

Annual Audit and Inspection Letter

Harlow District Council

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Reference:	HA019 Annual Audit and Inspection Letter
Date:	December 2004

Executive summary

The purpose of this letter

This is our audit and inspection 'Annual Letter' for Members, which incorporates the Annual Audit Letter for 2003/04, and is presented by the Council's Relationship Manager and District Auditor. The letter summarises the conclusions and significant issues arising from our recent audit and inspections of the Council.

We have issued separate reports during the year. These reports are listed at Appendix 1 for information.

Appendix 2 sets out the scope of our audit and inspection work.

Appendix 3 provides information about the fees charged for this work.

Key messages

Council performance

Comprehensive Performance Assessment

The Council is still working on developing an Improvement Plan following the 'poor' rating under Comprehensive Performance Assessment (CPA). This work is being undertaken in conjunction with the ODPM Lead Official.

Best Value Performance Plan and indicators

The Council's Best Value Performance Plan (BVPP) complied in all material respects with legislation and statutory guidance. The arrangements for preparing performance indicators were also improved compared to the previous year, and we have issued an unqualified opinion on the BVPP and the system for collecting the 2003/04 outturn Best Value Performance Indicators (BVPIs).

The accounts

We have given your accounts an unqualified audit opinion. This opinion was delayed due to issues surrounding the compilation of the Housing Benefit claim and the reconciliation to the financial statements.

Financial position

The Council's financial position is adequate but continues to be diminished as reserves are used to support revenue spending. There is an urgent need to set a balanced and priority-led budget for 2005/06 to ensure that the level of reserves is not eroded further.

Other accounts and governance issues

We have not identified any significant weaknesses in the overall control framework, although we have made a number of suggestions to further tighten the control processes that are currently in place.

Action needed by the Council

- Ensure that a balanced and priority-led budget is set for 2005/06.
- Continue to use the strengths and weaknesses identified in the formal CPA report as the basis for work on the Council's recovery plan, in conjunction with the ODPM lead official.
- Continue to work on the methods of data collection and calculation of BVPIs.
- Review the current debt profile and the relevant processes for debt collection as appropriate.
- The Council needs to review its current approach to the compilation of grant claim returns and ensure that Quality Assurance procedures are introduced to reduce the level of amendments and qualifications to claims.

Council performance

The Council is still working on developing an Improvement Plan following the 'poor' rating under Comprehensive Performance Assessment. This work is being undertaken in conjunction with the ODPM Lead Official.

CPA and improvement

In June 2004 the Council was assessed as 'poor' under the Comprehensive Performance Assessment (CPA) framework.

The main elements of the assessment were:

- a self-assessment completed by the Council;
- accredited peer challenge to inform the Council's self-assessment;
- a corporate assessment of the Council's overall effectiveness in supporting services to deliver improvements;
- an assessment of the Council's service delivery performance through two diagnostic assessments on:
 - progress in meeting the decent homes standard;
 - management of public space;
- the Benefit Fraud Inspectorate's (BFI) assessment of benefit services;
- the District Auditor's assessment of performance on each of the main elements of the Code of Audit Practice; and
- audited performance indicators, inspection reports and plan assessments.

Summary of CPA judgements

The following section details the CPA judgements as they were reported in June 2004.

Since its inception in the 1950s, Harlow has taken a paternalistic approach to providing a wide range of services for local people. Spending has increased to a point where it is one of the highest spending Councils in England. Whilst this has been buoyed up by large capital receipts from right to buy and a capital transfer from the major repairs allowance, and drawing on reserves, this is no longer sustainable.

The Council has seen 47 years of single party leadership. This situation changed in 2002 and there has been no overall political control since. It has ambitious plans, in partnership with others, for what it wants to achieve for the local community. In order to fulfil these ambitions, the Council needs to make some important decisions about the future for both the Council and the local area.

However, there are constant political battles, played out very publicly in meetings and in the local media, which do not allow these to receive sensible debate. There is little trust between officers and members and overall there is a poor relationship between them, which gets in the way of Council business. There is a strong blame culture and both sides have become entrenched and frustrated. There is a danger that the Council will not be able to deliver the ambitions it has for its local community.

Current resources are spread too thinly and despite three years of trying, the Council has not been able to identify clear priorities or carry out a strategic assessment of the high levels of discretionary spending. Some savings have been made, but these have either been non-strategic, across the board reductions or involved tinkering around the edges. The failure to identify priorities and focus activities and resources on those priorities, is a serious failure, and puts in jeopardy the Council's ambitions as a community leader.

The Council has an ambitious new chief executive who is clearly focused on sorting out the many significant challenges facing the Council. He will need strong support from within and outside of the organisation to be successful.

Although not clearly identified as priorities, there has been some focus in areas such as housing, young people, regeneration, community safety and environment. There have been some achievements and improvements in a number of these and examples of where it has made a difference to the lives of local people, especially the most disadvantaged. But this is not part of a clear plan which the Council has been following.

The Council was subject to a number of corporate governance inspections from December 2000 onwards and has begun a journey to change.

Investments aimed at improving the way the Council works, include a number of initiatives in procurement, IT, customer care, capital investment assessment and human resources. Investments in broader areas include the Gateway scheme, waste management, work around estate sustainability and building partnerships, such as those to manage anti-social behaviour and health improvement. However, investment in some of the key building blocks to allow it to move forward is still under-developed, for example performance management, project management and a culture which allows effective decision making and scrutiny. There is no effective medium-term financial strategy which is a key tool to allow the Council to be clear about the capacity it needs to meet its future ambitions.

The community strategy (Harlow 2020), is the longer-term plan for the future of Harlow. In response to the need to accommodate significant growth, the Council is working with partners to explore a number of options. This puts pressure on the Council in terms of its senior management capacity, at a time when it also faces many other significant challenges. There is no overall corporate plan, and the Council has a history of getting distracted from what it set out to do.

Since the CPA report was published, the Council has worked with the ODPM lead official and have recently submitted a recovery plan to the ODPM.

Recommendation

Continue to use the strengths and weaknesses identified in the formal CPA report as the basis for work on the Council's recovery plan, in conjunction with the ODPM lead official.

Other Audit Commission inspections

Given the timing of the CPA, no other inspections have been undertaken at the Council in the last year.

Other performance work

Given the timing of the CPA, no other performance work has been undertaken during the year, as we had previously reported our work on Procurement and Key Performance Management developments in last year's letter.

Best Value Performance Plan

The Council's Best Value Performance Plan (BVPP) complied in all material respects with legislation and statutory guidance. The arrangements for preparing performance indicators were also improved compared to the previous year, and we have issued an unqualified opinion on the BVPP and the system for collecting the 2003/04 outturn Best Value Performance Indicators (BVPIs).

Under the Local Government Act 1999, specified local government bodies are required to comply with the general duty of best value, which is defined as making arrangements to secure continuous improvement in the way in which their functions are exercised, having regard to a combination of economy, efficiency and effectiveness.

The Council is required to publish annually a BVPP, which summarises its assessment of performance and its plans in relation to Best Value. The Council is responsible for preparing the BVPP and for the information and assessments that are set out within it and the assumptions and estimates on which they are based. It is also responsible for putting in place appropriate performance management and internal control systems, from which the information and assessments in the BVPP are derived.

Auditors consider and report on whether the Council has complied with statutory requirements in respect of the preparation and publication of its BVPP.

Auditors are not required to form a view on the completeness or accuracy of the information or the realism and achievability of the assessments published by the audited body in its BVPP.

Publication of the 2004/05 BVPP

We concluded that the Council's BVPP contains all the key elements required by legislation and statutory guidance. We have therefore issued an unqualified audit opinion on the BVPP.

Performance information

The Council has continued to improve its arrangements for the production and publication of accurate and reliable performance information. We are required to review these arrangements and report our findings to the Audit Commission.

Our audit was supplemented by some early testing of a number of key BVPIs at the request of officers, so that remedial action could be taken where necessary. As only one reservation was placed on an indicator, we were able to issue an unqualified opinion on the system for collecting 2003/04 outturn indicators. This compares well to last year when we reported reservations on seven indicators, which led to the qualification of the BVPP. The Council has taken positive action to overcome the system weaknesses which led to the reservations last year and is to be congratulated on this.

In total we reviewed 43 indicators as part of our audit, making amendments in 28 instances. Again, this is a significant improvement on the previous year, but improvements can still be made to the collation process to reduce the number of amendments needed for errors emanating from the use of the wrong population figure or base data.

Recommendation

Continue to work on the methods of data collection and calculation of BVPIs.

Follow-up of previous reviews

In our last Annual Audit Letter we reported our recommendations from our earlier work on:

- performance management; and
- procurement.

We have not undertaken any formal follow up work since this piece of work because of CPA and Improvement Planning but we have included it in our future work programme and we will report any significant issues to Members as appropriate.

Accounts and governance

We have given your accounts an unqualified audit opinion. Your overall corporate governance arrangements are satisfactory in most key areas however we have made a number of recommendations to further strengthen your current arrangements.

Review of core processes

We examined the Council's core processes to assess the basis on which the accounts are prepared. The work was undertaken in March and April 2004 and we reviewed:

- the main accounting system;
- the budgetary control process; and
- the year-end closedown process.

We concluded that there was a risk of these processes leading to material misstatements in the financial statements. There were 12 recommendations arising from our work, especially around the compilation and review of financial reconciliations. Where data is transferred between separate financial systems, a clear audit trail needs to exist between the two and be regularly agreed. This is to ensure that all transactions are captured by the central system.

A number of these recommendations had not been implemented by the time of the final accounts audit and have given rise to audit issues during our review of these statements.

Audit of 2003/04 accounts

We gave an unqualified opinion on the Council's accounts on the 30 November 2004. This opinion was delayed due to issues surrounding the compilation of the Housing Benefit claim and the reconciliation to the financial statements.

A set of draft accounts was received in mid-August 2004. This was in advance of the statutory deadline for 2003/04 of 31 August, for which the Council should be congratulated.

The published accounts are an essential means by which the Council reports its stewardship of the public funds at its disposal and its financial performance in the use of those resources. Members approved the Council's annual accounts on 19 August 2004.

In last year's Annual Audit and Inspection Letter we emphasised that timeliness in producing the accounts will become increasingly important over the next few years as the deadline for completion of the accounts is brought forward in line with the Government's requirement (see Exhibit 1 below).

Whilst the accounts have been prepared to meet the requirements this year, the deadlines will become increasingly more difficult to achieve and will require early planning and thoughtful scheduling of key meetings next year.

EXHIBIT 1 TIMETABLE FOR ACCOUNTS PRODUCTION

	2004/05	2005/06
Financial statements to be approved by	31 July	30 June
Audit opinion to be given by	31 October	30 September

Matters arising from the final accounts audit and report to 'those charged with governance' in the Council

We are required to comply with the Statement of Auditing Standard (SAS) 610 – reporting to those charged with governance.

This required us to report on matters arising from our audit in relation to:

- expected modifications to the standard auditors' report included in the accounts;
- unadjusted misstatements;
- material weaknesses in the accounting and internal control systems identified during the audit;
- our views about the qualitative aspects of the Council's accounting practices and financial reporting;
- matters specifically required by other auditing standards to be communicated to those charged with governance; and
- any other relevant matters relating to the audit.

Our SAS 610 report was presented to the Policy and Resources Committee on 18 November 2004. The key issues were in relation to weaknesses in accounting and internal control systems and were:

- reconciliations - there are significant weaknesses in the production and quality of reconciliations between feeder systems and the main ledger. This issue is raised for the second year;
- missing bank accounts - two bank accounts were omitted from the financial statements;
- benefits claims - there were fundamental uncertainties over the accuracy of the original Housing Benefit and Housing Subsidy claims. The Council changed its IT software provider at the year-end but the compilation of the 2003/04 claim was based on the old software. This software was not updated with the various software updates after the year-end; and
- unauthorised write-offs - £67k of non-domestic rates bad debts were written off without authorisation which is contrary to the Council's financial regulations.

These key issues need to be addressed as a matter of priority. All other audit adjustments required as a result of our audit had been made by officers.

Further details of these and other matters arising from our audit of final accounts will be included in our final accounts audit memo.

The prudential code

The CIPFA prudential code has been produced to underpin the revised system of capital finance for local government, which came into force in January 2004.

The objectives of the code are to ensure that:

- capital expenditure plans are affordable;
- external borrowing and other liabilities are within prudent and sustainable levels;
- treasury management decisions are in accordance with professional good practice; and
- the Authority is accountable.

Because the Authority is debt free and does not currently have plans to borrow money, the prudential code has not been seen as central to the formulation of capital plans. However, the prudential code should be fundamental to the way in which Council's consider future capital plans and the revenue consequences of them, to allow the Council's corporate priorities to be delivered.

We will review in detail the progress made in implementing the prudential code, through our audit work in 2004/05 and we will report to Members any significant issues that arise.

Financial standing

The Council's financial position is adequate but continues to be diminished as reserves are being used to support revenue spending. There is an urgent need to set a balanced and priority-led budget for 2005/06 to ensure that the level of reserves is not eroded further.

General fund spending and balances

There was a budgeted use of reserves amounting to £0.5 million in order to finance revenue spending during 2003/04. The general fund balances now stands at £2.8 million, which represents 13 per cent of the 2004/05 gross revenue budget. Although a contribution of £1.4 million was made to the general reserve, the general fund balance was reduced by £1.1 million. Therefore, over the last three years general fund balances have been used to support spending on the general fund by £2.2 million.

This seriously undermines the Council's ability to ensure that resources are effectively focussed on delivering its priorities and could affect future Council Tax levels if the continued use of reserves to finance corporate spending is not brought under control.

2003/04 financial year

General fund net expenditure for the year was £13.9 million, which was £0.8 million below the revised budget but in line with the original budget. The outturn position in relation to the statutory accounts was a reported breakeven position, once the use of general fund balances had been taken into account.

The 2004/05 budget has been set with a view to using a further £0.25 million of general fund reserves, which does not equate to a balanced and priority led budget.

As previously recommended, the Council needs to review its budget setting process to ensure that a balanced and priority led budget, that is unsupported by the use of reserves, is set.

2004/05 financial year

The net revenue budget for 2004/05 was set at £13.7 million. The latest quarterly monitoring report (Month 7) shows a current underspend of £0.96 million against this profiled budget. The monthly monitoring by the Budget and Performance Working Party of such information is to be commended. However, such an underspend at this point in time, suggests that the profiling of the budget needs further work, if the Council is to make full use of these monitoring reports. Members should continue to be made aware of the ongoing financial position so that remedial action can be taken as appropriate.

Recommendation

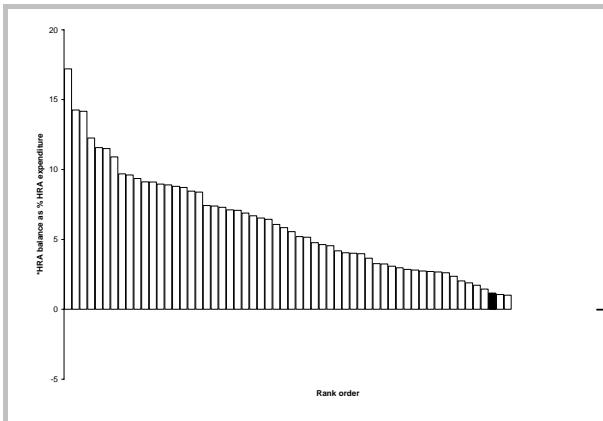
Ensure that a balanced and priority led budget is set for 2005/06.

Housing Revenue Account

The Audit Commission 'Balances database' assesses Harlow's financial health compared to other district Council in terms of a number of key financial ratios. The Housing Revenue Account (HRA) balance as a percentage of HRA expenditure is also low compared to other Districts, again suggesting this balance is not healthy (Exhibit 2).

The 2004/05 budget does make provision for a significant transfer of funds to the HRA balance which should, if it materialises, improve the current position.

EXHIBIT 2 HRA BALANCE AS % OF HRA EXPENDITURE



Note: Harlow is represented by the black bar.

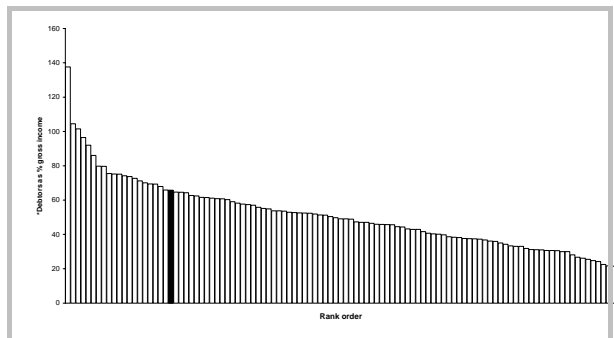
Capital programme

The revised capital forecast for 2003/04 was £24.6 million (Original budget - £22.9 million, including bought forward underspends). Against this revised forecast, there was an underspend of £7.7 million. Whilst the slippage has been carried forward to the 2004/05 capital programme, incurring such underspends should not become the norm as the Authority is unduly exposing itself to resourcing implications for such schemes. This is the second year in which significant underspends have occurred (£4.1 million in 2002/03). The capital programme also supports the Authority's Community Plan and delays to the implementation of capital schemes may impinge on the ability to deliver the key aspects of this plan.

Income collection and arrears

The total level of debtors as a percentage of gross income at Harlow is significant when compared to other District Council (Balances database), even when taking account of the £6 million Gateway debtor and the provision for bad debts. This suggests that the Council has a problem in collecting the arrears that are due to it (Exhibit 3) and the relevant processes should be reviewed.

EXHIBIT 3 DEBTORS AS % GROSS INCOME



Note: Harlow is represented by the black bar.

Recommendation

Review the current debt profile and the relevant processes for debt collection as appropriate.

Systems of internal financial control

We have not identified any significant weaknesses in the overall control framework, although we have made a number of suggestions to further tighten the control processes that are currently in place.

Internal Audit

We undertook our annual review of Internal Audit and reported our findings within our Interim Regularity report.

We expressed concerns around the current management and reporting arrangements in place, given the central role that Internal Audit should play as part of the control environment of the Council.

We understand that this issue is being addressed through the new corporate management structure and we will review these new arrangements in the coming year.

Any other issues

Our overall review of your arrangements for internal financial did not identify any significant weaknesses but we have highlighted a number of areas where controls could be further enhanced.

Our audit of the 2002/03 benefit claim was qualified because there was not an adequate reconciliation between the claim and the amount reported within the accounting system (ledger).

Standards of financial conduct and the prevention and detection of fraud and corruption

We have not identified any significant weaknesses in your arrangements to prevent and detect fraud and corruption, but we have suggested that an anti-fraud and corruption policy be formulated and adopted by Members.

We completed our assessment of the Authority's overall arrangements to maintain standards of conduct and prevent and detect fraud and corruption.

A key gap in the Council's arrangements is the lack of a formally agreed anti-fraud and corruption policy, which will set the standards of conduct in a transparent and open manner.

No instances of fraud or corruption have been reported to us during the year.

Legality of transactions

We have not identified any significant weaknesses in the Council's framework for ensuring the legality of its significant financial transactions.

We reviewed both the Authority's overall arrangements to help ensure the legality of transactions with financial consequences and we did not identify any significant areas of concern.

Other work

Additional voluntary work

We have not undertaken any additional voluntary work on your behalf during 2003/04.

Grant claims

Over recent years the number of claims requiring audit certification has grown and audit fees have risen in line with this growth. In accordance with Strategic Regulation, the Audit Commission has adopted a more risk-based approach to the certification of grant claims. With effect from 2003/04 the smaller claims have not been subject to audit or have received a lighter touch. The approach to larger claims has been determined by risk and the adequacy of the Council's control environment.

Once again the Council has completed and submitted the required grant returns in a timely manner. However, the Council's arrangements for managing and quality assuring grant claims submitted for audit is poor. Of the significant grant claims which we have certified, all have been qualified and the majority amended. There is a lack of formal quality assurance by a peer reviewer once they have been compiled, although there are other technical issues which have led to a number of the qualifications. Exhibit 4 below shows the details of claims certified since the last Annual Audit Letter.

EXHIBIT 4 GRANT CLAIM CERTIFICATIONS

Claim	Qualified	Amended
Housing Benefits (2002/03)	Yes	Yes
Housing Subsidy (2002/03)	Yes	Yes
Single Regeneration Budget (2002/03)	Yes	Yes
European Social Fund (2002/03)	Yes	Yes
National Non-Domestic Rates (2003/04)	Yes	No
Housing Subsidy Baseline data return (2004/05)	Yes	Yes

Similar issues were reported to the Council in our Annual Audit Letter last year and as a response we issued a grant claims guidance protocol to officers. The Council is potentially putting at risk the levels of subsidy which it receives from the grant paying bodies through the current approach.

Recommendation

The Council needs to review its current approach to the compilation of grant claim returns and ensure that Quality Assurance procedures are introduced to reduce the level of amendments and qualifications to claims.

National Fraud Initiative

The Council took part in the Audit Commission's National Fraud Initiative (NFI) 2002/03. The NFI, which is undertaken every two years, brings together data from local authorities, NHS bodies, government departments and other agencies, to detect a wide range of frauds against the public sector. Total savings from the 2002/03 exercise exceeded £83 million. The Authority undertook a review of its data matching information in October 2003. This review highlighted nine possible matches which were then investigated further. These cases did not prove to be fraudulent.

The Audit Commission is repeating the exercise this year and will again collect payroll, pensions, housing benefits, student loan and housing rents data from Authorities.

Alongside the core exercise a number of pilot initiatives are being undertaken at selected sites. These are focused on risk areas that were highlighted by Authorities and include payments made to privately run care homes, abuse of blue badge parking permits, serial insurance claimants and duplicate payments to suppliers. These pilot areas, if they prove effective, will be incorporated into future NFI exercises.

Looking forwards

Future audit and inspection work

We have an agreed plan for 2004/05 and we have reported in this letter those aspects that have already been completed.

The remaining elements of that plan, including our audit of the 2004/05 accounts, will be reported in next year's Annual Letter.

We will seek to ensure, wherever possible, that our work relates to the improvement priorities of the Council when planning our programme of work for 2005/06. We will seek to reconsider, with you, your improvement priorities in the light of the CPA assessment and your own analysis, and develop an agreed programme by 31 March 2005.

Revision to the Code of Audit Practice

The Audit Commission has consulted on a revised Code of Audit Practice for application to the audit of the 2005/06 accounts. The new Code, which will be laid before Parliament in January 2005, is designed to secure:

- a more streamlined audit, which is proportionate to risk and targeted on areas where auditors have most to contribute to improvement;
- a stronger emphasis on value for money, focussing on corporate performance and financial management arrangements (rather than individual services and functions); and
- better and clearer reporting of the results of audits.

Further details will be provided in the Audit and Inspection Plan 2005/06.

Closing remarks

This letter has been discussed and agreed with the Chief Executive and Executive Director - Resources. A copy of the letter was presented at the Policy and Resources Committee on 20 December 2004.

The Council has taken a positive and constructive approach to our audit and inspection and we would like to take this opportunity to express our appreciation for the Council's' assistance and co-operation.

Availability of this letter

This letter will be published on the Audit Commission's website at www.audit-commission.gov.uk, and also on the Council's website.



Simon Cookson
District Auditor

Ian Davidson
Relationship Manager
December 200

Status of our reports to the Council

Our Annual Audit and Inspection Letter is prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. Annual audit and Inspection Letters are prepared by relationship managers and appointed auditors and addressed to Members and officers. They are prepared for the sole use of the audited and inspected body, and no responsibility is taken by the Audit Commission or its appointed auditors to any Member or officer in their individual capacity, or to any third party.

Audit and inspection reports issued

Reports issued	Date
Grant Claim Guidance Protocol	February 2004
Procurement Review	March 2004
Key Performance Management Developments	March 2004
2004/05 Audit Plan	April 2004
Comprehensive Performance Assessment	June 2004
2002/03 Final Accounts Memorandum	September 2004
2003/04 Interim Regularity Report	September 2004
Best Value Performance Indicator Audit	October 2004
Best Value Performance Plan Opinion	November 2004
2003/04 Final Accounts Memorandum	November 2004 (Draft)
Annual Audit and Inspection Letter	December 2004

Scope of audit and inspection

Audit

Our main objective as your appointed auditor is to plan and carry out an audit that meets the requirements of the Code of Audit Practice. We adopt a risk-based approach to planning our audit, and our audit work has focused on your significant financial and operational risks that are relevant to our audit responsibilities.

Central to our audit are your corporate governance arrangements. Our audit is then structured around the three elements of our responsibilities as set out in the Code and shown in Exhibit 5.

EXHIBIT 5 THE THREE MAIN ELEMENTS OF OUR AUDIT OBJECTIVES



Accounts

- Opinion.

Financial aspects of corporate governance

- Financial standing.
- Systems of internal financial control.
- Standards of financial conduct and the prevention and detection of fraud and corruption.
- Legality of transactions.

Performance management

- Use of resources.
- Performance information.
- Best Value Performance Plan.

Inspection

Inspection work is based around section 10 of the Local Government Act 1999, which requires us to carry out inspections and deliver reports that will:

- enable the Council and the public to judge whether best value is being delivered;
- enable the Council to assess how well it is doing;
- enable the Government to assess how well its policies are being implemented; and
- identify failing services where remedial action may be necessary.

The Audit Commission has circulated to all audited bodies a statement that summarises the key responsibilities of auditors. Our audit has been conducted in accordance with the principles set out in that statement. What we say about the results of our audit should be viewed in the context of that more formal background.

Audit and inspection fee

Audit fee update

Audit area	Plan 2003/04 (£)	Actual 2003/04 (£)
Accounts	32,500	32,500
Financial aspects of corporate governance	30,000	30,000
Performance	86,000	86,000
TOTAL CODE OF AUDIT PRACTICE FEE	148,500	148,500
Grant claim certification	40,000	62,990
Additional voluntary work (under section 35)	0	0

Inspection fee update

The full year inspection fee is £17,468. The work reported in this Audit and Inspection Letter has been funded by an element of the fee covering 2003/04 and by an element of the fee covering 2004/05. In both years the actual fee will be in line with that planned.