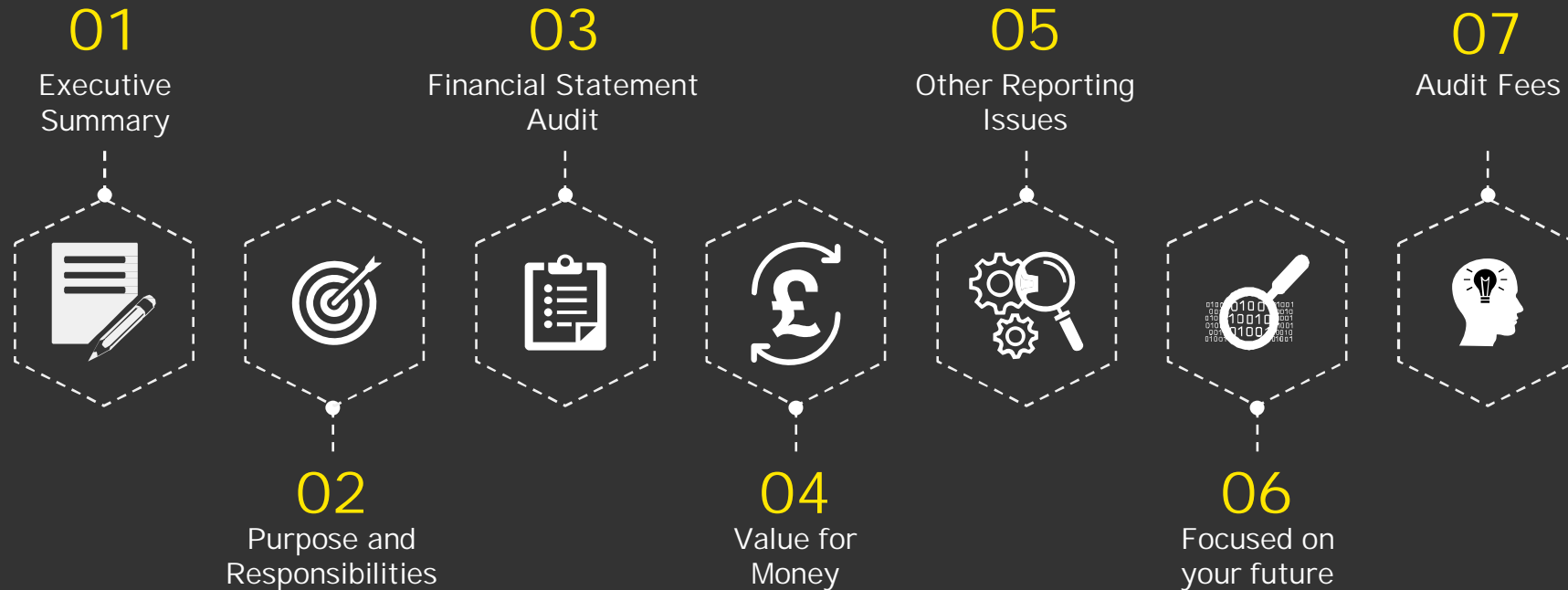


Fareham Borough  
Council

Annual Audit Letter for the year  
ended 31 March 2019

August 2019

# Contents



Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website ([www.psa.co.uk](http://www.psa.co.uk)).

This 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 (updated April 2018)' issued by PSAA set 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 statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities and Terms of Appointment. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.



# 01 Executive Summary

## Executive Summary

We are required to issue an annual audit letter to Fareham Borough Council (the Council) following completion of our audit procedures for the year ended 31 March 2019.

Below are the results and conclusions on the significant areas of the audit process.

| Area of Work  | Conclusion  |
|---|---|
| Opinion on the Council's:   | Unqualified – the financial statements give a true and fair view of the financial position of the Council as at 31 March 2019 and of its expenditure and income for the year then ended |
| ▶ Financial statements  |   |
| ▶ Consistency of other information published with the financial statements                  | Other information published with the financial statements was consistent with the Annual Accounts.  |
| Concluding on the Council's arrangements for securing economy, efficiency and effectiveness | We concluded that you have put in place proper arrangements to secure value for money in your use of resources.   |

| Area of Work  | Conclusion   |
|---|--|
| Reports by exception:   |  |
| ▶ Consistency of Governance Statement   | The Governance Statement was consistent with our understanding of the Council. |
| ▶ Public interest report  | We had no matters to report in the public interest.                            |
| ▶ Written recommendations to the Council, which should be copied to the Secretary of State                  | We had no matters to report.   |
| ▶ Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014 | We had no matters to report.   |

| Area of Work   | Conclusion  |
|--|---|
| Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA). | The Council is below the specified audit threshold of £500mn. Therefore, we did not perform any audit procedures on the consolidation pack. |

## Executive Summary (cont'd)

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As a result of the above we have also:

| Area of Work  | Conclusion  |
|---|---|
| Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.  | Our Audit Results Report was issued on 11 July 2019 |
| Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice. | Our certificate was issued on 31 July 2019          |

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Kevin Suter  
Associate Partner  
For and on behalf of Ernst & Young LLP



## 02 Purpose and Responsibilities

# Purpose and Responsibilities

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## The Purpose of this Letter

The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council.

We have already reported the detailed findings from our audit work in our 2018/19 Audit Results Report to the 22 July 2019 Audit and Governance Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.

## Responsibilities of the Appointed Auditor

Our 2018/19 audit work has been undertaken in accordance with the Audit Plan that we issued on 1 February 2019 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- ▶ Expressing an opinion:
  - ▶ On the 2018/19 financial statements; and
  - ▶ On the consistency of other information published with the financial statements.
- ▶ Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- ▶ Reporting by exception:
  - ▶ If the annual governance statement is misleading or not consistent with our understanding of the Council;
  - ▶ Any significant matters that are in the public interest;
  - ▶ Any written recommendations to the Council, which should be copied to the Secretary of State; and
  - ▶ If we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on your Whole of Government Accounts return. The Council is below the specified audit threshold of £500mn. Therefore, we did not perform any audit procedures on the return.

## Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement (AGS). In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.



03

## Financial Statement Audit



## Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health.

We audited the Council's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office and issued an unqualified audit report on 31 July 2019.

Our detailed findings were reported to the 22 July 2019 Audit and Governance Committee.

The key issues identified as part of our audit were as follows:

| Significant Risk   | Conclusion  |
|--|---|
| <p>Misstatements due to fraud or error</p> <p>The financial statements as a whole are not free of material misstatements whether caused by fraud or error.</p> <p>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.</p> | <p>We obtained a full list of journals posted to the general ledger during the year, and analysed these journals using criteria we set to identify any unusual journal types or amounts. We then tested a sample of journals that met our criteria and tested these to supporting documentation.</p> <p>We did not identify any material weaknesses in controls or evidence of material management override.</p> <p>We did not identify any instances of inappropriate judgements being applied.</p> <p>We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business</p> |

## Financial Statement Audit (cont'd)

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The key issues identified as part of our audit were as follows: (cont'd)

| Significant Risk   | Conclusion  |
|--|---|
| <p>Risk of fraud in revenue and expenditure recognition</p> <p>Auditing standards also required us to presume that there is a risk that revenue and expenditure may be misstated due to improper recognition or manipulation.</p> <p>We identified in our planning the incentive and opportunity to classify revenue spend as capital.</p> | <p>We:</p> <ul style="list-style-type: none"><li>• Documented our understanding of the controls relevant to this significant risk and considered they have been appropriately designed;</li><li>• Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in preparing the financial statements;</li><li>• Amended our sample sizes when testing capital additions to reflect the existence of this risk. Agreed samples to source documentation to ensure the classification was reasonable; and</li><li>• Reviewed whether management were inappropriately processing journals that transferred amounts from revenue to capital.</li></ul> <p>Our testing did not identify any material misstatements from revenue and expenditure recognition.</p> |

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## Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

| Other financial statement risk  | Conclusion   |
|---|--|
| <p>Valuation of land and buildings</p> <p>The fair value of Property, Plant and Equipment (PPE) 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.</p> <p>We focused on the following:</p> <ul style="list-style-type: none"> <li>• The adequacy of the scope of the work performed by the valuer including their professional capabilities;</li> <li>• The reasonableness of the underlying assumptions used by the Council's expert valuer; and</li> <li>• Assets not subject to valuation in 2018/19 to confirm whether the remaining asset base was not materially misstated</li> </ul>   | <p>We reviewed the instructions and data provided to the valuer by the Council. We identified no issues.</p> <p>We reviewed assets not subject to valuation in 2018/19 and confirmed that the remaining asset base was not materially misstated.</p> <p>We reviewed the relationship of the valuer to the Council and identified no issues.</p> <p>Our review of accounting entries at period end and those journals made in processing valuation adjustments did not reveal any instances of management intention to misreport the financial position. However, we did identify one item within Other Land and Buildings that was incorrectly calculated due to the omission of demolition and other fees in the valuation under the Depreciated Replacement Cost method. Management opted not to correct the accounts and we reported an unadjusted error of £72k in our Audit Results Report.</p>   |
| <p>Pension Asset valuation</p> <p>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.</p> <p>The Council's pension fund deficit contains material estimations and the Code requires that this asset be disclosed on the Council's balance sheet. At 31 March 2019 this totalled £59.224mn.</p> <p>The information disclosed is based on the IAS 19 report issued to the Council by the actuary to the County Council.</p> <p>Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.</p> | <p>We obtained assurances from the auditors of Hampshire Pension Fund that the information supplied to the actuary in relation to Fareham Borough Council was accurate and complete.</p> <p>We assessed and were satisfied with the competency and objectivity of the Council's actuaries: Aon Hewitt. We have reviewed the work of the actuaries. We challenged the actuarial valuation and found no indication of management bias in this estimate.</p> <p>Our review of accounting entries at period end and those journals made in processing valuation adjustments did not reveal any misstatements.</p> <p>We identified an adjusting event after reporting date relating to the pension fund liability, the effect of which increased past service cost and gross liability. The Council contacted the actuary for an updated IAS 19 report and amended the accounts. However, the new IAS 19 report did not take into account the effect of guaranteed minimum pension indexation thereby understating the net pension liability and we reported an unadjusted error of £351k in our Audit Results Report.</p> |

## Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

| Other financial statement risk   | Conclusion   |
|--|--|
| <p><b>NDR Appeals Valuation</b></p> <p>The Code of Practice on Local Authority Accounting requires the Council to account for NDR income (business rates) on an accruals basis. Therefore, the Council is required to consider a provision for the outcome of any appeals to business rates</p> <p>The Non Domestic Rates Appeals Provision is a material balance in the financial statements which requires a number of assumptions and judgements.</p>                               | <p>We have reviewed the calculation of the provision and confirmed that the calculation used a 4.7% national guideline to determine the estimate of outstanding appeals. This did not take into account local considerations. Our recalculation resulted in a £438k understatement. Management have opted not to amend the accounts and we reported this as an unadjusted error in our Audit Results Report.</p> <p>We confirmed that the provision considered unlodged appeals.</p> <p>We reviewed the assumptions, methods and models used by management's specialist. We identified no issues.</p> <p>Our post year-end review of appeals settled identified no issues.</p> |
| <p><b>New Accounting Standards – IFRS 9</b></p> <p>This new accounting standard is applicable for local authority accounts from the 2018/19 financial year and changed how financial assets are classified and measured, how the impairment of financial assets are calculated, and the disclosure requirements for financial assets.</p>  | <p>We reviewed the authority's implementation arrangements and impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19. We identified no issues.</p> <p>Financial instruments were appropriately classified and valued in line with the requirements of IFRS 9.</p> <p>We reviewed the new expected credit loss model impairment calculations for assets and identified no issues.</p> <p>Additional disclosure requirements were in line with the requirements of IFRS 9.</p>  |
| <p><b>New Accounting Standards – IFRS 15</b></p> <p>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.</p> <p>Where the standard is relevant, the recognition of revenue will change and new disclosure requirements introduced</p> | <p>We reviewed the authority's implementation arrangements and impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19. We identified no issues.</p> <p>For relevant revenue streams we confirmed that revenue was recognised appropriately, and disclosure requirements were in line with the requirements of IFRS 15 and the CIPFA Code.</p>  |

## Financial Statement Audit (cont'd)

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### Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

| Item                 | Thresholds applied  |
|----------------------|---|
| Planning materiality | <p>We determined planning materiality to be £1.377mn (2018: £1.333mn), which is 2% of gross revenue expenditure reported in the draft accounts of £57.589mn adjusted for other operating expenditure, other financing and investment expenditure and Housing Revenue Account Dwellings revaluation gain.</p> <p>We consider gross revenue expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.</p> |
| Reporting threshold  | <p>We agreed with the Audit and Governance Committee that we would report to the Committee all audit differences in excess of £0.068mn (2018: £0.066mn).</p>  |

We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include:

- ▶ Remuneration disclosures including any severance payments, exit packages and termination benefits.
- ▶ Related party transactions.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.

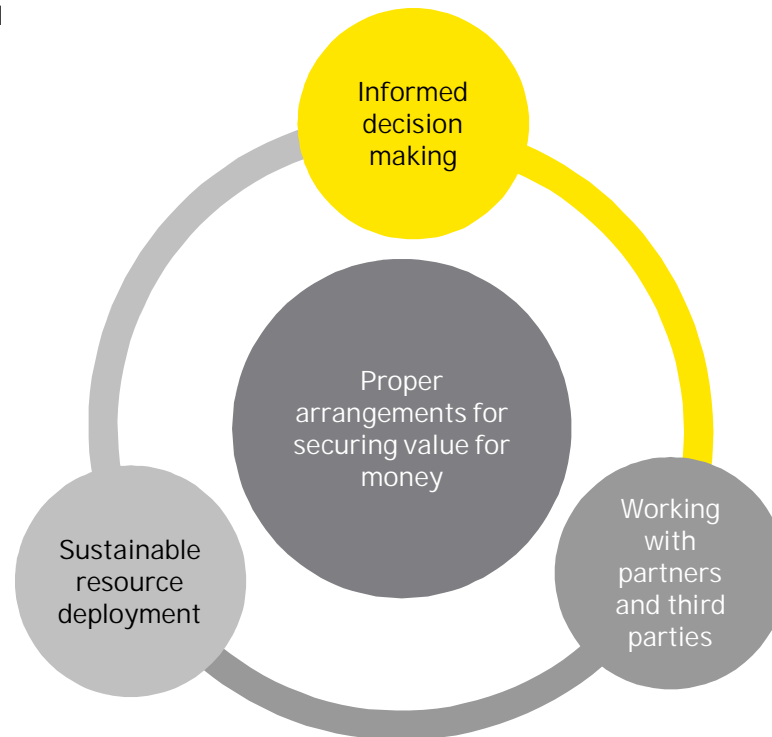


## 04 Value for Money

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

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.



We did not identify any significant risks in relation to these criteria.

We did not identify any significant weaknesses in the Council's arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We therefore issued an unqualified value for money conclusion on 31 July 2019.



## 05 Other Reporting Issues





## Other Reporting Issues

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### Whole of Government Accounts

We are required to perform the procedures specified by the National Audit Office on the accuracy of the consolidation pack prepared by the Council for Whole of Government Accounts purposes. The Council is below the specified audit threshold of £500mn. Therefore, we were not required to perform any audit procedures on the consolidation pack

### Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and did not identify any areas of concern.

### Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Council or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

### Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.

### Objections Received

We did not receive any objections to the 2018/19 financial statements from members of the public.

### Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

## Other Reporting Issues (cont'd)

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### Independence

We communicated our assessment of independence in our Audit Results Report to the Audit and Governance Committee on 22 July 2019. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

### Control Themes and Observations

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. We have adopted a fully substantive audit approach and have therefore not tested the operation of controls.

Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

Our audit did not identify any controls issues to bring to the attention of the Audit and Governance Committee.



06

Focused on your future



## Focused on your future

The Code of Practice on Local Authority Accounting in the United Kingdom introduces the application of new accounting standards in future years. The impact on the Council is summarised in the table below.

| Standard                  | Issue   | Impact  |
|---------------------------|---|---|
| IFRS 16 Leases            | <p>It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2020/21 financial year.</p> <p>Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet.</p> <p>There are transitional arrangements within the standard and although the 2020/21 Accounting Code of Practice for Local Authorities has yet to be issued, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.</p>   | <p>Until the 2020/21 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area.</p> <p>However, what is clear is that the Council will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Council must therefore ensure that all lease arrangements are fully documented.</p> |
| IASB Conceptual Framework | <p>The revised IASB Conceptual Framework for Financial Reporting (Conceptual Framework) will be applicable for local authority accounts from the 2019/20 financial year.</p> <p>This introduces;</p> <ul style="list-style-type: none"> <li>- new definitions of assets, liabilities, income and expenses</li> <li>- updates for the inclusion of the recognition process and criteria and new provisions on derecognition</li> <li>- enhanced guidance on accounting measurement basis</li> <li>- enhanced objectives for financial reporting and the qualitative aspects of financial information.</li> </ul> <p>The conceptual frameworks is not in itself an accounting standard and as such it cannot be used to override or disapply the requirements of any applicable accounting standards.</p> <p>However, an understanding of concepts and principles can be helpful to preparers of local authority financial statements when considering the treatment of transactions or events where standards do not provide specific guidance, or where a choice of accounting policies is available.</p> | <p>It is not anticipated that this change to the Code will have a material impact on Local Authority financial statements.</p> <p>However, Authorities will need to undertake a review to determine whether current classifications and accounting remains valid under the revised definitions.</p>   |



## 07 Audit Fees

## Audit Fees

The table below sets out the scale fee for 2018/19 and our final proposed audit fee.

| Description                            | Final Fee 2018/19<br>£ | Planned Fee 2018/19<br>£ | Scale Fee 2018/19<br>£ | Final Fee 2017/18<br>£ |
|--|------------------------|--------------------------|------------------------|------------------------|
| Total Audit Fee – Code work            | 38,545*                | 37,137                   | 37,137                 | 48,230                 |
| Total Audit Fee                        | 38,545                 | 37,137                   | 37,137                 | 48,230                 |
| Non-audit work<br>– Claims and returns | N/A                    | N/A                      | N/A                    | 18,391                 |

We confirm we have not undertaken any non-audit work outside of the PSAA's requirements.

\*The proposed final fee includes £1,026 in respect of additional work required to gain assurance over the restatement of gross income and gross expenditure within the various portfolios as a result of changes to Council's revised portfolio structure. The restatements affected the Comprehensive Income and Expenditure Statement, the Expenditure and Funding Analysis and the related notes.

The proposed final fee also includes £382 for work needed to be undertaken on aspects of housing benefit income and expenditure which would previously have been performed as part of HB certification. This had to be done separately this year as we are not the HBAP reporting accountant, therefore, increasing the scope where remuneration would previously have been under HBCOUNT principle through HB certification work. The detail of this work is as follows:

Module 2: Establishing that the system parameters had been appropriately updated to ensure the correct calculation of benefit awarded.

Module 5 - Ensuring that:

- (1) The system has been upgraded to the latest subsidy software, therefore, correctly producing figures for the subsidy claim – including supplementary adjustment reports - which is the basis of the annual income and any dr/cr compared to payments on account.
- (2) Reconciliation of the draft claim form to the Financial Statements.
- (3) The system has been balanced, and benefit awarded can be reconciled to (a) the subsidy claimed, and (b) reconciles to the general ledger and financial statements of the authority recording the expenditure recognised for the year.

This work was undertaken by audit staff, with supervision from the audit senior. The above are yet to be agreed with the S151 Officer and is subject to approval by PSAA.

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