Hampshire County Council

Audit planning report - update

Year ended 31 March 2020

July 2020

Building a better working world

13 July 2020

Audit Committee
Hampshire County Council
The Castle
Winchester
Hampshire
SO23 8UJ

Dear Members

Audit planning report

We are pleased to attach our an update to our Audit Plan reported to you in January 2020. Following the coronavirus outbreak (Covid-19) in March 2020, we have re-assessed our audit scope and strategy. We provide an update to the significant accounting and auditing matters, and audit approach outlined in the original Audit Plan. We have also included a section with an overview of our progress against our audit plan (Appendix D).

This report is a key mechanism in ensuring that our audit is aligned with the Committee's service expectations.

This report is intended solely for the information and use of the Audit Committee and management, and is not intended to be and should not be used by anyone other than these specified parties.

We welcome the opportunity to discuss this report with you on 23 July 2020 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Kevin Suter

For and on behalf of Ernst & Young LLP

Contents

Public Sector Audit Appointments Ltd (PSAA) issued the "Statement of responsibilities of auditors and audited bodies". It is available from the PSAA website (https://www.psaa.co.uk/audit-quality/statement-of-responsibilities/).The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.
The "Terms of Appointment and further guidance (updated April 2018)" issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature.
This report is made solely to the Audit Committee and management of Hampshire County Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee, and management of Hampshire County Council those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit Committee and management of Hampshire County Council for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.

01 Overview of our 2019/20 audit strategy

Overview of our 2019/20 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Investment Property Valuation	Significant Risk	New risk identified as a result of COVID-19	Covid-19 was declared a global pandemic on 11 March 2020 and since March, Covid-19 has had an impact on the investment property market. There has been an impact on the occupation of buildings due to forced closures and rental income is expected to fall as tenants default on their rents. In addition, valuers are including 'material valuation uncertainty' clauses in their valuation reports which indicate that there is less certainty over the valuations, and more valuer judgement is required as there is less transactional evidence to support market assumptions.
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively. In addition to our overall response, we consider where these risks may manifest themselves and identify separate fraud risks as necessary below. We concluded that only those procedures included under 'Inappropriate capitalisation of revenue expenditure' are required.
Inappropriate capitalisation of revenue expenditure	Fraud risk	No change in risk or focus	Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. Our judgement is that this risk at this Council relates to the improper capitalisation of revenue expenditure.
Valuation of Land and Buildings	Inherent risk	Focus now solely on valuation of land and buildings as increase in IP Valuation risk.	Property, Plant and Equipment Land and Buildings (L&B) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Material judgemental inputs and estimation techniques are required to calculate the year-end L&B balances held in the balance sheet. As the Council's asset base is significant, and the outputs from the valuer are subject to estimation, there is a higher inherent risk that L&B may be under/overstated or the associated accounting entries incorrectly posted. We are required us to undertake procedures on the use of experts and assumptions underlying fair value estimates.

Overview of our 2019/20 audit strategy

Risk / area of focus	Risk identified	Change from PY	Details
Pension Accounting	Inherent Risk	No change in risk or focus	The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Hampshire County Council. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2019 this totalled £1,327 million. The information disclosed is based on the IAS 19 report issued by the actuary to the County Council. Accounting for these schemes involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. We are required to undertake procedures on the use of experts and the assumptions underlying fair value estimates.
Private Finance Initiatives (PFI)	Inherent risk	New risk identified this year	There is a high level of estimation and complexity involved with this estimate. In addition, the amount is significant to the Council and as such a small variation in the estimate can have a significant impact.

Materiality – updated for the draft financial statements

Planning materiality £42.5m

Planning materiality has been set at £42,527,000 which represents 1.8% of 2019/20 gross expenditure

Performance materiality £31.9m

Performance materiality has been set at £31,895,000 which represents 75% of Planning Materiality

Audit differences £2.1m

We will report all uncorrected misstatements relating to the income statement and balance sheet that have an effect on income and misstatements in the OCI over £2,100,000. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

Overview of our 2019/20 audit strategy

Audit scope

This updated Audit Plan covers the work that we plan to perform to provide you with:

- our audit opinion on whether the financial statements of Hampshire County Council give a true and fair view of the financial position as at 31 March 2020 and of the income and expenditure for the year then ended; and
- our conclusion on the Council's arrangements to secure economy, efficiency and effectiveness;

We will also review and report to the National Audit Office (NAO), to the extent and in the form required by them, on the Council's Whole of Government Accounts return.
Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.
When planning the audit we take into account several key inputs:

- strategic, operational and financial risks relevant to the financial statements;
- developments in financial reporting and auditing standards;
- the quality of systems and processes;
- changes in the business and regulatory environment; and
- management's views on all of the above.

By considering these inputs, our audit focuses on the areas that matter and our feedback is more likely to be relevant to the Council.
We will provide an update to the Audit Committee on the results of our work in these areas in our report to those charged with governance scheduled for delivery in July 2020.

Taking the above into account, and as articulated in this audit plan, our professional responsibilities require us to independently assess the risks associated with providing an audit opinion and undertake appropriate procedures in response to that. Our Terms of Appointment with PSAA allow them to vary the fee dependent on "the auditors assessment of risk and the work needed to meet their professional responsibilities". PSAA are aware that the setting of scale fees has not kept pace with the changing requirements of external audit with increased focus on, for example, the valuations of land and buildings, the auditing of groups, the valuation of pension obligations, the introduction of new accounting standards such as IFRS 9, 15 and 16 in recent years as well as the expansion of factors impacting the value for money conclusion. Therefore to the extent any of these are relevant in the context of Hampshire County Council's audit, we will discuss these with management as to the impact on the scale fee.

Audit team changes

Key changes to our team.

Kevin Suter, Associate Partner

- Kevin takes over from Maria Grindley as the Engagement Lead.
- Kevin has significant public sector audit experience over 20 years, with a portfolio of Local Authorities, Police and Crime Commissioner & Constabularies, Local Government Pension Fund and National Park Authority audits.

02 Audit risks

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Misstatements due to fraud or error

Financial statement impact

Misstatements that occur in relation to the risk of fraud due to management override could affect a number of areas of the financial statements.

What is the risk?

As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively.

We identify and respond to this risk on every audit engagement.

Covid-19 update: No change to our original assessment at this stage. We will discuss with management what steps were taken to maintain a robust control environment during the disruption

What will we do?

- Inquire of management about risks of fraud and the controls put in place to address those risks.
- Understand the oversight given by those charged with governance of management's processes over fraud.
- Consider of the effectiveness of management's controls designed to address the risk of fraud.

Perform mandatory procedures regardless of specifically identified fraud risks, including:

- Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements
- Assessing accounting estimates for evidence of management bias, and
- Evaluating the business rationale for significant unusual transactions.

We will utilise our data analytics capabilities to assist with our work.

Having evaluated this risk we have considered whether we need to perform other audit procedures not referred to above. We concluded that only those procedures included under 'Inappropriate capitalisation of revenue expenditure' are required.

Our response to significant risks

We have set out the significant risks identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Inappropriate capitalisation of revenue expenditure

Financial statement impact

Misstatements that occur in relation to the risk of fraud in revenue and expenditure recognition could affect the income accounts. The relevant accounts we associate the revenue and expenditure recognition risk to had the following balances in the 2018-19 financial statements:

Cost of services expenditure: £2,165 million

PPE additions: £147.6 million

What is the risk?

Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

The risk in local government is in areas where management make judgements that impact whether material items of expenditure are financed from capital or revenue resources. This would be effected by management override of journal controls.

As such we associate this risk with capital additions.

Covid-19 update: No change to our original assessment, since proposed original testing will still cover this area.

What will we do?

For a sample of recorded capital additions we will examine invoices, capital expenditure authorisations and other data that support the appropriateness of these additions.

We will ensure that the items are capital in nature, and do not include revenue items.

We will utilise our data analytics capabilities to assist with our work through identifying high risk transactions, such as items originally recorded as revenue expenditure and subsequently capitalised.

Other areas of audit focus

What is the risk/area of focus?	What will we do?
Valuation of Land & Buildings and Investment Property Land and Buildings is the most significant balance in the Council's Balance Sheet. The valuation of Land and Buildings (L&B) and Investment Property (IP) is complex and subject to a number of assumptions and judgements. A small movement in these assumptions can have a material impact on the financial statements. Covid-19 update: Related constraints on property valuation Nationally, the Royal Institute of Chartered Surveyors (RICS), the body setting the standards for property valuations, has issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets may cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty have been included in some final year-end valuation reports produced by valuers. Covid-19 has had an impact on the investment property market. There has been an impact on the occupation of buildings due to forced closures and rental income is expected to fall as tenants default on their rents. Given the significant change in market conditions since the onset of Covid-19, investment property valuation will constitute a significant risk. This is due to the uncertainty in the financial and property markets.	We will: • Consider the competence, capability and objectivity of the Council's internal valuer; • Consider the scope of the valuer's work; • Ensure L&B assets have been revalued within a 5 year rolling programme as required by the Code; • Ensure IP has been annually revalued as required by the Code; • Consider if there are any specific changes to assets that should have been communicated to the valuer; • Sample test key inputs used by the valuer when producing valuations; • Consider the results of the valuer's work; • Challenge the assumptions used by the Council's valuer by reference to external evidence and our EY valuation specialists (where necessary); • Test journals for the valuation adjustments to confirm that they have been accurately processed in the financial statements; • Test a sample of assets revalued in year to confirm that the classification and valuation basis is appropriate and the accounting entries are correct; and • Review assets that are not subject to valuation in 2019/20 to confirm the remaining asset base is not materially misstated and classification correct. Additional procedures in response to our significant risk include: • Consider the Council's asset base by type of asset and valuation methodology, as impacts are likely to be more significant for assets valued on the basis of data from market transactions; • Ensure the appropriate disclosure has been made in the accounts concerning the material uncertainty; • Further input engaged from EY Real Estates, our internal specialists on asset valuations; and • Consider the wider impact of material uncertainty on whether reasonable assurance over valuation can be obtained.

Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures and therefore may be key audit matters we will include in our audit report.

What is the risk/area of focus?	What will we do?
<u>Pension Liability Valuation</u> The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Hampshire County Council. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2019 this totalled £1,327 million. The information disclosed is based on the IAS 19 report issued by the actuary to the County Council. Accounting for these schemes involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. The pension fund is subject to a triennial valuation this year. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates. In the prior year the 'McCloud' judgement impacted the estimate and resulted in an amendment of the net pension liability. We anticipate this will again be a key assumption in estimating the pension liability. We would expect the Authority's actuary to be basing their assumptions taking into account the Authority's specific membership profile and how it has been impacted by the judgement. We also note that there may be further developments in this area, potentially again coming after the balance sheet date.	We will: • Liaise with the auditors of Hampshire Pension Fund, to obtain assurances over the information supplied to the actuary in relation to the Council's scheme members, including any additional assurances required regarding membership data used in the triennial valuation; • Assess the work of the LGPS Pension Fund actuary (Aon Hewitt) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by the National Audit Office for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team; • Review Hampshire Pension Fund's financial statements and compare the year end asset value with the estimate used by the actuary when producing the Council's IAS 19 report; and • Review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS19. COVID-19 update: Volatility in the financial markets is likely to have a significant impact on pension assets, and therefore net liabilities, which needs to be considered by the CC. There is no change to the definition of the risk identified or procedures we will perform.

Audit risks

Other areas of audit focus (continued)

What is the risk/area of focus?	What will we do?
IFRS 16 Leases This new accounting standard is applicable for local authority accounts from the 2020/21 financial year and will change: • How operating leases are recognised (as lessee); and • The disclosure requirements for operating leases (as lessee). The 2020/21 Cipfa Code of practice on local authority accounting has not yet been issued. However, the Code requires the disclosure of information relating to the impact of an accounting change that will be required by a new accounting standard, but one which has not yet been implemented. As at 31 March 2019, the Council had £39m of future minimum operating lease payments. Covid-19 update The adoption of IFRS 16 as the basis for preparation of Local Authority financial statements has been deferred to 2021/22. The Council will therefore no longer be required to undertake an impact assessment, and disclosure of the impact of the standard in the financial statements does not now need to be financially quantified.	We therefore no longer consider this to be an areas of audit focus, but will feedback to the CC any relevant observations from our discussions with the management earlier in the year.
Private Finance Initiatives The Council has 2 PFI contracts in place, in respect of waste and street lighting, with liabilities amounting to £180 million in 2018/19. These were both operational and recognised in the Council's balance sheet as at 31 March 2019. Covid-19 update No change to our original assessment or approach.	We will: • We will involve EY specialists in this area to ensure accounting treatment proposed by the Council is appropriate; and • This work will include analysis of the contracts, and review and consideration of the financial model

03 Value for Money Risks

Value for Money

Background

We are required to consider whether the Council has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

For 2019-20 this is based on the overall evaluation criterion:

“In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people”

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.

In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

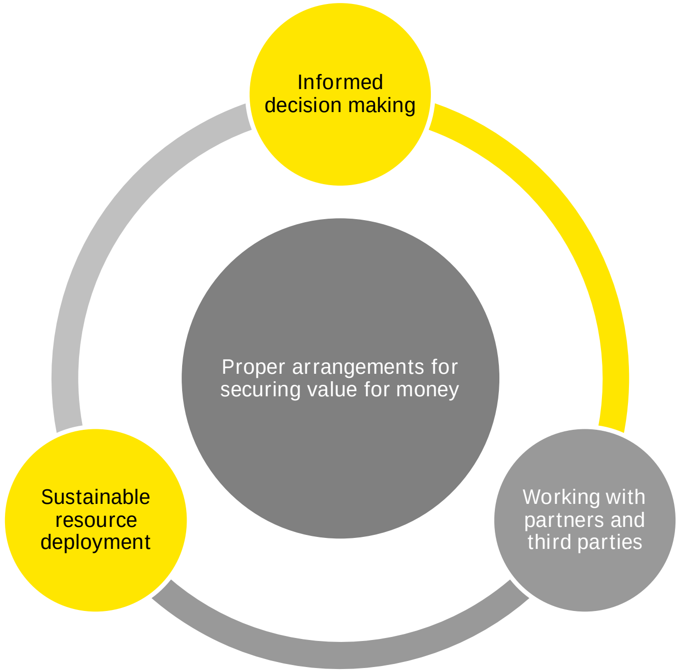
We are only required to determine whether there are any risks that we consider significant, which the Code of Audit Practice defines as:

“A matter is significant if, in the auditor’s professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public”

Our risk assessment supports the planning of sufficient work to enable us to deliver a safe conclusion on arrangements to secure value for money and enables us to determine the nature and extent of further work that may be required. If we do not identify any significant risks there is no requirement to carry out further work. We consider business and operational risks insofar as they relate to proper arrangements at both sector and organisation-specific level.

Our risk assessment has therefore considered both the potential financial impact of the issues we have identified, and also the likelihood that the issue will be of interest to local taxpayers, the Government and other stakeholders. This has resulted in the identification of no significant risks which we view as relevant to our value for money conclusion. We will continue to update our risk assessment throughout the course of our audit.

Covid-19 update
No change to our original assessment or approach.



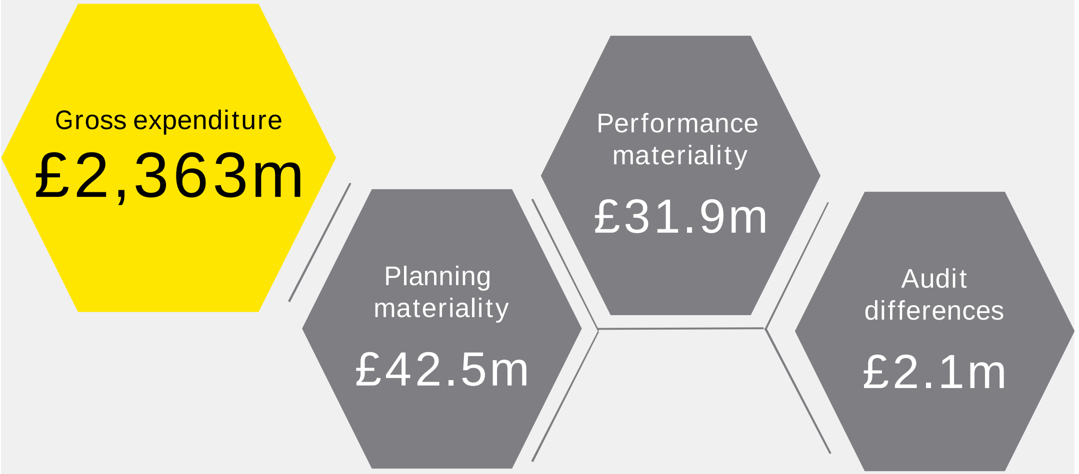
04 Audit materiality

Audit materiality

Materiality

Materiality – updated for the draft financial statements

For planning purposes, materiality for 2019/20 has been set at £42,527,000. This represents 1.8% of the Council's gross expenditure taken from the draft financial statements. This is based on the rationale that's public sector organisation do not have a focus on earnings profits. We consider industry factors, and using gross revenue expenditure is the industry norm.



We request that the Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

Key definitions

Planning materiality – the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

Performance materiality – the amount we use to determine the extent of our audit procedures. We have set performance materiality at £31,895,000 which represents 75% of planning materiality.

Audit difference threshold – we propose that misstatements identified below this threshold are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the income statement and balance sheet that have an effect on income or that relate to other comprehensive income.

Other uncorrected misstatements, such as reclassifications and misstatements in the cashflow statement or disclosures and corrected misstatements will be communicated to the extent that they merit the attention of the Audit Committee, or are important from a qualitative perspective.

Specific materiality – We have set a materiality of £1k for officers and senior employees' remuneration and audit fees disclosures. This reflects our understanding that an amount less than our materiality would influence the economic decisions of users of the financial statements in relation to these.

COVID-19 update: We have considered the materiality levels we reported to you in our original audit plan (as noted on this slide), and whether any change to our materiality is required in light of Covid-19. Following this consideration we remain satisfied that the values for planning materiality, performance materiality and our audit threshold for reporting differences remain appropriate.

05 Scope of our audit

Our Audit Process and Strategy

Objective and Scope of our Audit scoping

Under the Code of Audit Practice our principal objectives are to review and report on the Council's financial statements and arrangements for securing economy, efficiency and effectiveness in its use of resources to the extent required by the relevant legislation and the requirements of the Code.

We issue an audit report that covers:

1. Financial statement audit

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK).

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Procedures required by standards

- Addressing the risk of fraud and error;
- Significant disclosures included in the financial statements;
- Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- Auditor independence.

Procedures required by the Code

- Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance Statement; and
- Reviewing and reporting on the Whole of Government Accounts return, in line with the instructions issued by the NAO.

2. Arrangements for securing economy, efficiency and effectiveness (value for money)

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources.

Our Audit Process and Strategy (continued)

Audit Process Overview

Our audit involves:

- Identifying and understanding the key processes and internal controls; and
- Substantive tests of detail of transactions and amounts.

Our initial assessment of the key processes across the Council has identified the following key processes where we will seek to rely on controls, both manual and IT:

- Accounts receivable;
- Accounts payable;
- Payroll;
- Cash and bank;

In 2019/20, Hampshire County Council Integrated business centre (IBC) have commissioned an ISAE 3402 type 2 report from EY's Financial Audit IT (FAIT) team. The ISAE 3402 report provides the users of the IBC with assurance over the suitability of the design and existence of controls and on the operating effectiveness of these controls during the financial year.

Analytics:

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular journal entries. These tools:

- Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- Give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Audit Committee.

Internal audit:

We will regularly meet with the Head of Internal Audit, and review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit plan where they raise issues that could have an impact on the financial statements.

Changes in audit processes

Audit Process overview

Additional audit procedures as a result of Covid-19

Other changes in the entity and regulatory environment as a result of Covid-19 that have not resulted in an additional risk, but result in the following impacts on our audit strategy are as follows:

- Going concern: management's assessment of whether the Council is a going concern will need to consider the impact of the current conditions on the Council's future performance. Additional narrative disclosure will be required, including on the future principal risks and uncertainties, including the impact on operations for 2020/21 and beyond.
- Annual Governance Statement: the widespread use of home working is likely to change the way internal controls operate. The Annual Governance Statement will need to capture how the control environment has changed during the period and what steps were taken to maintain a robust control environment during the disruption. This will also need to be considered in the context of internal audit's ability to issue their Head of Internal Audit opinion for the year, depending on the ability to complete the remainder of the internal audit programme.
- Information Produced by the Entity (IPE): There is an increased risk around the completeness, accuracy, and appropriateness of information produced by the entity due to the likely inability of the audit team to verify original documents or re-run reports on-site from the CC's systems. We will:
    - Use the screen sharing function of Microsoft Teams to evidence re-running of reports used to generate the IPE we're auditing; and
    - Agree IPE to scanned documents or other system screenshots.
- Post balance sheet events: There is an increased risk that further events after the balance sheet date concerning the current Covid-19 pandemic will need to be disclosed. The amount of detail required in the disclosure will need to reflect the specific circumstances of the Council. We will review the CC's approach to identifying and disclosing events after the balance sheet date.
- Additional EY consultation requirements concerning the impact on auditor reports if necessary.

Changes in audit processes (continued)

Other ways in which COVID-19 could impact the financial statements. These may include, but not be limited to:

- Receivables – there may be an increase in amounts written off as irrecoverable and impairment of year-end balances due to the increased number of businesses and residents unable to meet their financial obligations.
- Holiday and sickness pay – the change in working patterns may result in year-end staff pay accruals which are noticeably different to prior years.
- Government support – any Covid-19 specific government support is likely to be a new transaction stream and may require development of new accounting policies and treatments

In addition to the impact on the financial statements themselves, the disruption caused by Covid-19 may impact on management's ability to produce the financial statements and our ability to complete the audit to the planned timetable. For example, it may be more difficult than usual to access the supporting documentation necessary to support our audit procedures. There will be additional audit procedures we have to perform to respond to the additional risks caused by the factors noted above.

The changes to audit risks and audit approach will change the level of work we perform. This may impact the audit fee. We will agree changes to the audit fee with management and report back to the Audit Committee in our Audit Results Report.

06 Audit team

Audit team

Audit team structure:

Kevin Suter*
Associate Partner

Sarah Croft
Senior Manager

Jack Dunkley
Manager

EY Real Estates

EY Actuaries

Working together with the Council

We are working together with officers to identify continuing improvements in communication and processes for the 2019/20 audit.

We will continue to keep our audit approach under review to streamline it where possible.

* Key Audit Partner

Use of specialists

When auditing key judgements, we are often required to use the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where EY specialists are expected to provide input for the current year audit are:

Area	Specialists
Pension valuation	Management Specialist – AoN Hewitt PwC (Consulting Actuary to the NAO) EY Specialist - EY actuaries
PFI valuation	Management Specialist - Capita
PPE valuation	Management Specialist - Management's in-house valuation experts EY Specialist - EY real estates

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Council's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- Analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- Assess the reasonableness of the assumptions and methods used;
- Consider the appropriateness of the timing of when the specialist carried out the work; and
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

07 Audit timeline

Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2019/20. The final timetable will depend on our ability to obtain sufficient, appropriate audit evidence to support our audit opinion.

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.

Due to the disruption caused by COVID-19, the statutory dates for publishing the accounts were changed this year. The deadline for publishing the audited accounts has been moved to 30 November 2020. Acknowledging the additional risks, and the additional time taken to complete an audit remotely, it was agreed with management to revise the signing timetable to September 2020.

Audit phase	Timetable	Audit committee timetable	Deliverables
Planning: Risk assessment and setting of scopes.	November		
Walkthrough of key systems and processes	November - December		
Development of audit plan	January		Audit Planning Report
Testing of routine processes and controls	February	Audit Committee	
Interim audit testing	February - March		
Year end audit Audit Completion procedures	September	Audit Committee	Audit Results Report Audit opinions and completion certificates
Year end audit Audit Completion procedures	October	Audit Committee	Annual Audit Letter

08 Independence

Introduction

The FRC Ethical Standard and ISA (UK) 260 "Communication of audit matters with those charged with governance", requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in June 2016, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	**Final stage**
► The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between the you, your affiliates and directors and us; ► The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review; ► The overall assessment of threats and safeguards; ► Information about the general policies and process within EY to maintain objectivity and independence. ► Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard	► In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed; ► Details of non-audit services provided and the fees charged in relation thereto; ► Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us; ► Written confirmation that all covered persons are independent; ► Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy; ► Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and ► An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, are disclosed.

Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non –audit services if the service has been pre-approved in accordance with your policy.

Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Kevin Suter, your audit engagement partner and the audit engagement team have not been compromised.

Self interest threats

A self interest threat arises when EY has financial or other interests in the Council. Examples include where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees. [

We believe that it is appropriate for us to undertake permissible non-audit services and we will comply with the policies that you have approved.

None of the services are prohibited under the Financial Reporting Council's Ethical Standard or the National Audit Office’s Auditor Guidance Note 01 and you have no policy on pre-approval. The ratio of non audit fees to audits fees is not permitted to exceed 70%.

At the time of writing, the current ratio of non-audit fees to audit fees is approximately 63%. All fees are set out in Appendix A.

The only non-audit fees relate to the independent Service Organisation Controls Type 2 Assurance Report for the Hampshire Integrated Business Centre (IBC).

From 2019/20 (and future years), the Council would like to obtain independent third party assurances over the financial reporting controls in place at the IBC. This is in respect of services provided to the IBC’s clients. The Council would like to obtain an independent Service Organisation Controls (SOC) 1 Type 2 assurance report covering the relevant financial year. This will need to be performed under the International Standard for Assurance Engagements (ISAE) No. 3402 issued by the International Auditing and Assurance Standards Board (IAASB). As this will be a Type 2 engagement, the review will focus on the design and operating effectiveness of controls for the relevant financial year.

To ensure our independence as external auditor to Hampshire County Council is not impaired we are required to seek approval from PSAA (Public Sector Audit Appointments Ltd) to provide these non-audit services. This approval has been requested.

We have adopted the following safeguards as a result:

- The work will be led and delivered by a separate Service Organisation Controls (SOC) reporting team. Members of the existing audit team at Hampshire County Council will not work on this project. The remuneration of the Engagement Lead and the audit team are not impacted by this project.
- The estimated fee is in line with market rates for this type of engagement. The engagement will have a clearly defined scope, as set out in the scope of work and this work would not influence our conduct of or the outcome of the audits.
- The SOC report issued will be generic in nature and not specific to a particular customer of IBC. The controls reviewed will be homogenous controls.
- This work is limited to review of controls within the end to end processes at the IBC. It does not include any aspects of decision-making on behalf of the IBC or the Council. It will not involve giving and advice in relation to decisions the IBC/ Council may take.

Relationships, services and related threats and safeguards

Self interest threats (continued)

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 4. There are no other self interest threats at the date of this report.

Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no self review threats at the date of this report.

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of the Council. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work.

There are no management threats at the date of this report.

Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

Other communications

EY Transparency Report 2019

Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the year ended 1 July 2019 and can be found here:

https://www.ey.com/en_uk/who-we-are/transparency-report-2019

09 Appendices

Appendix A

Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Communities and Local Government.

PSAA has published a scale fee for all relevant bodies. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the NAO Code.

	Planned fee 2019/20	Scale fee 2019/20	Final Fee 2018/19
		£	£
Total Fee	89,720	89,720	91,570*
Total audit	89,720	89,720	91,570*
Other non-audit services	56,500	N/A	43,000
Total other non-audit services	56,500	N/A	43,000
Total fees	146,220		132,720

All fees exclude VAT

- For 19/20 the scale fee may be impacted by a range of factors (see page 7), which we will update the committee on, as the audit progresses.
- We are in discussions with management and PSAA regarding changes to the scale fee due to significant changes in audit procedures and regulation since the award of the PSAA contract. We are yet to agree an update, and discussions continue.
- The planned fee does not include changes due to the updated risk assessment as a result of Covid-19. Again, we have raised this with management and discussions will continue.
- * the variation to 18/19 scale fee is still to be approved by PSAA

The agreed fee presented is based on the following assumptions:

- ► Officers meeting the agreed timetable of deliverables;
- ► The production of materially accurate draft accounts;
- ► Our accounts opinion and value for money conclusion being unqualified;
- ► Appropriate quality of documentation is provided by the Council; and
- ► The Council has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with the Council in advance.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

Appendix B

Required communications with the Audit Committee

We have detailed the communications that we must provide to the Audit Committee .

Required communications	What is reported?	Our Reporting to you When and where
Terms of engagement	Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit planning report
Significant findings from the audit	• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures • Significant difficulties, if any, encountered during the audit • Significant matters, if any, arising from the audit that were discussed with management • Written representations that we are seeking • Expected modifications to the audit report • Other matters if any, significant to the oversight of the financial reporting process	Audit results report
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: • Whether the events or conditions constitute a material uncertainty • Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements • The adequacy of related disclosures in the financial statements	Audit results report
Misstatements	• Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation • The effect of uncorrected misstatements related to prior periods • A request that any uncorrected misstatement be corrected • Corrected misstatements that are significant • Material misstatements corrected by management	Audit results report

Appendix B

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	What is reported?	When and where
Fraud	• Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity • Any fraud that we have identified or information we have obtained that indicates that a fraud may exist • A discussion of any other matters related to fraud	Audit results report
Related parties	• Significant matters arising during the audit in connection with the entity's related parties including, when applicable: • Non-disclosure by management • Inappropriate authorisation and approval of transactions • Disagreement over disclosures • Non-compliance with laws and regulations • Difficulty in identifying the party that ultimately controls the entity	Audit results report
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: • The principal threats • Safeguards adopted and their effectiveness • An overall assessment of threats and safeguards • Information about the general policies and process within the firm to maintain objectivity and independence	Audit Planning Report Audit Results Report
External confirmations	• Management's refusal for us to request confirmations • Inability to obtain relevant and reliable audit evidence from other procedures	Audit results report

Appendix B

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	What is reported?	When and where
Consideration of laws and regulations	• Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off • Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of	Audit results report
Internal controls	• Significant deficiencies in internal controls identified during the audit	Audit results report
Representations	Written representations we are requesting from management and/or those charged with governance	Assurance letter
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report
Auditors report	• Any circumstances identified that affect the form and content of our auditor's report	Audit results report
Fee Reporting	• Breakdown of fee information when the audit plan is agreed • Breakdown of fee information at the completion of the audit • Any non-audit work	Audit planning report Audit results report
Certification work	Summary of certification work undertaken	Certification report

Additional audit information

Other required procedures during the course of the audit	
In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.	
Our responsibilities required by auditing standards	• Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. • Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Council's internal control. • Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management. • Concluding on the appropriateness of management's use of the going concern basis of accounting. • Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation. • Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Council to express an opinion on the financial statements. Reading other information contained in the financial statements, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and • Maintaining auditor independence.

Appendix C

Additional audit information (continued)

Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines:

- The locations at which we conduct audit procedures to support the opinion given on the financial statements; and
- The level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

Appendix D - Progress on 2019/20 Audit

The following 'dashboard' summarises the progress of the 2019/20 audit after our interim audit visit. It seeks to provide the Audit Committee with an overview of the progress of the audit to date, and any issues arising.

Audit Area	Status	Details
Walkthroughs of key systems	Completed	- Accounts Payable - Accounts Receivable - Pensions - Payroll - Cash & Bank - Property, Plant & Equipment - Treasury Management - CONFIRM - SWIFT - Financial Statement Close Process
Interim substantive testing	In progress	We have completed testing on the following areas and note no issues: - Additions - Disposals (not material) - We have also started work on PPE Valuation and Existence testing which is ongoing but good progress has been made. - We have completed period 1-9 testing on payroll using our analytics tools and programme and have noted no issues - We have completed period 1-9 testing on income and expenditure and have noted no issues
Year-end substantive testing	In progress	Our year-end audit fieldwork is well underway. At this stage, we have nothing to bring to your attention.
Other procedures	Completed	We have completed testing on the following procedures and have encountered no issues: - Journal testing - Contract Review