

A high-angle, close-up photograph of several people's hands and arms gathered around a white table. They are looking at and pointing to various documents and papers spread across the surface. A smartphone is visible on the table. The scene suggests a collaborative meeting or review session.

Southampton City  
Council  
Audit planning report  
Year ended 31 March 2019

January 2019

31 January 2019



Governance Committee Members  
Southampton City Council  
Civic Centre  
Southampton, Hampshire, SO14 7LY

Dear Governance Committee Members

## Audit planning report

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the Governance Committee with a basis to review our proposed audit approach and scope for the 2018/19 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This plan summarises our initial assessment of the key risks driving the development of an effective audit for the Council, and outlines our planned audit strategy in response to those risks.

This report is intended solely for the information and use of the Governance 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 11 February 2019 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Helen Thompson  
For and on behalf of Ernst & Young LLP  
Enc

# 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.psa.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 Governance Committee and management of Southampton City Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Governance Committee, and management of Southampton City 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 Governance Committee, and management of Southampton City 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 2018/19 audit strategy



# Overview of our 2018/19 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Governance 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
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.
Risk of fraud in revenue and expenditure recognition, through inappropriate capitalisation of revenue expenditure	Fraud risk/ Significant risk	No change in risk; refocused	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. We have assessed the risk is most likely to occur through the inappropriate capitalisation of revenue expenditure.
Valuation of Land and Buildings	Other risk	No change in risk or focus	The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.
PFI Accounting	Other risk	No change in risk or focus	The Council has two PFI arrangements which are material to our audit. PFI accounting is a complex area, and a detailed review of these arrangements was undertaken by our internal specialist in 2017/18. We will review the accounting entries and disclosures in relation to PFI in 2018/19, with a focus on the correction of the non-material audit differences identified in 2017/18, and any significant changes since the specialist's review.
Pension Liability Valuation	Other 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. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.
New accounting standards	Other risk	Increase in risk or focus	The CIPFA Code of Practice for 2018/19 confirms that the local government bodies will implement International Financial Reporting Standard ("IFRS") 9 – Financial Instruments and IFRS 15 – Revenue from Contracts with Customers this year.

# Overview of our 2018/19 audit strategy

## Materiality

Planning  
materiality

£11.6m

Materiality has been set at £11.552m, which represents 1.8% of the prior years gross expenditure on provision of services. In light of changes across the audit profession, we have reduced the top of our range for materiality from 2% to 1.8%. This reduction in range has been applied across other Councils of a similar size audited by EY, and is not as a result of factors specific to Southampton City Council.

Performance  
materiality

£8.7m

Performance materiality has been set at £8.664m, which represents 75% of planning materiality.

Audit  
differences

£0.58m

We will report all uncorrected misstatements relating to the primary statements (comprehensive income and expenditure statement, balance sheet, housing revenue account and collection fund) greater than £0.578m. Other misstatements identified will be communicated to the extent that they merit the attention of the Governance Committee.

# Overview of our 2018/19 audit strategy

## Audit scope

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

- our audit opinion on whether the financial statements of Southampton City Council give a true and fair view of the financial position as at 31 March 2019 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 is focused on the areas that matter and our feedback is more likely to be relevant to the Council.



# 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\*

### What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK) 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 otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

### What will we do?

We will:

- identify fraud risks during the planning stages;
- enquire 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 the effectiveness of management's controls designed to address the risk of fraud;
- perform mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments in the preparation of the financial statements;
- review accounting estimates for evidence of management bias; and
- evaluate the business rationale for significant unusual transactions.

## Audit risks

# Our response to significant risks (continued)

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.

Risk of fraud in revenue and expenditure recognition, through inappropriate capitalisation of revenue expenditure\*

### Financial statement impact

We have assessed that the risk of fraud in revenue and expenditure recognition is most likely to occur through the inappropriate capitalisation of revenue expenditure. This would have the impact of reducing revenue expenditure and increasing additions to Property, Plant and Equipment.

### 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.

We have assessed the risk is most likely to occur through the inappropriate capitalisation of revenue expenditure, as there is an incentive to reduce expenditure which is funded from Council Tax.

### What will we do?

We will:

- test PPE additions using lowered testing thresholds, to ensure they are appropriately supported by documentary evidence, and that the expenditure incurred and capitalised is clearly capital in nature; and
- seek to identify and understand the basis for any significant journals transferring expenditure from non-capital codes to PPE additions or from revenue to capital codes on the general ledger at the end of the year.

## 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.

### What is the risk/area of focus?

#### Valuation of Land and Buildings

The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.

#### PFI accounting

The Council has two PFI arrangements which are material to our audit. PFI accounting is a complex area, and a detailed review of these arrangements was undertaken by our internal specialist in 2017/18. We will review the accounting entries and disclosures in relation to PFI in 2018/19, with a focus on the correction of the non-material audit differences identified in 2017/18, and any significant changes since the specialist's review.

### What will we do?

#### We will:

- consider the work performed by the Council's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work;
- sample test key asset information used by the valuers in performing their valuation (e.g. floor plans to support valuations based on price per square metre) and challenge the key assumptions used by the valuer;
- consider the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code for PPE and annually for IP. We have also considered if there are any specific changes to assets that have occurred and that these have been communicated to the valuer;
- review assets not subject to valuation in 2018/19 to confirm that the remaining asset base is not materially misstated;
- consider changes to useful economic lives as a result of the most recent valuation; and
- test accounting entries have been correctly processed in the financial statements,

#### We will:

- review assurances brought forward from prior years regarding the appropriateness of the PFI financial models;
- review the PFI financial models for any significant changes, and if identified consider engaging relevant experts to review the models to ensure they are still working as expected;
- ensure the PFI accounting models have been updated for any service or other agreed variations and confirm consistency of current year models with prior year brought forward assurances;
- agree outputs of the models to the accounts, and review the completeness and accuracy of disclosures; and
- review the correction of non-material audit differences identified in 2017/18 which are expected to be corrected this year.

## Other areas of audit focus (continued)

### What is the risk/area of focus?

#### Pension Liability Valuation

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 2018 this totalled £464 million.

The information disclosed is based on the IAS 19 report issued to the Council by the actuary to the County Council.

Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

### What will we do?

#### We will:

- liaise with the auditors of Hampshire Pension Fund, to obtain assurances over the information supplied to the actuary in relation to Southampton City Council;
- assess the work of the 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; and
- review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS19.

## Other areas of audit focus (continued)

### What is the risk/area of focus?

### What will we do?

#### IFRS 9 financial instruments

This new accounting standard is applicable for local authority accounts from the 2018/19 financial year and will change:

- How financial assets are classified and measured;
- How the impairment of financial assets are calculated; and
- The disclosure requirements for financial assets.

There are transitional arrangements within the standard; and the 2018/19 CIPFA Code of practice on local authority accounting provides guidance on the application of IFRS 9.

#### We will:

- assess the Council's implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19;
- consider the classification and valuation of financial instrument assets;
- review new expected credit loss model impairment calculations for assets; and
- check additional disclosure requirements.

#### IFRS 15 Revenue from contracts with customers

This new accounting standard is applicable for local authority accounts from the 2018/19 financial year.

The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations.

The 2018/19 CIPFA Code of practice on local authority accounting provides guidance on the application of IFRS 15 and includes a useful flow diagram and commentary on the main sources of LG revenue and how they should be recognised.

The impact on local authority accounting is likely to be limited as large revenue streams like council tax, non domestic rates and government grants will be outside the scope of IFRS 15. However where that standard is relevant, the recognition of revenue will change and new disclosure requirements introduced.

#### We will:

- assess the Council's implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19.
- consider application to the authority's revenue streams, and where the standard is relevant test to ensure revenue is recognised when (or as) it satisfies a performance obligation; and
- check additional disclosure requirements.



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## 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 2018/19 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.

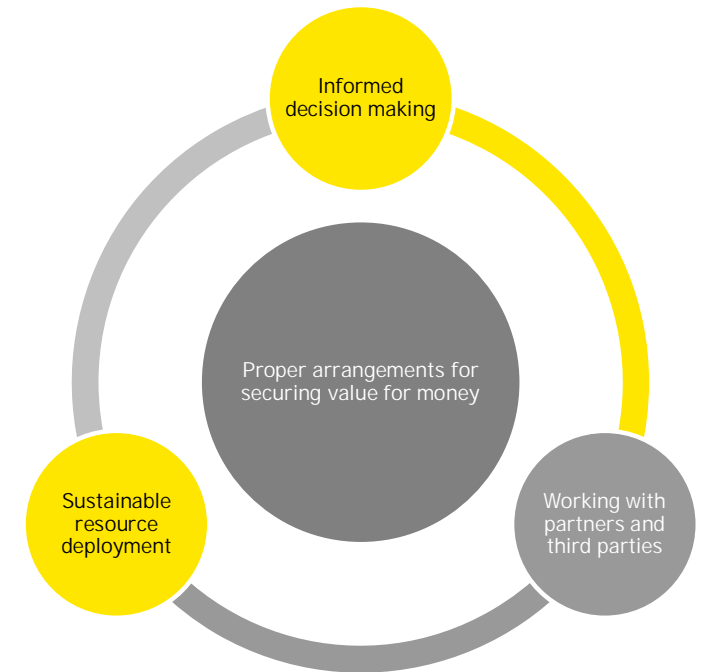
In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

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. In 2018/19 this has included consideration of the steps taken by Southampton City Council to consider the impact of Brexit. Although the precise impact cannot yet be modelled, we anticipate that councils will be carrying out scenario planning.

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 the significant risk noted on the following page which we view as relevant to our value for money conclusion.





## Value for Money Risks

What is the significant value for money risk?	What arrangements does the risk affect?	What will we do?
<p>Compliance with both procurement and contracting policies as part of a sound system of internal control.</p> <p>Our value for money conclusion in 2017/18 was qualified “except for” as a result of the identification of significant levels of non-compliance with the Council’s procurement rules. As the process of addressing the underlying issues has been ongoing through 2018/19, we consider that this remains an area of risk for our value for money conclusion this year. We will therefore seek to evaluate the strength and effectiveness of the measures the Council has put in place through our value for money work in 2018/19.</p>	<p>Take informed decisions</p>	<p>Our approach will focus on seeking assurance that the measures which have been introduced and reinforced in response to the adverse findings reported in 2017/18 are robust, and that effective controls are now in place to prevent, detect and correct any non compliance. We will seek to liaise with Internal Audit to ensure we take into account the findings of their follow up work in this area.</p>





04

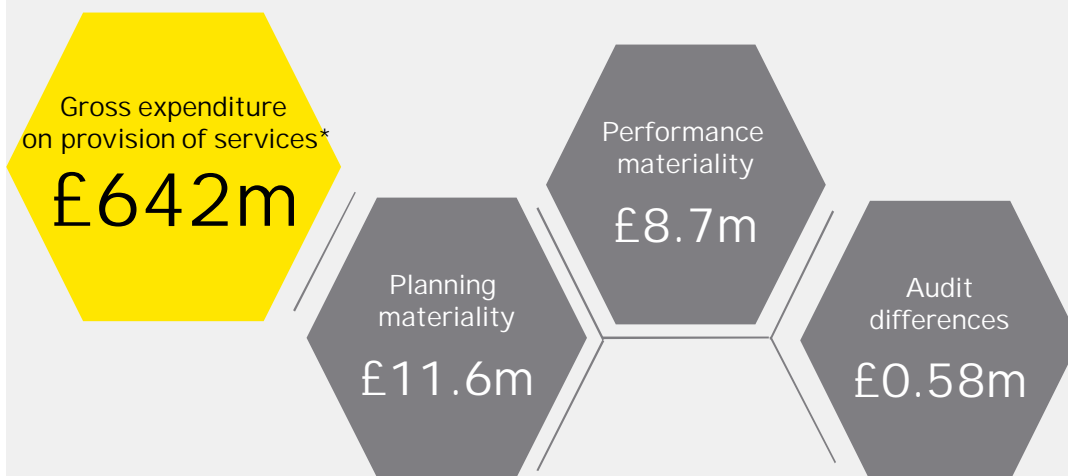
## Audit materiality



# Materiality

## Materiality

For planning purposes, materiality for 2018/19 has been set at £11.6m. This represents 1.8% of the Council's prior year gross expenditure on provision of services. It will be reassessed throughout the audit process. We have set materiality using gross revenue expenditure as our expectation is that users of the Council's accounts are focussed on how it uses its resources to provide services to local people. We have used 1.8% based on our assessment of the Council's financial position, levels of public interest, lack of planned reorganisations and sources of borrowing. We have provided supplemental information about audit materiality in Appendix C.



\*Figure used to calculate materiality excludes a small number of non-recurring items.

We request that the Governance 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 £8.664m which represents 75% of planning materiality. The rationale for using 75% is based on the anticipation of identifying few or no errors during the audit. This expectation has been built on our experience of the Council in prior years.

**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 comprehensive income and expenditure statement, balance sheet, housing revenue account and collection fund. Other uncorrected misstatements, such as reclassifications and misstatements in the cashflow statement and movement in reserves statement or disclosures, and corrected misstatements will be communicated to the extent that they merit the attention of the Committee, or are important from a qualitative perspective.

**Specific materiality** – We have also set a materiality of £1k for remuneration disclosures, related party transactions, members' allowances and exit packages, which 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 areas.



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.

For 2018/19 we plan to follow a substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

### 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 Governance Committee.

### Internal audit

We regularly meet with the Chief Internal Auditor, 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 work, where they raise issues that could have an impact on the financial statements, the Annual Governance Statement of the Narrative Statement.



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## Audit team



# Audit team

## Audit team structure:

Client Service  
Partner

Helen Thompson  
Associate  
Partner



Helen Thompson  
Associate Partner  
HThompson2@uk.ey.com



David White  
Manager  
dwhite@uk.ey.com



Shabbir Hussain  
Senior  
shabbir.hussain@uk.ey.com

## Working together with the Council

We are working together with officers to identify continuing improvements in communication and processes for the 2018/19 audit.

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

## Changes to the audit team

David White has joined the audit as Manager. David has extensive public sector audit experience, including as Manager of other local Unitary Councils.

Shabbir Hussain has joined the audit as Senior. Shabbir has worked for EY for 5 years, leading teams across a range of clients.

## Use of specialists

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

Area	Specialists
Valuation of Land and Buildings	Southampton CC in house property valuers (management specialist)
Pensions disclosure	Aon Hewitt (management specialist) PwC (consulting actuary) and EY Actuaries (auditor specialists)
PFI	EY Internal PFI Specialist (auditor specialist)

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, consider 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.





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## Audit timeline





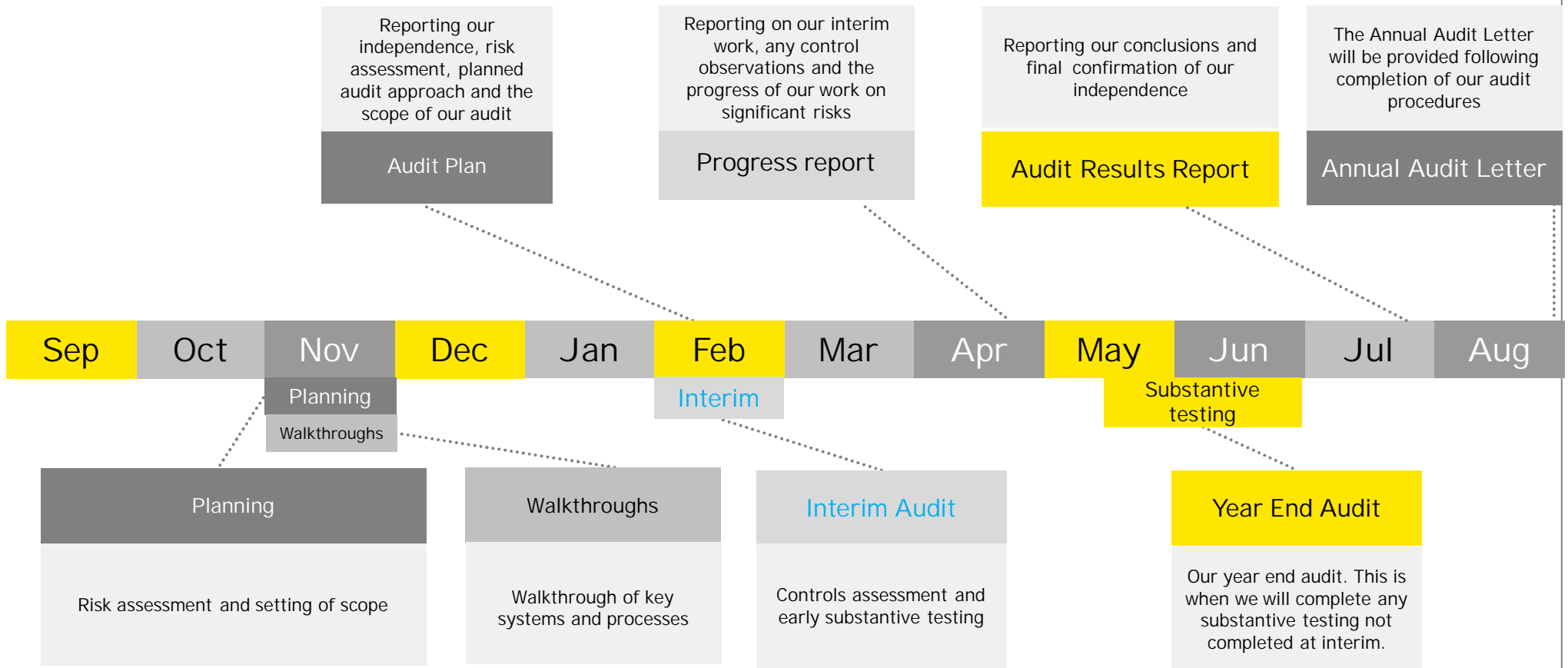
# Audit timeline

## 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 2018/19.

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





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
<ul style="list-style-type: none"> <li>▶ The principal threats, if any, to objectivity and independence identified by Ernst &amp; Young (EY) including consideration of all relationships between the you, your affiliates and directors and us;</li> <li>▶ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review;</li> <li>▶ The overall assessment of threats and safeguards;</li> <li>▶ Information about the general policies and process within EY to maintain objectivity and independence.</li> <li>▶ Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard</li> </ul>	<ul style="list-style-type: none"> <li>▶ 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;</li> <li>▶ Details of non-audit services provided and the fees charged in relation thereto;</li> <li>▶ 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;</li> <li>▶ Written confirmation that all covered persons are independent;</li> <li>▶ 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;</li> <li>▶ Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and</li> <li>▶ An opportunity to discuss auditor independence issues.</li> </ul>

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 Helen Thompson, 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 FRC's ES or the National Audit Office's Auditor Guidance Note 01 and the services have been approved in accordance with your policy on pre-approval. The ratio of non-audit fees to audit fees is not permitted to exceed 70%.

At the time of writing, no non-audit services have been undertaken, therefore the current ratio of non-audit fees to audit fees is zero. No additional safeguards are required.

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.

## Relationships, services and related threats and safeguards

### 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 2018

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 2018 and can be found here:

<https://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2018>



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# Appendices



## Appendix A

### Fees

Public Sector Audit Appointments Ltd (PSAA) has published the fee scale for the audit of the 2018/19 accounts of opted-in principal local government and police 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 requirements of the Code of Audit Practice and supporting guidance published by the National Audit Office, the financial reporting requirements set out in the Code of Practice on Local Authority Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.

	Planned fee 2018/19	Scale fee 2018/19	Final Fee 2017/18
	£	£	£
Total Fee – Code work	109,891	109,891	154,362*
Certification of claims and returns (housing benefits)	-	-	19,524
<b>Total fees</b>	<b>109,891</b>	<b>109,891</b>	<b>173,886</b>

The agreed fee presented is based on the following assumptions:

- ▶ Officers meeting the agreed timetable of deliverables;
- ▶ 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.

All fees exclude VAT

\* The total includes a proposed scale fee variation of £11,647, for additional work relating to:

- the matters giving rise to the 'except for' conclusion on the Council's proper arrangements to secure economy, efficiency and effectiveness in its use of resources;
- correspondence related to a formal objection; and
- involvement of an auditor's specialist in the audit of property valuations.

The fee variation has been agreed with management but remains subject to agreement with PSAA.

Our 2018/19 Code work includes additional planned procedures highlighted in section two of this report to address the new accounting requirements of IFRS 9 Financial Instruments and IFRS 15 Revenue from contracts with customers. As at the date of our planning report we are yet to review management's assessment of the impact of these standards, and so we cannot currently quantify the expected scale fee variation for these additional procedures. We will agree this with management, depending on the identified impact of the new standards. Any additional fee will be subject to approval by the PSAA.

To obtain sufficient assurance over housing benefits expenditure and subsidy income in the Council's financial statements, we will need to undertake some elements of the work which also form part of the housing benefit subsidy claim certification process. This work would previously have been covered by the certification fee and used additionally to provide assurance for the main audit. As we are no longer the reporting accountant for the Council's subsidy claim, we will need to consider the requirement for a scale fee variation to cover the performance of this work as part of the main audit for 2018/19.






## Appendix B

# Required communications with the Governance Committee

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







Our Reporting to you

Required communications	 What is reported?	  When and where
Terms of engagement	Confirmation by the Governance 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	<ul style="list-style-type: none"> <li>• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>• Significant difficulties, if any, encountered during the audit</li> <li>• Significant matters, if any, arising from the audit that were discussed with management</li> <li>• Written representations that we are seeking</li> <li>• Expected modifications to the audit report</li> <li>• Other matters if any, significant to the oversight of the financial reporting process</li> </ul>	Audit results report




## Appendix B

### Required communications with the Governance Committee (continued)

		 Our Reporting to you
Required communications	 What is reported?	  When and where
Going concern	<p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>• Whether the events or conditions constitute a material uncertainty</li> <li>• Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>• The adequacy of related disclosures in the financial statements</li> </ul>	Audit results report
Misstatements	<ul style="list-style-type: none"> <li>• Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation</li> <li>• The effect of uncorrected misstatements related to prior periods</li> <li>• A request that any uncorrected misstatement be corrected</li> <li>• Corrected misstatements that are significant</li> <li>• Material misstatements corrected by management</li> </ul>	Audit results report
Fraud	<ul style="list-style-type: none"> <li>• Enquiries of the Governance Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>• Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>• A discussion of any other matters related to fraud</li> </ul>	Audit results report
Related parties	<ul style="list-style-type: none"> <li>• Significant matters arising during the audit in connection with the entity's related parties including, when applicable:</li> <li>• Non-disclosure by management</li> <li>• Inappropriate authorisation and approval of transactions</li> <li>• Disagreement over disclosures</li> <li>• Non-compliance with laws and regulations</li> <li>• Difficulty in identifying the party that ultimately controls the entity</li> </ul>	Audit results report




## Appendix B

### Required communications with the Governance Committee (continued)

			 Our Reporting to you
Required communications	 What is reported?	 When and where	
Independence	<p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> <li>• The principal threats</li> <li>• Safeguards adopted and their effectiveness</li> <li>• An overall assessment of threats and safeguards</li> <li>• Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul>	<p>Audit Planning Report</p> <p>Audit Results Report</p>	
External confirmations	<ul style="list-style-type: none"> <li>• Management's refusal for us to request confirmations</li> <li>• Inability to obtain relevant and reliable audit evidence from other procedures</li> </ul>	<p>Audit results report</p>	
Consideration of laws and regulations	<ul style="list-style-type: none"> <li>• 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</li> <li>• Enquiry of the Governance Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Committee may be aware of</li> </ul>	<p>Audit results report</p>	
Internal controls	<ul style="list-style-type: none"> <li>• Significant deficiencies in internal controls identified during the audit</li> </ul>	<p>Management letter / Audit results report</p>	
Representations	<p>Written representations we are requesting from management and/or those charged with governance</p>	<p>Audit results report</p>	
Material inconsistencies and misstatements	<p>Material inconsistencies or misstatements of fact identified in other information which management has refused to revise</p>	<p>Audit results report</p>	

## Appendix B

### Required communications with the Governance Committee (continued)

			 Our Reporting to you
Required communications	 What is reported?	 When and where	
Auditors report	<ul style="list-style-type: none"> <li>Any circumstances identified that affect the form and content of our auditor's report</li> </ul>	Audit results report	
Fee Reporting	<ul style="list-style-type: none"> <li>Breakdown of fee information when the audit plan is agreed</li> <li>Breakdown of fee information at the completion of the audit</li> <li>Any non-audit work</li> </ul>	Audit planning report Audit results 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.
- Reading other information published with the financial statements, and reporting whether it is materially inconsistent with our understanding and the financial statements; and
- Maintaining auditor independence.

### 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 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.