

# Hart District Council Audit Update Report

Year ended 31 March 2022

07 October 2022



Hart District Council  
Civic Offices  
Harlington Way  
Fleet GU51 4AE

07 October 2022

Dear Audit Committee Members

We are pleased to attach our audit update report, summarising the status of our audit for the forthcoming meeting of the Audit Committee. We will update the Audit Committee at its meeting scheduled for 25 October 2022 on further progress to that date and explain the remaining steps to the issue of our final opinion.

The audit is designed to express an opinion on the 2022 financial statements and address current statutory and regulatory requirements. This report contains our findings related to the areas of audit emphasis, our views on Hart District Council's accounting policies and judgements and material internal control findings. Each year sees further enhancements to the level of audit challenge and the quality of evidence required to achieve the robust professional scepticism that society expects. We thank the management team for supporting this process.

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

We welcome the opportunity to discuss the contents of this report with you at the Audit Committee meeting on 25 October 2022.

Yours faithfully

Kevin Suter

Partner

For and on behalf of Ernst & Young LLP

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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 Audit Committee and management of Hart District 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 Hart District 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 Hart District 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 Executive Summary

## Executive Summary

### Scope update

In our audit planning report presented at the 25<sup>th</sup> May Audit Committee meeting, we provided you with an overview of our audit scope and approach for the audit of the financial statements. We updated our planning materiality assessment using the draft financial statements and have also reconsidered our risk assessment. Based on our materiality measure of 2% of gross expenditure on provision of services and 75% of planning materiality, our year-end testing is completed to the levels noted in the table below. The slight decrease is based on overall decrease in gross revenue expenditure of the Council in FY 2021-22 compared to FY 2020-21.

Materiality - Council	Audit Plan	Draft Financial Statements
Planning	£849k	£803k
Performance	£637k	£602k
Reporting	£42k	£40k

### Changes to reporting timescales

The Ministry of Housing, Communities and Local Government established regulations to extend the target date for publishing audited local authority accounts from 31 July to 30 September, for a period of two years (i.e. covering the audit of the 2020/21 and 2021/22 accounting years).

In December 2021, the Department for Levelling Up, Housing and Communities (DLUHC) announced proposals to extend the deadline for the publication of audited accounts to 30 November for 2021/22, which has been implemented by the The Accounts and Audit (Amendment) Regulations 2022.

We are working with the Council to deliver the audit in line with these timescales.



## Executive Summary

### Status of the financial statements audit

Our audit work in respect of the Council's opinion is in progress on all high risk areas that we highlighted to you in our Audit Plan presented at the 24 May 2022 Audit Committee. Details of audit progress in each of these areas is provided in Section 2 of the report.

Given that the audit process is still ongoing, we will continue to challenge the evidence provided and the final disclosures in the Narrative Report and Accounts which could influence our final audit opinion.

### Areas of audit focus

In our Audit Plan we identified a number of key areas of focus for our audit of the financial report of Hart District Council. This report sets out our observations and status in relation to these areas, including our views on areas which might be conservative and areas where there is potential risk and exposure. Our consideration of these matters and others identified during the period is summarised within the "Areas of Audit Focus" section of this report.

### Audit differences

As at the date of writing this report, we have no adjusted or unadjusted differences to bring to the attention of the committee. We are currently in discussions with the client regarding treatment of the housing company as well as valuation of assets which could lead to differences. We will provide a verbal update during the committee meeting in this area.

### Control observations

We have noted that the Council does not currently have an agreement with its housing management subsidiary, Hart Housing Property Management Ltd (HHPMC), for leasing the 41 flats in Edenbrook Apartments to HHPMC. HHPMC has entered into rental contracts with third parties and is collecting income from the tenants. We would expect the Council to ensure appropriate agreements are in place to capture the correct accounting treatment in the financial statements. Therefore, we have requested management to prepare an accounting paper to establish the nature of the arrangement in place and also ensure that this is accurately reflected in the accounts. This impacts the valuations of the asset which is discussed on Page 13 of the report.

As at the date of this report, we have no other control observations to bring to your attention.

### Other reporting issues

As part of our procedures, we review the information presented in the Annual Governance Statement for consistency with our knowledge of the Council. Our work in this area is currently ongoing. Therefore, we will provide an update at the next audit committee meeting upon finalisation of key audit risks.

We have not yet performed the procedures required by the National Audit Office (NAO) on the Whole of Government Accounts (WGA) submission. We are currently awaiting guidance from the NAO regarding the process for FY 2021-22. Therefore, our work on WGA will begin once the guidance is available.

We have no other matters to report.



## Executive Summary

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### Status of the audit – Value for Money

We have previously reported to the Committee our responsibilities in relation to the VFM for 2021/22. We are currently completing our work and assessing the Council against the three sub-criteria. This includes arranging meetings with senior officers to understand in detail the arrangements in place.

As at the date of this report we are not reporting any significant weakness in arrangements. However, we are considering the arrangement with Hart Housing Property Management Ltd (HHPMC) and the lack of completed agreement between the Council and HHPMC, as described on the previous page, and whether this indicates a risk of significant weakness.

We will be able to make this judgement when we have management's paper.

There are no other issues regarding our Value for money responsibilities to bring to your attention at this time.

### Independence

In our Audit Plan presented at the 25 May Audit Committee meeting we did not identify any independence issues.

There are no updates to report.





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## Areas of Audit Focus



## Significant risk

### 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 judgements are we focused on?

How management address to the risk of material misstatement due to fraud or error through the policies and procedures put in place at the Council.

#### Audit procedures

We:

- Identified fraud risks during the planning stages;
- Inquired of management about risks of fraud and the controls put in place to address those risks;
- Understood the oversight given by those charged with governance of management's processes over fraud;
- Considered of the effectiveness of management's controls designed to address the risk of fraud;
- Determined an appropriate strategy to address those identified risks of fraud.

#### What is the status of our work?

We are currently in the process of:

- Performing mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments in the preparation of the financial statements;
- Assessing the nature of any significantly unusual transactions identified; and
- Considering if management bias is present in the key accounting estimates and judgements in the financial statements.

Our testing in this area is currently ongoing and as at the date of this report, we have nothing to bring to the attention of the committee in this area.



# Fraud risk

## Inappropriate capitalisation of revenue expenditure due to fraud or error

### 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.

From our risk assessment, we have assessed that the risk manifests itself solely through the inappropriate capitalisation of revenue expenditure to improve the financial position of the general fund.

### What judgements are we focused on?

How management decides on appropriate capitalisation of revenue expenditure, including consideration of REFCUS.

### Audit procedures

Our approach focuses on the following:

- For significant capitalised additions (including REFCUS) we examine invoices, capital expenditure authorisations, leases and other data that support these additions. We review the sample selected against the definition of capital expenditure in IAS 16.
- Journal testing - we use our testing of Journals to identify high risk transactions, such as items originally recorded as revenue expenditure and subsequently capitalised.

### What is the status of our work?

Our work in this area is currently under review and we have gone back to the finance team with some follow up queries arising out of review.

As at the date of this report, we have nothing to bring to the attention of the committee in this area.

## Significant risk

### Valuation of Investment Properties

#### What is the risk?

The fair value of Investment Property (IP) has previously mainly been attributed to one asset however the Council purchased a further investment property in the current financial year which has increased the total projected year end balance to £17m. This represents significant balances in the Council's accounts and are subject to valuation changes and impairment reviews. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet which triggers the use of experts by management and EY likewise. Although the economic conditions may now be considered more stable, there are still uncertainties with regards to valuations impacting Investment Properties, which are held at Fair Value. With a greater value of properties held by the Council, we therefore have increased the risk on investment properties compared to prior year to significant risk for valuations as at 31 March 2022.

#### What judgements are we focused on?

We focus on aspects of the valuation which could have a material impact on the financial statements, primarily:

- Complex methodology and market based inputs e.g. fair value assets
- the assumptions and estimates used to calculate the valuation; and
- changes to the basis for valuing the assets.

#### Audit procedures

We:

- Consider the work performed by the Council's valuers, 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, or assessing comparative market information);
- Challenge key assumptions used by the valuers;
- Consider the annual cycle of valuations to ensure that assets have been valued annually as required by the Code for IP, and any significant changes notified to the valuer including changes in rental or other tenancy agreements;
- Consider the potential impact of current economic environment on valuation uncertainties while also evaluating the need to involve our internal specialist valuations team; and
- Test accounting entries have been correctly processed in the financial statements.

#### What is the status of our work?

We have involved our internal property valuation experts in this area and held discussions with the Council's external valuers to understand assumptions as well methodology adopted.

The work of the audit team is currently ongoing and we are also awaiting a final memo from our internal valuations team once we finalise the queries on two Property, Plant and Equipment assets discussed on Pg 13.

As at the date of this report, we have no points to highlight for the attention of the committee.

## 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 is the status of our work?
<p><b>Valuation of Property, Plant and Equipment (PPE)</b></p> <p>The value of DRC and EUV assets represents a significant balance in the Council's accounts and it is subject to revaluation changes and impairment reviews.</p> <p>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>DRC and EUV assets are subject to regular review by the external valuers - Capita.</p> <p>Valuation of these assets involves higher risk estimates due to the significant assumptions and judgments involved in their valuation, which triggers the use of experts by management and EY (where necessary). These estimates give scope for higher inherent risk in this area of accounts therefore we have identified PPE as an area of focus.</p>	<p>We are currently:</p> <ul style="list-style-type: none"> <li>Evaluating the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work;</li> <li>Sample testing 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 challenging the key assumptions used by the valuers;</li> <li>Evaluating 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. We also consider if there are any specific changes to assets that have occurred and whether these have been communicated to the valuers;</li> <li>Reviewing PPE assets not subject to valuation in 2021/22 to confirm that the remaining asset base is not materially misstated;</li> <li>Considering the potential impact of current economic conditions on valuation uncertainties;</li> <li>Considering changes to useful economic lives as a result of the most recent valuation; and</li> <li>Testing to confirm that accounting entries have been correctly processed in the financial statements.</li> </ul> <p>As at the date of this report, our work is ongoing. We have two issues at the date of drafting this report which we are discussing with management:</p> <ul style="list-style-type: none"> <li>Edenbrook Apartments - There is not currently in place a signed contract or agreement between the Council and Hart Housing Property Management Ltd (HHPMC) regarding the management of this asset. We are consequently unable to progress our work on valuation of the asset. This is because the valuation depends on several factors such as the leasing agreement in place, ownership of the asset and also the arrangement around income retention which is currently unclear due to the lack signed agreement. We are currently awaiting a memo from management on the accounting treatment of the asset and we aim to involve our internal valuers while liaising with the Council and the external valuers to evaluate the valuation methodology. We have already held various discussions with management on this issue.</li> <li>Civic Offices - We have verbally communicated another potential difference in valuation flagged by our valuation team in advance of receiving a final report. This is due a difference in methodology whereby the external valuer have disregarded sublet income and valued a market rent based on a reduced rent per sq ft. Our internal valuers believe it should be valued on the basis of the sublet income that the Council currently receives until lease expiry before reverting a higher market rent reflecting a multi-let approach, which is what is being undertaken at the property currently.</li> </ul> <p>We are currently in discussions with management as well as the external valuer to progress our work in these areas and note that there may be other queries arising from our review process.</p>

# 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 is the status of our work?
<p><b>Pension Liability Valuation</b></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 is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2021 this totalled £30.06million.</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) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.</p>	<p>We have liaised with the auditors of Hampshire Pension Fund, to obtain assurances over the information supplied to the actuary in relation to Hart District Council and are currently awaiting their response.</p> <p>In addition, we are also:</p> <ul style="list-style-type: none"> <li>assessing the work of the Pension Fund actuary 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;</li> <li>evaluating the reasonableness of the Pension Fund actuary's calculations by comparing them to the outputs of our own auditor's actuarial model; and</li> <li>reviewing and testing the accounting entries and disclosures made within the Council's financial statements in relation to IAS19.</li> </ul> <p>As at the date of writing this report, we have nothing to bring to the attention of the committee in this area.</p>
<p><b>Accounting for Covid-19 grants</b></p> <p>Central Government have provided a number of different Covid-19 related grants to local authorities during the year which were new in the prior year i.e. 20/21. There are also funds that have been provided for the Council to disseminate to other bodies.</p> <p>Similar to prior year, the Council needs to review each of these to establish the correct accounting treatment. It needs to assess whether it is acting as a principal or agent, with the accounting to follow that decision. For those where the decision is a principal, it also needs to assess whether there are any outstanding conditions that may also affect the recognition of the grants as revenue during 2021/22. We continue to identify this area as high inherent risk given the number of issues identified in the prior year.</p>	<p>As part of our testing we have undertaken the following procedures and the work is currently subject to review:</p> <ul style="list-style-type: none"> <li>Reviewed the accounting guidance applied by the Council and assess whether the appropriate guidance was considered and correctly applied;</li> <li>Reviewed whether any conditions are attached to grants impacting their recognition;</li> <li>Assessed whether the accounting appropriately follows those judgements; and</li> <li>Ensured sufficient and appropriate disclosures are included in the accounts.</li> </ul> <p>As at the date of writing this report, we have nothing to bring to the attention of the committee in this area.</p>



## 03 Other reporting issues

## Other reporting issues

### Other powers and duties

We have a duty under the Local Audit and Accountability Act 2014 to consider whether to report on any matter that comes to our attention in the course of the audit, either for the Authority to consider it or to bring it to the attention of the public (i.e. “a report in the public interest”). As at the date of writing this report, we did not identify any issues which required us to issue a report in the public interest.

### Other matters

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we must tell you significant findings from the audit and other matters if they are significant to your oversight of the Council's financial reporting process. They include the following:

- Significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures;
- Any significant difficulties encountered during the audit;
- Any significant matters arising from the audit that were discussed with management;
- Written representations we have requested;
- Expected modifications to the audit report;
- Any other matters significant to overseeing the financial reporting process;
- Findings and issues around the opening balance on initial audits (if applicable);
- Related parties;
- External confirmations;
- Going concern;
- Consideration of laws and regulations; and
- Group audits

As at the date of this report we have nothing that we need to bring to the attention of the Audit Committee in respect of Other Matters.



## Other communications

### EY Transparency Report 2020

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 end 30 June 2021:

[EY UK Transparency Report 2021 | EY UK](#)

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