduction of IFRS, in setting the fee at this level, we have assumed that the general level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2009/10. We have also assumed that the resource input for Use of Resources assessments will be at the same level as for 2009/10, though we will be looking in more detail at the Council's financial position in light of the level of efficiencies required to be delivered.

The above fee excludes improvement work we may agree to undertake. Each piece of work would be separately negotiated and a detailed project specification agreed with you.

Tel 020 7065 0000 | Fax 020 7065 0650

Email richard.bint@uk.pkf.com | www.pkf.co.uk

PKF (UK) LLP | Farringdon Place | 20 Farringdon Road | London | EC1M 3AP | DX 479 London/Chancery Lane

PKF (UK) LLP is a limited liability partnership registered in England and Wales with registered number OC310487.

A list of members' names is open to inspection at Farringdon Place, 20 Farringdon Road, London EC1M 3AP, the principal place of business and registered office. PKF (UK) LLP is authorised and regulated by the Financial Services Authority for investment business activities. PKF (UK) LLP is a member firm of the PKF International Limited network of legally independent firms and does not accept any responsibility or liability for the actions or inactions on the part of any other individual member firm or firms.

A separate plan for the audit of the financial statements will be issued in December 2010. This will detail the significant risks identified, planned audit procedures to respond to those risks and any changes in fee. If we need to make any significant amendments to the audit fee during the course of the audit, we will first discuss this with you and then prepare a report outlining the reasons why the fee needs to change for discussion with the Audit and Best Value Scrutiny Committee.

### Use of resources work

We will carry out use of resources work as set out in the Audit Commission's work programme and scales of fees 2010/11. This includes work on the use of resources assessment currently being carried out.

Our use of resources assessment is based upon the evidence from three themes:

- Managing finances
- Governing the business
- Managing resources.

The key lines of enquiry specified for the assessment are set out in the Audit Commission's work programme and scales of fees 2010/11. Our work on use of resources informs our 2009/10 value for money conclusion. We have identified additionally two specific risks in relation to our value for money conclusion for 2010/11. For each risk, we will consider the arrangements put in place by the Council to mitigate the potential risk, and plan our work accordingly. Our initial assessment of indicative key risks in relation to value for money audit work is shown in the table below:

Indicative key risk	Planned work	Timing of work
<p>There are significant <b>financial pressures</b> 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.</p>	<p>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 Use of Resources assessment.</p>	<p>March 2010 – March 2011</p>
<p>The <b>Age well PFI scheme</b> is part of the Adult Social Care service plan and represents a significant investment in the service. There is a risk that the Council may not be able to demonstrate that value for money is obtained by the scheme.</p>	<p>As part of our Use of Resources assessment we will continue to review the procurement process for the PFI scheme through analysis of supporting documentation.</p>	<p>April 2010 – March 2011</p>

In addition to the significant risks identified above, our risk assessment has also identified an accounts risk which is detailed in the table below. Although we would not ordinarily identify accounts risks at this stage, the significance of the transition to IFRS is fundamental to our audit of the 2010/11 financial statements. Accordingly we feel it appropriate to bring this to your attention at this stage:

Indicative key risk	Planned work	Timing of work
<p><b>IFRS</b> will be adopted in local government from 2010/11 and will also require restatement of prior year comparative figures. There is a risk around transitional arrangements and preparation of the financial statements in compliance with IFRS. Failure to appropriately apply IFRS may impact on the accuracy of a number of balances, income and expenditure totals and disclosures within the financial statements.</p>	<p>We will monitor the Council's progress against implementation of their IFRS plan and management's transition arrangements, with particular audit emphasis on the following:</p> <ul style="list-style-type: none"> <li>• Review of service arrangements against IFRIC 12 (service concessions)</li> <li>• Review of arrangements against IFRIC 4 (lease arrangements)</li> <li>• Consideration of leasing arrangements against IAS 17 (Leases)</li> <li>• Review of valuation policies and component accounting for assets under IAS 16 (Property, plant and equipment)</li> <li>• Calculation of employee benefits under IAS 19 (Employee benefits)</li> <li>• Review of government grants in light of CiPFA's decision to apply IPSAS 23</li> <li>• Review of group accounting requirements under IFRS which focuses on ability to control as opposed to actual control.</li> </ul> <p>Additional detailed audit procedures will also be required in the restatement exercise of comparative balances for year ended 31 March 2009 and 31 March 2010.</p>	<p>April 2010 – September 2011</p>

There are a few matters which do not constitute use of resources risks but that we intend to maintain an ongoing review of during the course of the year:

- The movement to personal budgets for service users within Adult Social Care from April 2010, under the Putting People First programme, as the Council will need to ensure that appropriate financial controls are retained.
- The transfer to the Council of responsibility for concessionary travel from April 2011, as 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.
- The potential impact on the Council's services of the establishment of the South Downs National Park from April 2011.
- There is reasonable visibility of Government funding for 2010/11 but less so thereafter, and this could impact severely on the Council's financial standing from 2011/12.

We will issue a number of reports relating to our work over the course of the audit. These are listed in the appendix to this letter.

The key members of the audit team for the 2010/11 are:

- Engagement lead      R. Bint                      0207 065 0497
- Audit Manager         J. Combrinck                0207 065 0440
- Audit Supervisor      Emma Liddell                020 7065 0755

We are committed to providing you with a high quality service. If you are in any way dissatisfied, or would like to discuss how we can improve our service, please contact Richard Bint in the first instance. Alternatively, you may wish to contact our Managing Partner, Martin Goodchild. Any complaint will be investigated carefully and promptly. If you are not satisfied you may take up the matter with the Institute of Chartered Accountants in England and Wales (“ICAEW”).

Yours sincerely

**Richard Bint**  
Partner  
PKF (UK) LLP

cc Assistant Director – Audit and Performance

cc Chair of the Audit and Best Value Scrutiny Committee

## Appendix: Planned Outputs

Our reports will be discussed and agreed with the appropriate officers before being issued to the Audit and Best Value Scrutiny Committee.

<b>Planned output</b>	<b>Indicative date</b>
Audit plan	December 2010
Annual governance report	September 2011
Use of resources assessment report	October 2011
Annual audit letter	November 2011
Report on certification of grants claims	January 2011