Hampshire Police & Crime Commissioner and Chief Constable

Annual Audit Letter for the year ended 31 March 2019

August 2019

Building a better working world

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.psaa.co.uk)

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 (updated April 2018)’ issued by 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 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. 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 the Police and Crime Commissioner (PCC) and Chief Constable (CC) 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 Authority's and Pension Fund's: ► Financial statements	Unqualified – the financial statements give a true and fair view of the financial position of the PCC and CC as at 31 March 2019 and of its expenditure and income for the year then ended.
► 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 Authority'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 PCC and CC.
► Public interest report	We had no matters to report in the public interest.
► Written recommendations to the Authority, 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 Authority's Whole of Government Accounts return (WGA).	We have not yet completed our work on the Authority's Whole of Government Accounts return, (WGA) – this is not yet due. We are satisfied that this work does not have a material effect on the financial statements or our value for money conclusion.

Area of Work	Conclusion
Issued a report to those charged with governance of the Authority communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 12 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.	We have not as yet issued our audit completion certificate. We cannot formally conclude the audit and issue an audit certificate until we have completed the work necessary to issue our assurance statement in respect of the Council's Whole of Government Accounts consolidation pack. We are satisfied that this work does not have a material effect on the financial statements or on our value for money conclusion.

We would like to take this opportunity to thank the Police and Crime Commissioner and Chief Constables' staff for their assistance during the course of our work.

Maria Grindley

Associate Partner

For and on behalf of Ernst & Young LLP

02 Purpose and Responsibilities

Purpose and Responsibilities

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 Authority.

We have already reported the detailed findings from our audit work in our 2018/19 Audit Results Report to the 23 July 2019 Joint Audit 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 Authority.

Responsibilities of the Appointed Auditor

Our 2018/19 audit work has been undertaken in accordance with the Audit Plan that we issued on 08 January 2019 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- Expressing an opinion:
  - On the 2018/19 financial statements, including the pension fund; and
  - On the consistency of other information published with the financial statements.
- Forming a conclusion on the arrangements the PCC and CC have 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 Authority;
  - Any significant matters that are in the public interest;
  - Any written recommendations to the PCC or CC, which should be copied to the Secretary of State; and
  - If we have discharged our duties and responsibilities as established by thy 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 you Whole of Government Accounts return.

Responsibilities of the Authority

The PCC and CC are responsible for preparing and publishing their statement of accounts accompanied by an Annual Governance Statement, (AGS). In the AGS, the PCC and CC report 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 PCC and CC are also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

03 Financial Statement Audit

Financial Statement Audit

Key Issues

The PCC and CC's Statement of Accounts are important tools for the Authorities to show how they have used public money and how they can demonstrate its financial management and financial health.

We audited the PCC and CC's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office and issued an [un]qualified audit report on 25 July 2019.

Our detailed findings were reported to the 23 July 2019 Joint Audit Committee.

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

Significant Risk	Conclusion
Misstatements due to fraud or error The financial statements as a whole are not free of material misstatements whether caused by fraud or error. As identified in ISA (UK and Ireland) 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. The risk of management override at the Authority is mainly through the possibility that management could override controls and manipulate in-year financial transactions that have an impact on the General Fund's medium to longer-term projected financial position. The risk is focused in non-routine transactions as they are not protected by system controls and the robust segregation of duties in routine transactions. These non-routine and estimation transactions are also more subjective and therefore more susceptible to management override. We are specific that at the Authority, this risk only manifests itself in any estimates and judgements that impact the General Fund.	We enquired of management about risks of fraud and the controls put in place to address those risks. We gained an understanding of the oversight given by those charged with governance of management's processes over fraud. We performed mandatory procedures, 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 utilised our data analytics capabilities to assist with our work, including carrying out testing on the Income and Expenditure accounts, and journal entry testing. We assessed journal entries for evidence of management bias and evaluate for business rationale. We did not identify any material weaknesses in controls or evidence of material management override. We have not identified any instances of inappropriate judgements being applied. We did not identify any other transactions during our audit which appeared unusual or outside of the Authority's normal course of business

Financial Statement Audit (cont'd)

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

Significant Risk	Conclusion
Risk of fraud in revenue and expenditure recognition 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 Authority, 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. As such we associate this risk with capital additions. There is a risk that management will inappropriately capitalise revenue expenditure to improve the financial position of the general fund. Capitalised revenue expenditure can be funded through borrowing with only minimal MRP charges hitting the general fund, deferring the expenditure for 30+ years when the borrowing is repaid. Due to the environment the Authority operates in there could be incentive to improve the general fund balance. As such we have focussed on significant additions to PPE and management's judgement as to what they recognise as capital and what they recognise as revenue spend	We have extended our testing of items capitalised in the year by raising our combined risk assessment. This means we will identify a larger sample of key items, as our testing threshold will be lowered, and select a large representative same through the use of our audit risk tables. For significant additions (including capitalised labour (staff costs), borrowing costs and other acceptable costs) we examined invoices, capital expenditure authorisations, leases and other data that supported these additions and ensured that the items are capital in nature, and did not include revenue items. We have designed additional journal tests to identify high risk journals that may be an indication of management override. We reviewed journals where management have capitalised expenditure outside the normal process. Specifically - where management have posted to additions from outside the capital codes; and - where management have manually posted to the capital codes from another expenditure code. Our testing has not identified any material misstatements from revenue and expenditure recognition specific to inappropriate capitalisation. Overall our audit work did not identify any issues or unusual transactions to indicate any misreporting of the Authority's financial position.

Financial Statement Audit (cont’d)

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

Other Risks	Conclusion
Implementation of IFRS 9 IFRS 9 financial instruments This new accounting standard is applicable for local authority accounts from the 2018/19 financial year and will change: • How financial assets are classified and measured; • How the impairment of financial assets are calculated; and • The disclosure requirements for financial assets. There are transitional arrangements within the standard; and the 2018/19 Cipfa Code of practice on local authority accounting provides guidance on the application of IFRS 9. However, until the Guidance Notes are issued and any statutory overrides are confirmed there remains some uncertainty on the accounting treatment.	There were a number of conversations with management over the option to irrevocably elect to account for equity instruments at fair value through other comprehensive income (FVOCI) and specifically that the strategic pooled funds that PCC hold meet the definition of an equity instrument. The PCC accepted EY’s position and subsequently processed an adjustment to show these assets as FV through Profit & Loss.
Implementation of IFRS 15 IFRS 15 Revenue from contracts with customers This new accounting standard is applicable for local authority accounts from the 2018/19 financial year. The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations. The 2018/19 Cipfa Code of practice on local authority accounting provides guidance on the application of IFRS 15 and includes a useful flow diagram and commentary on the main sources of LG revenue and how they should be recognised. The impact on local authority accounting is likely to be limited as large revenue streams like council tax, non domestic rates and government grants will be outside the scope of IFRS 15. However where that standard is relevant, the recognition of revenue will change and new disclosure requirements introduced.	We completed our review of the IFRS 15 assessment and agreed with the conclusions reached by the Authority.

Financial Statement Audit (cont'd)

Other Risks	Conclusion
Valuation of land and buildings The fair value of Property, Plant and Equipment (PPE) represent significant balances in the Authority'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.	The Authority's PPE is valued by the internal Valuers. We reviewed the instructions and data provided to the valuer by the Authority. We identified no issues. We reviewed the classification and valuation methods used and identified no issues. 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. We noted a difference in our analysis of assets not revalued in the year that was above our nominal amount therefore we have recorded as a misstatement. Management have chosen not to adjust due to materiality.
Pension Liability Valuation The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Hampshire County Council. The PCC and CC's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Authority's balance sheet. At 31 March 2019 this totalled £3.7 million. The information disclosed is based on the IAS 19 report issued to the PCC and CC by the actuary to the County Council and also the police pension fund. 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.	We assessed and are satisfied with the competency and objectivity of the Pension Fund's actuaries: Aon Hewitt. EY pensions team and PwC (Consulting Actuary to the NAO) have reviewed the work of the actuaries. We challenged the actuarial valuation and found no indication of management bias in this estimate. 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.

Financial Statement Audit (cont'd)

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	We determined planning materiality for the PCC Group to be £9.8m (2017/18: £8.2m) and for the CC to be £9m (2017/18: £7.4m) which is 1.8% of gross revenue expenditure reported in the accounts. We consider gross revenue expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Authority.
Reporting threshold	We agreed with the Joint Audit Committee that we would report to the Committee all audit differences in excess of £0.4m for the PCC (2017/18: £0.4m) and £0.45m for the CC (2017/18: £0.37m)

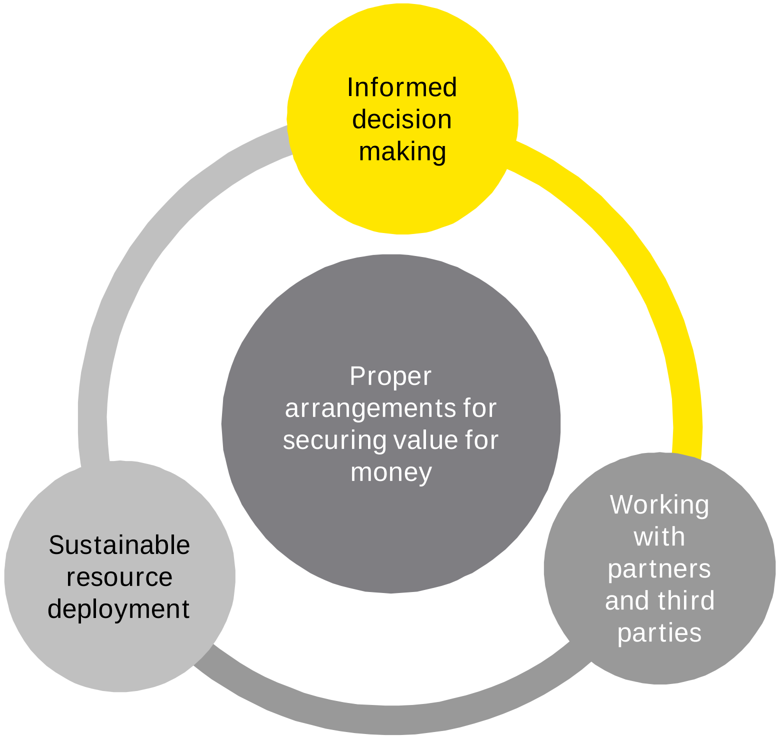
04 Value for Money

Value for Money

We are required to consider whether the Authority 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.

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 have performed the procedures outlined in our audit plan to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. We did not identify any significant weaknesses in the Authority’s arrangements.

We therefore issued an unqualified value for money conclusion on 25 July 2019.

05 Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

We are yet to complete our procedures on Whole of Government Accounts. We will issue a separate report on our conclusions in September 2019

Annual Governance Statement

We are required to consider the completeness of disclosures in the Authority'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 Authority 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 Authority 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.

Other Reporting Issues (cont'd)

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.

Independence

We communicated our assessment of independence in our Audit Results Report to the Joint Audit Committee on 23 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. 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.

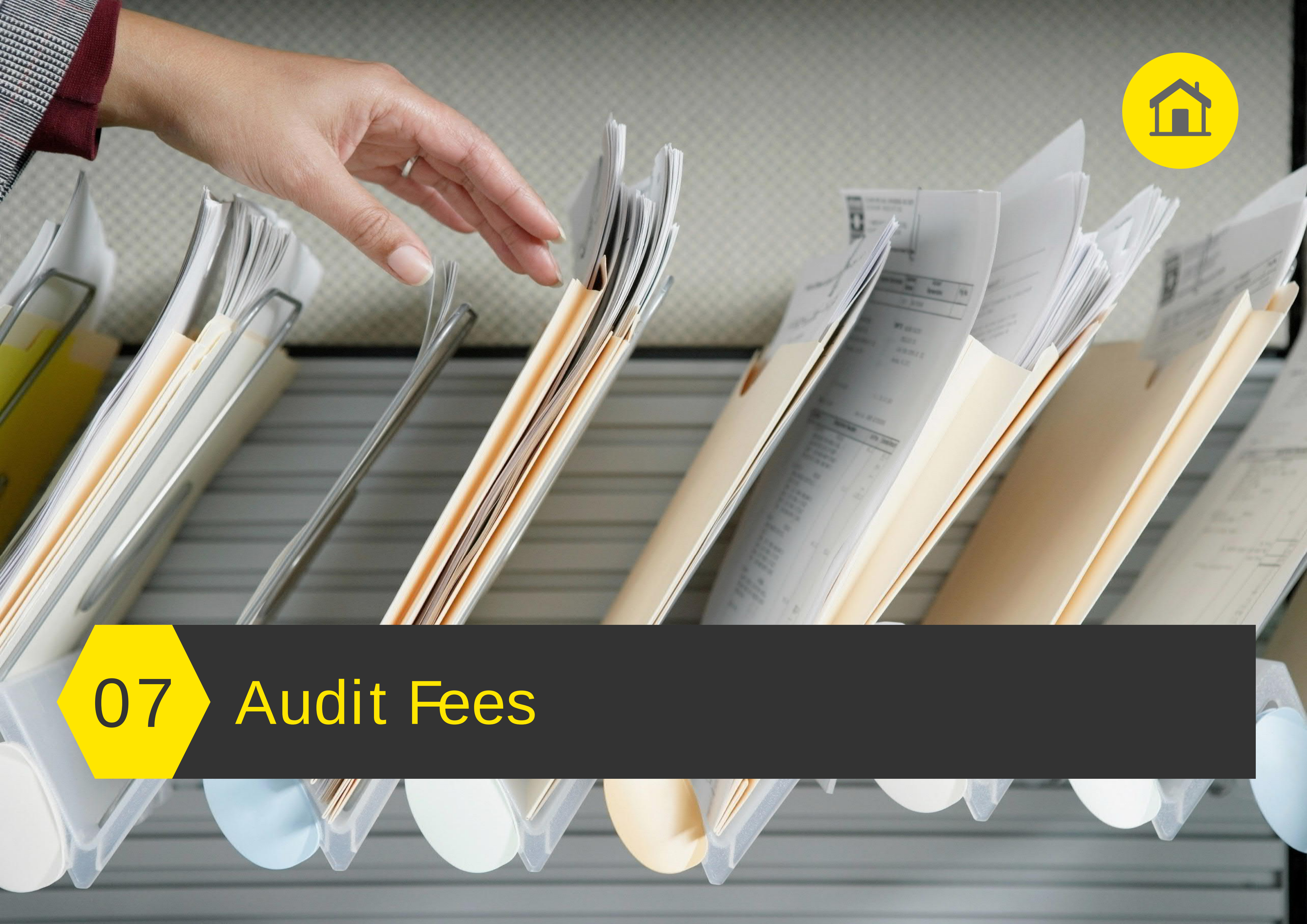
Our audit did not identify any controls issues to bring to the attention of the Joint Audit Committee.

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	It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2020/21 financial year. 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. 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.	Until the 2020/21 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area. However, what is clear is that the Authority will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Authority must therefore ensure that all lease arrangements are fully documented.
IASB Conceptual Framework	The revised IASB Conceptual Framework for Financial Reporting (Conceptual Framework) will be applicable for local authority accounts from the 2019/20 financial year. This introduces; – new definitions of assets, liabilities, income and expenses – updates for the inclusion of the recognition process and criteria and new provisions on derecognition – enhanced guidance on accounting measurement bases - enhanced objectives for financial reporting and the qualitative aspects of financial information. 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. 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.	It is not anticipated that this change to the Code will have a material impact on Local Authority financial statements. However, Authorities will need to undertake a review to determine whether current classifications and accounting remains valid under the revised definitions.



07 Audit Fees

Audit Fees

Our planned fee for 2018/19 is in line with the scale fee set by the PSAA and reported in our 08 January 2019 Audit Plan.

	Final Fee 2018-19	Planned Fee 2018-19	Final Fee 2017/18	Planned Fee 2017/18
	£	£	£	£
Total Audit Fee – PCC Code work	TBC*	31,751	41,235	41,235
Total Audit Fee – CC Code work	TBC*	14,438	18,750	18,750
Total fees	TBC*	46,189	59,985	59,985

All fees exclude VAT

*The final fee for the audit has yet to be concluded. Once we have concluded, we will discuss any additional fees with key contacts and also these will be subject to review by PSAA Ltd.

EY | Assurance | Tax | Transactions | Advisory

About EY
EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

ED None

EY-000070901-01 (UK) 07/18. CSG London.

In line with EY's commitment to minimise its impact on the environment, this document has been printed on paper with a high recycled content.

ey.com