

## **AUDIT COMMITTEE**

**21 MARCH 2013**

### **EXTERNAL AUDIT ANNUAL AUDIT PLAN 2012/2013**

Report Author: Mick Hayward, Chief Finance Officer

#### **Summary**

This report and attachment sets out the Annual Audit Plan. The Council's external auditors (PKF) have produced the plan and it is reported to the Audit Committee to comply with governance requirements.

#### **1. Budget and Policy Framework**

- 1.1 International Standards on Auditing require the audit plan to be communicated to 'those charged with governance'.
- 1.2 The terms of reference of the Audit Committee include: discussions with the external auditor on new accounting standards, changes to the reporting framework and the basis of the annual audit, including the content of performance work. This is therefore a matter for this Committee.

#### **2. Background**

- 2.1 In accordance with the International Standards on Auditing (UK and Ireland) 260, it is necessary to communicate the Annual Audit Plan for 2012/2013.
- 2.2 As the external auditor, independently appointed by the Audit Commission, PKF has a responsibility to audit and provide an opinion on the Statement of Accounts and to provide a conclusion on the use of resources.
- 2.3 The Annual Audit Plan for 2012/2013, produced by PKF, is attached as Appendix 1 to this report.

#### **3. Scope of the Plan**

- 3.1 The overall scope of the work to be carried out is determined by the Audit Commission's Code of Audit Practice for Local Government (March 2010), which describes how auditors carry out their functions as set out in the Audit Commission Act 1998. This requires PKF to review and report on the Council's:
  - financial statements
  - arrangements for securing economy, efficiency and effectiveness in the use of resources.

3.2 PKF have drawn up the detailed plan in accordance with their risk based approach to audit planning and planning meetings held. PKF will target work where it will have the greatest effect based upon assessments of risk and performance.

#### **4 Financial and Legal Implications**

4.1 Audit fees are calculated in accordance with national scales established by the Audit Commission. The proposed audit fee for PKF's code audit work the year is £207,460 plus VAT, which is £19,000 above the scale fee published by the Audit Commission. The proposed fee for the certification of claims and returns is £23,950 plus VAT, which is the composite scale fee published by the Audit Commission.

4.2 The International Standards on Auditing require the plan to be communicated to discharge governance requirements.

#### **5. Risk Analysis**

5.1 PKF have assessed the key audit risks, which are contained within Appendix A of the attached Audit Plan. However, there will always be a risk that the auditor may find material errors or misstatements in the accounts and the results of the audit of the statements will not be known before they are presented for adoption by the Council as part of the Audit Committee function.

#### **6. Recommendation**

6.1 That the Audit Committee accepts the proposed Annual Audit Plan for 2012/2013.

#### **Lead officer contact**

Mick Hayward, Chief Finance Officer

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#### **Background papers**

The Annual Audit Plan 2012/2013 (attached as Appendix 1)

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# Audit Plan 2012/13

REPORT TO THE AUDIT COMMITTEE

Medway Council

MARCH 2013



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## Disclaimer

The *Code of Audit Practice* and *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 and officers. They are prepared for the sole use of the audited body and no responsibility is taken by auditors to any member of officer in their individual capacity or to any third party.

We accept no responsibility for any reliance that might be placed on reports and letters for any purpose by third parties, to whom it should not be shown without our prior written consent.

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# 1 Executive summary

We are pleased to present our Audit Plan for the year ending 31 March 2013. This plan summarises our proposed audit work for the year for Medway Council, the significant risks that impact on our audit and our planned work in response to those risks.

## AUDIT SCOPE AND RESPONSIBILITIES

The scope of the audit is determined by the Audit Commission's *Code of Audit Practice for Local Government (March 2010)* and requires us to review and report on your:

- financial statements
- arrangements for securing economy, efficiency and effectiveness in the use of resources.

BDO LLP and PKF (UK) LLP recently announced that we have agreed to merge our businesses and this is expected to be completed in spring 2013.

## RISK ASSESSMENT

We have identified the following areas of significant risk that impact on our audit:

### Financial statements

- management override of controls
- revenue recognition
- heritage assets
- property, plant and equipment (PPE) balances
- sundry debtor requisitions
- expenditure authorisation.

### Use of resources

- managing the reduction in central Government grant funding and addressing the budget gaps identified through the medium term financial strategy
- securing the necessary improvements in arrangements for protecting children following a review by Ofsted in January 2013 which judged such services to be inadequate (below minimum requirements).

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## REPORTING AND COMMUNICATIONS

We will provide an opinion on your financial statements and a conclusion on your arrangements to secure economy, efficiency and effectiveness by 30 September 2013. We will provide our detailed report on findings and conclusions to the Audit Committee ahead of the reporting deadline and provide reports throughout the year as appropriate.

In addition, we will provide an Annual Audit Letter summarising the key issues from our audit, as a public facing document to be included on your website. We will also provide a report summarising our grants certification work for the year.

## FEES

The proposed audit fee for our code audit work the year is £207,460 plus VAT, which is £19,000 above the scale fee published by the Audit Commission.

The proposed fee for the certification of claims and returns is £23,950 plus VAT, which is the composite scale fee published by the Audit Commission.

The scale fee for 2012/13 has been reduced compared to 2011/12 to reflect the combined impact of the Audit Commission's outsourcing of its in-house Audit Practice and other internal efficiency savings.

The scale fee has been increased by £19,000 after completing our detailed risk assessment in order to address:

- significant risks identified as part of this detailed risk assessment (detailed in section 3 of this report)
- the need to undertake detailed audit work on certain key financial systems where the Internal Audit section is not planning any review this year (as agreed with the Head of Internal Audit under our joint working arrangements).

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# 2 Audit scope and responsibilities

## PURPOSE OF THIS REPORT

We are pleased to present our Audit Plan for the year ending 31 March 2013, to set out a mutual understanding of our respective responsibilities, and to promote effective two-way communication between us.

This plan summarises our proposed audit work for the year for Medway Council, the significant risks that impact on our audit and our planned work in response to those risks.

The information and fees in this plan will be kept under review throughout the year and updated as necessary for any significant changes to risks and the focus of the audit, which will be reported to the Audit Committee.

## COMMUNICATION

Auditing Standards require auditors to communicate relevant matters relating to the audit to “those charged with governance”. Relevant matters include issues on auditor independence (below), audit planning information and significant risks (section 3) and findings from the audit (section 4).

## SCOPE OF THE AUDIT

The scope of the audit is determined by the Audit Commission’s *Code of Audit Practice for Local Government (March 2010)* which describes how auditors carry out their functions as set out in the *Audit Commission Act 1998*. This requires us to review and report on your:

- financial statements
- arrangements for securing economy, efficiency and effectiveness in the use of resources.

### Financial statements

The financial statements audit is conducted in accordance with International Standards on Auditing (UK & Ireland) (ISAs), *Practice Note 10: audit of public sector bodies in the United Kingdom (Revised)* and guidance issued by the Audit Commission.

### Use of resources

Our review of your arrangements to secure economy, efficiency and effectiveness is based on the following two criteria:

- the organisation has proper arrangements in place for securing financial resilience

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- the organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

### Whole of Government Accounts (WGA)

Local authorities are required to prepare information to allow HM Treasury to prepare consolidated Whole of Government Accounts based on the statutory financial statements. The WGA return is audited in accordance with Audit Commission specified procedures and requires additional assurance to confirm that counter-party data is properly and accurately recorded.

We provide an assurance report to the National Audit Office to confirm that the WGA return is consistent with the audited financial statements and that it is properly prepared.

### Certification of grant claims and returns

As an agent of the Audit Commission we will undertake a review of grant claims and returns above the audit threshold in accordance with the certification instructions issued by the Audit Commission.

We express a conclusion whether the claim or return: is in accordance with the underlying records (claims and returns above the minimum level and below the threshold value specified by the Audit Commission); or is fairly stated and in accordance with the relevant terms and conditions (claims and returns over the specified threshold value).

### RESPECTIVE RESPONSIBILITIES

The respective responsibilities of the Council and ourselves are set out in in the *Statement of Responsibilities of Auditors and Audited Bodies (2010)* and *Statement of responsibilities of grant-paying bodies, authorities, the Audit Commission and appointed auditors in relation to claims and returns*, both available from the Audit Commission's website.

The Council remains responsible for: the preparation of the financial statements; for exercising its functions economically, efficiently and effectively; the preparation of the Whole of Government Account return; and for preparing accurate grant claims and returns.

We are responsible for forming and expressing an opinion on these in accordance with the requirement of the *Code* and other guidance. Our audit responsibilities do not relieve you of your responsibilities.

### INDEPENDENCE AND OBJECTIVITY

We consider there are no relationships between PKF or other member firms of the PKF International network and yourselves, including councillors, senior management and affiliates, which may reasonably be thought to bear upon our objectivity and independence as auditors.

BDO LLP and PKF (UK) LLP recently announced that we have agreed to merge our businesses and this is expected to be completed in spring 2013. The firm, under the BDO



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brand, will be a leading accountancy and business advisory firm, with some 3,500 people in the UK generating revenues approaching £400 million. The merger creates a financially strong business with significant sector and geographical coverage across the UK.

PKF has a significant presence in providing audit and assurance services to public sector entities, including local authorities. BDO offers a well regarded advisory and consultancy practice across the public sector. Our clients should see significant benefits arising from this merger in the depth and breadth of the services available.

A copy of PKF's general policies and processes for maintaining objectivity and independence can be provided on request.

#### CO-OPERATION WITH OTHER BODIES

The *Code* requires co-operation between auditors and other regulatory bodies including the National Audit Office to facilitate an efficient audit. In preparing this plan, we have assumed that the Council has provided us permission to discuss issues relevant to the audit with regulators and other auditors.

#### QUALITY OF SERVICE

We are committed to providing 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 Robert Grant 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").

In addition, the Audit Commission's complaints handling procedure is detailed on their website <http://www.audit-commission.gov.uk/about-us/contact-us/complaints/>

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# 3 Risk assessment

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 significant risk relevant to our audit responsibilities and reflecting this in the audit fees.

The determination of significant risks is a matter for auditors' professional judgment. For each of the significant audit risks identified, we consider the arrangements put in place to mitigate the risk and plan our work accordingly. Current and emerging risks that do not impact on our audit are also discussed with management so that we may add value to the risk assessment process and monitor any areas of concern to the Council.

We detail below significant risks impacting on our audit of the financial statements or arrangements for securing economy, efficiency and effectiveness in the use of resources.

If you consider there to be other significant risks, whether due to fraud or error, please let us know.

## FINANCIAL STATEMENTS

We will plan and perform procedures designed to obtain reasonable assurance about whether the financial statements are free from material misstatement, whether due to fraud or error, thereby enabling us to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. The applicable financial reporting framework is the *CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2012/13*.

We will obtain an understanding of the Council and of the environment in which it operates, including the Council's internal controls and this, together with information obtained from discussions with management, provides a basis for identifying and assessing the risks of material misstatement.

### Fraud risk assessment

The primary responsibility for ensuring that your internal control frameworks are sufficient to prevent and detect fraud and corrupt practices lies with management and "those charged with governance" (the Audit Committee).

We have discussed the possible risk of material misstatement arising from fraud with the Chief Finance Officer and the Head of Internal Audit. Each has confirmed that they are not aware of any actual, suspected or alleged instances of material fraud during the financial year. We continue to liaise with the Head of Internal Audit on cases identified by the Council's anti fraud arrangements.

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We will also be writing to the Chairman of the Audit Committee to confirm he is not aware of any actual, suspected or alleged instances of fraud during the financial year.

In the meantime, please let us know if there are any actual, suspected or alleged instances of fraud of which you are aware.

For all fraud risks, and for any actual frauds that have been identified and which we have been informed of, we will consider the possible impact on your financial statements and our audit programme.

### Significant risks

We have identified areas of significant risk that impact on our audit. These, and our proposed work to respond to such risks, are set out below.

#### **Management override of controls**

ISA (UK&I) 240 *The auditor's responsibilities in relation to fraud in an audit of financial statements* requires us to presume that a risk of management override of controls is present and significant in all entities.

We are required to respond to this risk by testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements. We will review accounting estimates for evidence of possible bias and obtain an understanding of the business rationale for significant transactions that are outside the normal course of business for the Council or that otherwise appear to be unusual. We are also required to consider the need to perform other additional procedures to respond to the identified risk of management override of controls.

#### **Revenue recognition**

ISA (UK & Ireland) 240 requires us to presume that there are risks of fraud in revenue recognition. These risks may arise from the use of inappropriate accounting policies, failure to apply the Council's stated accounting policies or from an inappropriate use of estimates in calculating revenue. As a consequence our audit work will be designed to focus on these areas.

#### **Heritage assets**

In our 2011/12 annual governance report, we reported that the insurance value of heritage assets is uplifted each year using an index determined by the Council's Insurers. The calculation was used to determine the valuation of heritage assets as at 1 April 2011 and 31 March 2012 for inclusion in the 2011/12 financial statements. A formal valuation of heritage assets has not been undertaken for a number of years. We recommended that the Council obtain a full valuation of its heritage assets as at 1 April 2012 to inform the closure of the 2012/13 accounts.

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As at February 2013, officers are in the process of planning for the commissioning of the required revaluation work. However there is a risk that the information will not be available in time for inclusion in the draft financial statements which could lead to a materially misstated heritage asset balance. We will review the outcome of the professional valuers work to ensure that heritage assets are fairly stated in the accounts.

### **Property, plant and equipment (PPE) balances**

Since the introduction of IFRS in 2010/11, the Council has implemented new systems and procedures to ensure the accuracy of PPE balances. The Council has made good progress in implementing the new asset management system (Logotech), to assist in the production of the financial statements. In 2011/12, we found a number of significant errors and inconsistencies which related to:

- ownership of fixed assets
- revaluations
- expenditure incurred on Academy schools.

Our liaison with officers to date indicates that good progress is being made in addressing these issues. However there remains a risk that systems and procedures may not have been fully embedded into the closure of accounts process. In addition, the Council has experienced some turnover in finance staff which may adversely affect the resources and knowledge available to the department in the short term. We will review the specific areas of PPE identified above to ensure such balances are fairly stated.

### **Expenditure authorisation**

Deficiencies in authorisation controls in the previous year meant some officers were approving invoices to be paid in excess of their approved limits.

Since we reported such deficiencies, management has assured us that, with effect from 1 September 2012, the Council has improved its processes and controls in this area. We intend to review the enhanced controls as part of our financial systems audit in April 2013.

There remains a risk around the authorisation of non-purchase order invoices for the first six months of the year. We will therefore undertake additional testing to address this.

### **Sundry debtor authorisation**

In 2011/12 we reported the deficiencies in controls over requests for, and subsequent authorisation of, sundry debtor accounts and that controls should be implemented in accordance with financial operating procedures.

Since we reported these deficiencies in controls management has assured us that, with effect from 1 September 2012, the Council has established improved processes and controls in this area.

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There remains a risk around the authorisation of sundry debtor requisitions for the first six months of the year. We will therefore undertake additional testing to address this.

#### Internal control

As part of our audit we obtain an understanding of the Council's system of internal control sufficient to plan the audit. We assess the adequacy of the design of specific controls that respond to significant risks of material misstatement and evaluate whether those controls have been implemented. Where we intend to place reliance on particular controls for the purposes of our audit, we will carry out procedures to test the operating effectiveness of those controls and use the results of those procedures to determine the nature, timing and extent of further audit procedures to be performed.

At this stage of the audit we are aware of the following matters that may require further work:

#### Care Director social care payments

Officers have informed us about the difficulties in reconciling the information interface between the Care Director system and the Integra (account payables) system. We are aware that additional management review controls have been put in place to ensure the information used to support the payment is accurate. We will review the management controls to ensure these are adequately designed and operating effectively to respond to the significant risk of material mis-statement. If we conclude that controls are not operating effectively, we will report this to the Audit Committee and carry out further audit procedures accordingly.

#### Journal authorisation

We reported deficiencies in journal authorisation controls (including schools) in 2011/12 and management agreed to improve procedures in this area with effect from 1 April 2012.

We intend to review the enhanced controls as part of our financial systems audit in April 2013. If any issues are identified as a result of this work we will report the impact on the financial statements audit to the Audit Committee as soon as practicably possible.

#### Internal audit

It is our intention to use the work of your internal auditors in reaching our audit conclusions. We will be seeking to use work performed on the following financial systems:

- housing and council tax benefits
- council tax
- national non-domestic rates
- housing rents
- expenditure & creditors

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We will review the following financial systems:

- debtors income & • general ledge • cash & bank
- treasury management • payroll • fixed assets
- care director income and expenditure • ICT

#### Reliance on management experts

Where the financial statements contain amounts included by management that have been derived from information or estimates provided by experts, we may seek to place reliance on that work in obtaining audit evidence. As part of our work we expect to obtain assurance on the work undertaken by the following experts:

- valuation of land, buildings and dwellings assets and estimated economic useful life provided by qualified valuers
- valuation of pension liabilities and share of the scheme assets provided by your actuary
- valuation of provision for insurance and other claims against the Council and recommendations for any change to associated earmarked reserves
- fair value calculations and disclosures for financial instruments carried at amortised costs including investment assets and borrowings.

#### Materiality

Materiality is the expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. In carrying out our work we will apply an appropriate level of materiality and as such the audit cannot be relied upon to identify all potential or actual misstatements.

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## USE OF RESOURCES

We will plan and perform procedures designed to obtain reasonable assurance about whether the Council has put in place proper arrangements for securing economy, efficiency and effectiveness in the use of resources. In meeting this responsibility, we will review and, where appropriate, examine evidence that is relevant to the Council's corporate performance management and financial management arrangements and report on these arrangements.

In doing so, we have regard to the criteria specified by the Commission.

### Significant risks

We have undertaken our value for money risk assessment for 2012/13. This takes into account matters arising from the completion of the 2011/12 audit and additional audit knowledge gained from our regular liaison meetings and planning processes. We have also considered the impact of other regulators' work throughout the year as part of our evaluation of the arrangements to secure economy, efficiency and effectiveness in the use of resources.

We have identified areas of significant risk that impact on our audit. These, and our proposed work to respond to such risks, are set out below.

### Financial resilience

#### *Medium term financial strategy*

The Government continues to reduce its funding to local government over the Spending Review period. Combined with additional pressures arising from demographic and other changes, further risks are emerging for all Councils to balance their financial positions over the medium and longer term planning horizons.

Changes to the arrangements for funding council tax support and the business rate retention scheme, along with the transfer of responsibility for public health services to local authorities such as Medway, provide further uncertainties to medium term financial planning.

We intend to review the Council's medium term financial strategy to assess how well it is addressing such pressures and to review financial resilience.

### Securing economy, efficiency and effectiveness

#### *Arrangements for the protection of children – Ofsted report*

In January 2013, Ofsted carried out an unannounced inspection of the Council's arrangements for the protection of children and concluded that overall effectiveness was inadequate (below minimum requirements). The review considered the effectiveness of the help and protection provided to children, young people, families and carers, the quality of practice and the leadership and governance provided by the Council. Ofsted specified action the Council should implement immediately and over the next six months (commencing February 2013). The Council has prepared an improvement plan and identified the investment

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needed to deliver it. Ensuring that the most vulnerable children and young people are safe, is a strategic priority stated in the Council Plan. In order to monitor the progress made on the improvement plans we will consider the conclusions of other regulators' work and other internal reviews throughout the year to ensure that the Council is adequately prioritising resources to secure value for money in achieving its priorities.

#### Other use of resources work

We will also review the following audit tools and discuss the findings with management as appropriate:

- Financial Ratios data to identify any areas of concern over spending commitments, funding levels, and reserves and balances
- Value for Money Profiles to identify areas where the Council is an outlier in terms of its annual expenditure on services and performance data.



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# 4 Reporting and communications

## COMMUNICATION

During the course of our work, we will communicate to you relevant matters relating to the audit. We will communicate matters of governance interest that have come to our attention as a result of the performance of the audit. The audit is not designed to identify all matters that may be relevant to you.

Communication may take the form of discussions or, where appropriate, be in writing.

If we identify significant deficiencies in internal control, we will communicate such deficiencies to you, in writing, as soon as is practicable.

Our contact for communications will be the Chief Finance Officer and the Audit Committee. When communicating with this Committee, we will consider all individuals representing those charged with governance as 'informed' and our responsibilities for communicating relevant matters will be discharged.

## FINDINGS FROM THE AUDIT

As required by auditing standards and the *Code*, we will communicate the following matters to you, where applicable:

- significant deficiencies in internal control identified during the audit
- significant qualitative aspects of the Council's accounting practices including the application of the applicable financial reporting framework
- significant matters discussed, or subject to correspondence with management or other employees
- uncorrected misstatements (see below)
- material misstatements that have been corrected by management
- other significant matters relevant to the financial reporting process
- material uncertainties relating to going concern
- written representations that we are requesting from you or from other parties
- expected modifications to the opinion or emphasis of matter (or other matter) paragraphs in the auditor's report

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- significant difficulties that we have encountered during the course of the audit
  - any matters that prevent us from being satisfied that you have put in place proper arrangements for securing economy, efficiency and effectiveness in the use of resources
  - any matters reported in the public interest
  - any recommendations made under section 11(3) of the Audit Commission Act 1998.

### UNCORRECTED MISSTATEMENTS

We will report to you all uncorrected misstatements that relate to the current financial year (including those arising in previous periods that have an effect on the current year financial statements) and the effect that they have individually, or in aggregate, on the opinion in the auditor's report except for those that are clearly trivial. For reporting purposes, we consider misstatements of less than £180,000 to be trivial, unless the misstatement is indicative of fraud.

We will identify material uncorrected misstatements individually. We will request that any uncorrected misstatements are corrected.

### AUDIT TEAM

The following staff will be involved in the audit throughout the year:

<p><b>Robert Grant</b> – Engagement partner            email: robert.grant@uk.pkf.com            Tel: 020 7065 0170</p>	<p>Responsible for delivering the audit in line with the <i>Code</i>, including agreeing the Audit Plan, Governance Report and any other reports.            Also responsible for signing opinions and conclusions.</p>
<p><b>Kerry Barnes</b> – Manager            email: kerry.barnes@uk.pkf.com            Tel: 020 7065 0217</p>	<p>Responsible for overall control of the audit, ensuring timetables are met and reviewing the audit output.            Also responsible for liaison with the senior management and the Audit Committee.</p>
<p><b>Jody Etherington</b> – Assistant manager            email: jody.etherington@uk.pkf.com            Tel: 020 7065 0485</p>	<p>Responsible for managing the delivery of our audit fieldwork on site.</p>

## TIMETABLE AND OUTPUTS

Area of audit	Fieldwork	Reporting
<b>Financial statements</b>		
Review of internal controls	Mar - Apr 2013	30 Sept 2013
Final audit of the financial statements	July - Aug 2013	30 Sept 2013
Report on the consistency of the WGA return	Aug - Sept 2013	4 Oct 2013
<b>Use of resources</b>		
Review of the arrangements to secure economy, efficiency and effectiveness in the use of resources	Apr - Aug 2013	30 Sept 2013
<b>Certification of grants and returns</b>		
Audit of grants and returns	Jun - Nov 2013	Departmental deadlines
<b>Reporting</b>		
Report on significant deficiencies in internal controls (if required)		June 2013
Governance report to the Audit Committee		Sept 2013
Annual Audit Letter		Oct 2013
Certification of grants and returns report		Dec 2013

We will agree specific dates for our site 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.

# 5 Fees

## AUDIT COMMISSION SCALE FEES

The proposed *Code* audit fee for the year is £207,460 plus VAT and is £19,000 above the scale fee.

The proposed fee for the certification of claims and returns is £23,950 plus VAT, which agrees to the composite scale fee published by the Audit Commission.

The fee for 2012/13 has been reduced compared to 2011/12 to reflect the combined impact of the Audit Commission's outsourcing of its in-house Audit Practice and internal efficiency savings at the Audit Commission.

The scale fee has been increased by £19,000 after completing our detailed risk assessment in order to address:

- significant risks identified as part of this detailed risk assessment (detailed in section 3 of this report)
- the need to undertake detailed audit work on certain key financial systems where the Internal Audit section is not planning any review this year (as agreed with the Head of Internal Audit under our joint working arrangements).

The fee is analysed by audit area as follows:

Audit area	Planned fee 2012/13 (£)	Outturn fee 2011/12 (£)
<b>Code audit work</b>		
Scale audit fee	188,460	314,100
Additional risk based work	19,000	59,000
<b>Total Code audit work</b>	<b>207,460</b>	<b>373,100</b>
<b>Certification of claims and returns, including grants report</b>	<b>23,950</b>	<b>45,000</b>

The fee reflects the effective co-operation with Internal Audit and the coverage of its work programmes. There are limited opportunities to further reduce fees other than by making improvements to the Council's accounting arrangements.

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## QUESTIONS AND OBJECTIONS

Should any arise, time spent dealing with questions and objections will be billed separately under the *Code* audit fee. Where possible we will provide an estimate of the likely time required to respond to the matters before starting the work.

## ASSUMPTIONS

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, to an adequate standard, and we are able to place full reliance on this work
- there are no significant changes to your main financial systems 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 Audit Commission or National Audit Office instructions or guidance.

The fee assumes efficient co-operation as set out above and is set at the minimum level to carry out the audit.

Subject to prior approval by the Audit Commission, we reserve the right to increase fees should the above assumptions not be met or where we encounter unexpected problems, or issues arise, that cause significant additional work. Time spent dealing with problems or matters arising are usually that of senior people and hence the cost will often, necessarily, be disproportionate to the original fee.

## BILLING ARRANGEMENTS

The *Code* audit fee will be billed as £94,230 in September 2012, £47,115 in December 2012, and £66,115 in March 2013.

Fees for certification of grants and returns will be billed upon completion of each relevant return.

## Appendix A – Risk assessment

Audit risk identified from planning	Area and assertions	Audit response
<b>FINANCIAL STATEMENTS</b>		
<p><b>1 Management override</b> ISA (UK&amp;I) 240 requires us to presume that a risk of management override of controls is present and significant in all entities.</p>	<p>Financial statement level risk across all account headings and assertions</p>	<p>We are required to respond to this risk by testing the appropriateness of journal entries and other adjustments made in the preparation of the financial statements.</p> <p>We will review accounting estimates for evidence of possible bias and obtain an understanding of the business rationale of significant transactions that are outside the normal course of business for the Council or that otherwise appear to be unusual.</p>
<p><b>2 Revenue recognition</b> ISA (UK &amp; Ireland) 240 requires us to presume that there are risks of fraud in revenue recognition. These risks may arise from the use of inappropriate accounting policies, failure to apply the Council's stated accounting policies or from an inappropriate use of estimates in calculating revenue.</p>	<p>Occurrence, accuracy and completeness of income</p>	<p>We will substantively test an extended sample of revenue items to ensure that accounting policies have been correctly applied in determining the point of recognition of income and that income is completely and accurately recorded.</p>
<p><b>3 Heritage assets</b> There is a risk that heritage asset balances will be materially misstated if information regarding revaluations are not received in time for the production of the draft financial statements.</p>	<p>Valuation &amp; allocation of non-current assets</p>	<p>We will review correspondence with the valuers to confirm that correct valuations have been incorporated into the financial statements.</p>
<p><b>4 Property, plant and equipment (PPE) balances</b> There is a risk that PPE balances may be materially misstated due to the closedown plan not being fully embedded and also due to the risk of loss of resources and knowledge of the production of these balances in the finance department.</p>	<p>All balance sheet assertions Accuracy of revaluation income and expenditure</p>	<p>We will substantively test an extended sample of assets to ensure that they have been accounted correctly to address the relevant assertions.</p>
<p><b>5 Expenditure authorisation</b> There is a risk that inappropriate expenditure has been processed throughout the first six months of the year due to deficiencies in authorisation controls of non-purchase order invoices.</p>	<p>Occurrence, accuracy and completeness of expenditure</p>	<p>We will substantively test an extended sample of non-purchase order invoices during the first six months of the year to ensure it was appropriate to do so.</p>
<p><b>6 Sundry debtor authorisation</b> There is a risk that inappropriate income has been raised on the</p>	<p>Occurrence, accuracy and completeness of</p>	<p>We will undertake specific audit procedures during the first six months of the year to ensure transactions are valid.</p>

Audit risk identified from planning	Area and assertions	Audit response
Council's ledger during the first six months of the year due to the lack of controls around the authorisation of sundry debtor requisitions.	income.	
<b>USE OF RESOURCES</b>		
<p>7 <b>Financial resilience</b></p> <p>There is a risk that the Council may not identify or achieve significant savings and efficiencies that are needed in the medium term to respond to the reduction in government funding and other financial pressures.</p>	Financial resilience	We will review the Council's achievement of financial targets and efficiencies required for maintaining financial balance.
<p>8 <b>Securing economy, efficiency and effectiveness</b></p> <p><i>Arrangements for the protection of children – Ofsted review</i></p> <p>There is a risk that improvement plans are not been fully implemented to address all of the weaknesses identified by Ofsted.</p>	Financial resilience Economy, efficiency and effectiveness	In order to monitor the progress made on the improvement plans we will consider the conclusions of other regulators' work and other internal reviews throughout the year to ensure that the Council is adequately prioritising resources to secure value for money in achieving its priorities.