Hampshire County Council

Audit planning report

Year ended 31 March 2019

January 2019

Building a better working world

Private and Confidential

22nd January 2019

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

Dear Members

Audit planning report

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as your auditor. Its purpose is to provide the Audit 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 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 21st February 2019 as well as understand whether there are other matters which you consider may influence our audit.

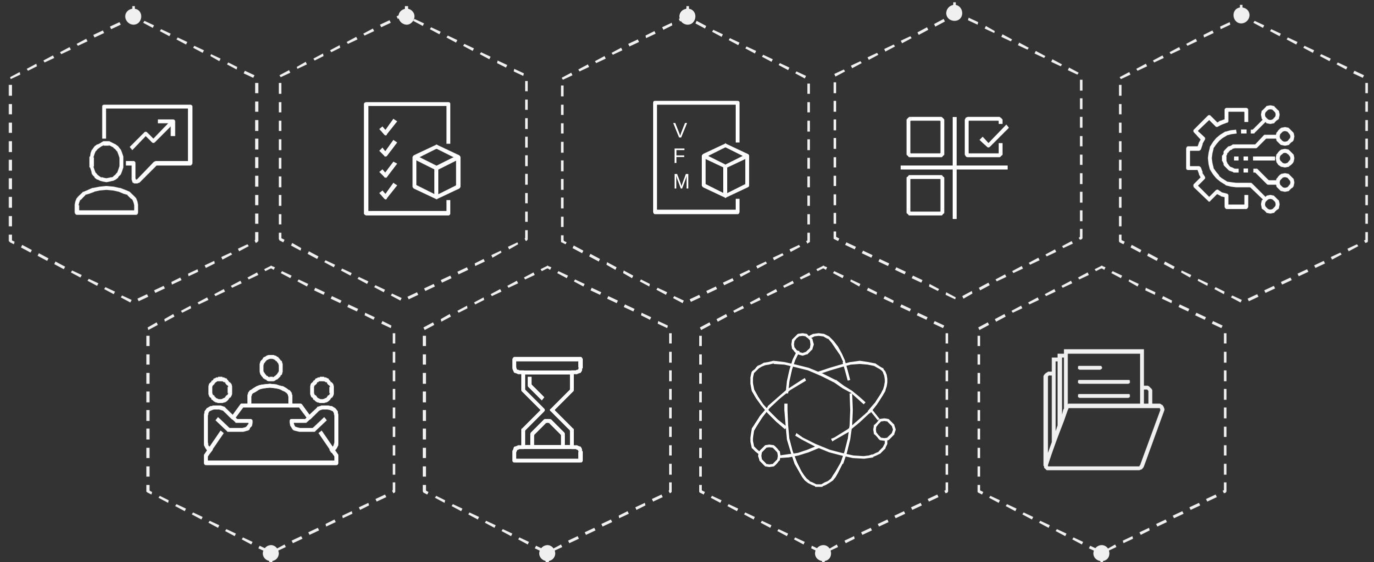
Yours faithfully

Maria Grindley

Associate Partner

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 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 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
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 - separately identified in 2018/19	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 and Investment Properties	Higher inherent risk	No change in risk or focus.	Property, Plant and Equipment Land and Buildings (L&B) and Investment Properties (IP) 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 and IP 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 and IP 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 2018/19 audit strategy

Risk / area of focus	Risk identified	Change from PY	Details
Pension Accounting	Higher inherent Risk	No change in risk of 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 2018 this totalled £1,340 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.
New Accounting Standards	Inherent risk	New risk identified this year.	IFRS 9 (Financial Instruments) and IFRS 15 (Revenue from contracts) apply from 1 April 2018. We will review the Council's assessment of the impact of these new standards to determine whether they have been appropriately implemented.

Materiality

Planning materiality

£38.2m

Planning materiality has been set at £38,222,000 which represents 1.8% of 2017/18 gross expenditure

Performance materiality

£28.7m

Performance materiality has been set at £28,666,000 which represents 75% of Planning Materiality

Audit differences

£1.9m

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 £1,911,000. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit 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 Hampshire County 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 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 2019.

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.

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 2017-18 financial statements:

Cost of services expenditure: £2,028 million

PPE additions: £167.7million

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.

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

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?
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.	We will: • Consider the competence, capability and objectivity of the Council's 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 valuation basis is appropriate and the accounting entries are correct; and • Review assets that are not subject to valuation in 2018/19 to confirm the remaining asset base is not materially misstated.

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 2018 this totalled £1,340 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. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	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; • 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.

Other areas of audit focus (continued)

What is the risk/area of focus?	What will we do?
New Accounting standards	
IFRS 9 financial instruments This new accounting standard is applicable 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: • Review 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 whether relevant assets have been appropriately classified and valued; • Review new expected credit loss model impairment calculations for assets; and • Ensure that, subject to materiality, additional disclosure requirements have been met.
IFRS 15 Revenue from contracts with customers This new accounting standard is applicable 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 local government revenue and how they should be recognised. The impact on the County Council’s accounting is likely to be limited as large revenue streams like council tax 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: • Review 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 revenue streams, and where the standard is relevant test to ensure revenue is recognised when (or as) it satisfies a performance obligation; and • Ensure that, subject to materiality, additional disclosure requirements have been met.

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 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.

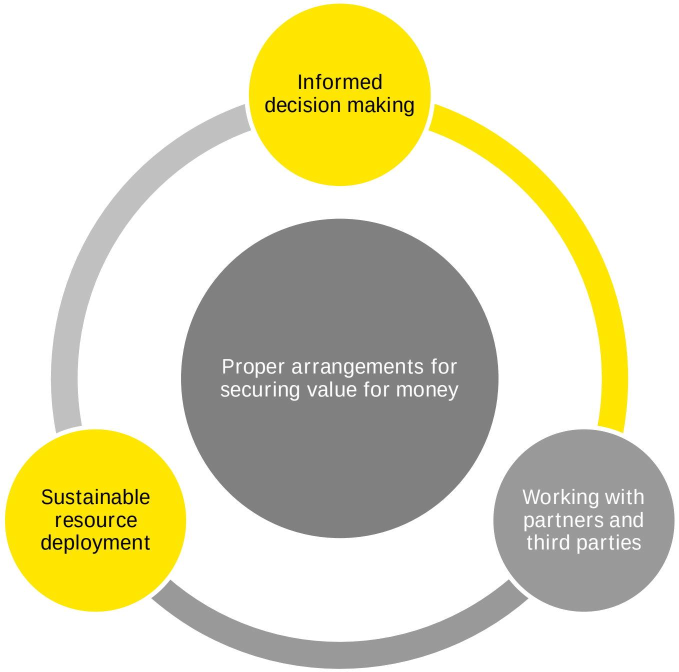
In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

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 the Council to consider the impact of Brexit on its future service provision, medium-term financing and investment values. Although the precise impact cannot yet be modelled, we anticipate that Authorities will be carrying out scenario planning and that Brexit and its impact will feature on operational risk registers.

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.



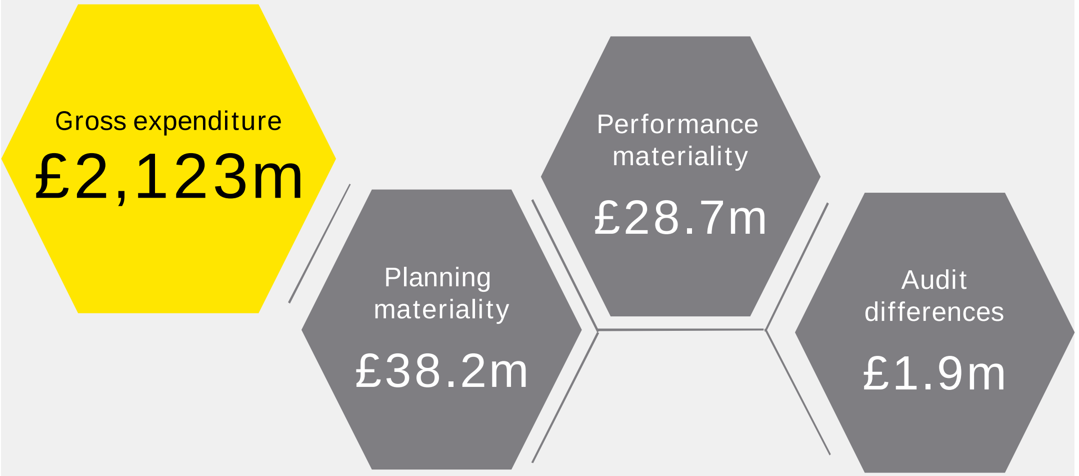
04 Audit materiality

Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2018/19 has been set at £38,222,000. This represents 1.8% of the Council's prior year gross expenditure. It will be reassessed throughout the audit process and once the draft 2018/19 statements have been prepared. 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 £28,666,000 which represents 75% of planning materiality. We apply 75% when it is not an initial audit and we have a sound understanding of the entity and past experience with the engagement indicates that a higher risk of misstatement is unlikely.

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.

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;
- SWIFT social care; and
- CONFIRM highway maintenance.

We will use staff with specialised knowledge from EY's Financial Audit IT (FAIT) team to assist with our work on IT processes and controls.

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.

06 Audit team

Audit team

Audit team structure:

Maria Grindley*
Associate Partner

Martin Young
Manager

Jack Dunkley
Assistant Manager

Maria Davison
Senior

EY Properties (as applicable)

EY Actuaries

EY Financial Audit IT (FAIT)

* Key Audit Partner

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.

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 (if necessary)

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 2018/19.

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.

Audit phase	Timetable	Audit committee timetable	Deliverables
Planning: Risk assessment and setting of scopes.	November		
Walkthrough of key systems and processes	November - December		
Testing of routine processes and controls	February	Audit Committee	Audit Planning Report
FAIT IT Systems Testing visit 1	February		
Interim audit testing	February - March		
FAIT IT Systems Testing visit 2	April		
Year end audit Audit Completion procedures	June/July	Audit Committee	Audit Results Report Audit opinions and completion certificates
Year end audit Audit Completion procedures	July / August	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 Maria Grindley, 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 48%. All fees are set out in Appendix A.

The only non-audit fees relate to a Readiness Assessment and independent Service Organisation Controls Type 1 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. Preparation in 2018/19 is in the following phases:

- the Council has asked us to perform a 'Readiness Assessment' at the IBC (also known as a 'Gap Assessment'). We will identify key risks, associated controls and identify any gaps in existing controls;
- on completion of the Readiness Assessment (and any necessary remediation by the IBC) we have been asked to perform an independent Service Organisation Controls (SOC) 1 Type 1 assurance engagement as at 31st March 2019. This will 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 1 engagement, our review will focus on the design of controls only as at 31st March 2019. We expect to issue our ISAE 3402 Type 1 report in April 2019.

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 received.

In subsequent years (i.e. 2019/20 and future years), 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.

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.

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 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:

http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2018

09 Appendices

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 2018/19	Scale fee 2018/19	Final Fee 2017/18
		£	£
Total Fee	89,720*	89,720*	116,519
Total audit	89,720*	89,720*	116,519
Other non-audit services**	43,000	N/A	N/A
Total other non-audit services	43,000	N/A	N/A
Total fees	132,720		116,519

All fees exclude VAT

*PSAA has set the 2018/19 fee scale on the basis that individual scale audit fees for all opted-in bodies have been reduced by 23 per cent from the fees applicable for 2017/18. This gives opted-in bodies the benefit of the cost savings achieved in the recent audit procurement.

**Non audit services relate the Readiness Assessment and independent Service Organisation Controls Type 1 Assurance Report for the Hampshire Integrated Business Centre (IBC) only. For further details, see Section 8 (page 28). The fee is being funded by the Shared Services Partnership not directly by Hampshire County Council

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.

Appendix B

Required communications with the Audit Committee

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

		Our Reporting to you
Required communications	What is reported?	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

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	Audit results report
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

Appendix C

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.

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.