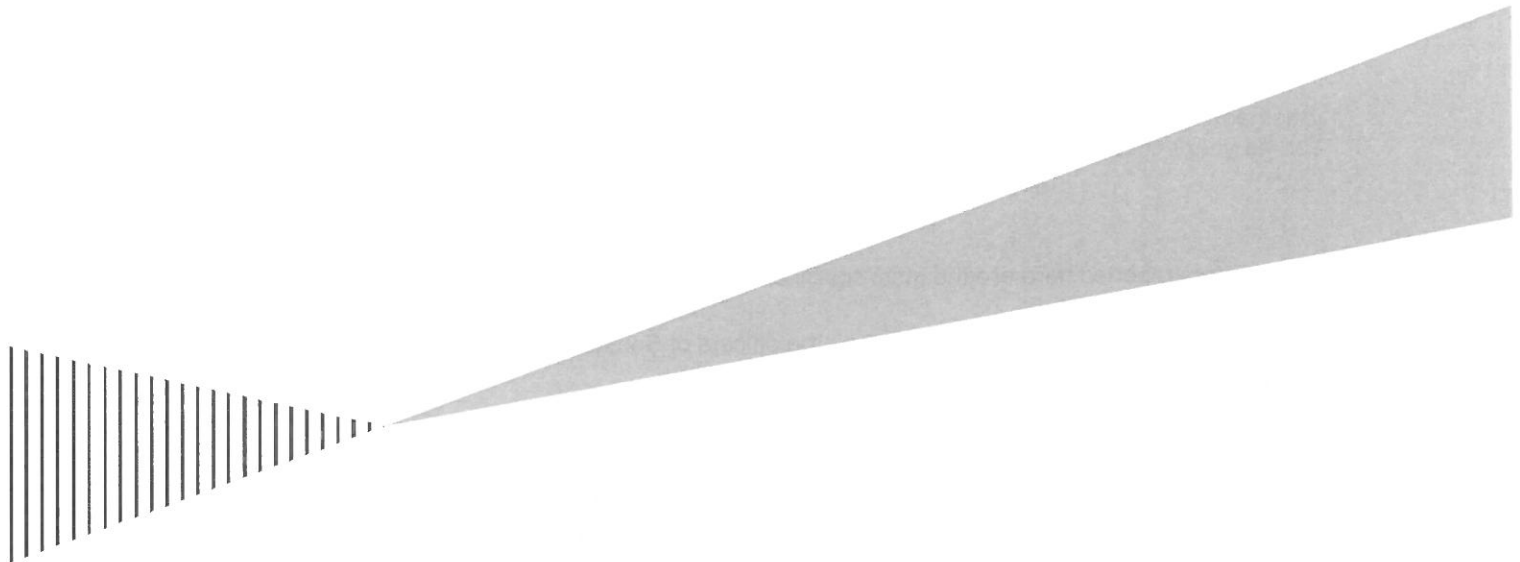


Annual Audit Letter

Southampton City Council

October 2014

Ernst & Young LLP



Building a better
working world



Ernst & Young LLP
Wessex House
19 Threefield Land
Southampton
SO14 3QB

Tel: + 44 23 8038 2000
Fax: + 44 23 8038 2001
ey.com

The Members
Southampton City Council
Civic Centre
Southampton
SO14 7LY

24 October 2014

Dear Members,

Annual Audit Letter

The purpose of this Annual Audit Letter is to communicate to the Members of Southampton City Council and external stakeholders, including members of the public, the key issues arising from our work which we consider should be brought to their attention.

We have already reported the detailed findings from our audit work to those charged with governance of the Council in the following reports:

Southampton City Council audit results report for the year ended 31 March 2014	Issued 4 September 2014 and presented to the Governance Committee on 15 September 2014
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The matters reported here are the most significant for the Authority.

I would like to take this opportunity to thank the officers of Southampton City Council for their assistance during the course of our work.

Yours faithfully

Kate Handy
For and behalf of Ernst & Young LLP
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In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the Chief Executive of each audited body and via the [Audit Commission's website](#).

The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's 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 Standing Guidance serves as our terms of appointment as auditors appointed by the Audit Commission. The Standing Guidance sets out additional requirements that auditors must comply with, over and above those set out in the Code of Audit Practice 2010 (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.

1. Executive summary

Our 2013/14 audit work has been undertaken in accordance with the Audit Plan we issued on 14 April 2014 and is conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

The Authority is responsible for preparing and publishing its Statement of Accounts, accompanied by the Annual Governance Statement. In the Annual Governance Statement, the Authority reports publicly on an annual basis on the extent to which it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period. The Authority is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

- ▶ forming an opinion on the financial statements;
- ▶ reviewing the Annual Governance Statement;
- ▶ forming a conclusion on the arrangements that the Authority has in place to secure economy, efficiency and effectiveness in its use of resources; and
- ▶ undertaking any other work specified by the Audit Commission.

Summarised below are the conclusions from all elements of our work:

Audit the financial statements of Southampton City Council for the financial year ended 31 March 2014 in accordance with International Standards on Auditing (UK & Ireland)	On 30 September 2014 we issued an unqualified audit opinion in respect of the Authority.
Form a conclusion on the arrangements the Authority has made for securing economy, efficiency and effectiveness in its use of resources.	On 30 September 2014 we issued an unqualified value for money conclusion.
Issue a report to those charged with governance of the Authority (the Audit Committee) communicating significant findings resulting from our audit.	On 4 September 2014 we issued our report in respect of the Authority.
Report to the National Audit Office on the accuracy of the consolidation pack the Authority is required to prepare for the Whole of Government Accounts.	We reported our findings to the National Audit Office on 30 September 2014.
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 complies with CIPFA / SOLACE guidance.	No issues to report.
Consider whether, in the public interest, we should make a report on any matter coming to our notice in the course of the audit.	No issues to report.

Determine whether any other action should be taken in relation to our responsibilities under the Audit Commission Act.

No issues to report.

Issue a certificate that we have completed the audit in accordance with the requirements of the Audit Commission Act 1998 and the Code of Practice issued by the Audit Commission.

On 30 September 2014 we issued our audit completion certificate.

2. Key findings

2.1 Financial statement audit

We audited the Authority's Statement of Accounts in line with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission. We issued an unqualified audit report on 30 September 2014.

In our view, the quality of the process for producing the accounts, including the supporting working papers was good. We believe that there is scope for further improvement and efficiencies in the process that we will be discussing with management in the run up to the preparation of next year's financial statements.

The main issues identified as part of our audit were:

Significant risk 1: Localisation of Business Rates

Issue:

- ▶ There were significant changes in the arrangements for business rates from April 2013. The detailed accounting arrangements were not clear, presenting an audit risk.
- ▶ One of the main changes was that individual councils needed to provide for rating appeals. This includes not only claims from 1 April 2013 but claims that relate to earlier periods. As appeals are made to the Valuation Office, Councils may not be aware of the level of claims and may also find it difficult to obtain sufficient information to establish a reliable estimate.

Findings:

- ▶ The Council's accounting for the new business rate framework, and its disclosures, are in accordance with the CIPFA Code of Accounting Practice.
 - ▶ The Council's provision benchmarks on the high side within its comparator groups. We have assessed the reasonableness of its methodology, and have not judged it to be an unreasonable estimation method.
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Significant risk 2: Minimum Revenue Provision

Issue:

- ▶ The Council reviewed the calculation of its Minimum Revenue Provision (MRP)

Finding:

- ▶ The Council made an adjustment of £3.9m, to amend the amount charged and audited in prior years.
 - ▶ Having reviewed the Council's previous accounting policies and MRP statements since 2007/08 we did not agree that it had previously made an error, which would be required under accounting standards to support this adjustment.
 - ▶ Therefore, we judged this to be a misstatement for 2013/14. We brought this to the attention of the Governance Committee, who decided not to amend the statements for the issue. This did not prevent us issuing an unqualified opinion as we did not judge the amount to be material.
-

Significant risk 3: Risk of management override

Issue:

- ▶ In all audits we recognise the risk that management is in a unique position to perpetrate fraud because of their ability to directly or indirectly manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be
-

operating effectively.

Finding:

- ▶ Our work did not identify indications of management override.
-

2.2 Value for money conclusion

We are required to carry out sufficient work to conclude on whether the Authority has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

In accordance with guidance issued by the Audit Commission, in 2013/14 our conclusion was based on two criteria:

- ▶ The organisation has proper arrangements in place for securing financial resilience; and
- ▶ The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

We issued an unqualified value for money conclusion on 30 September 2014.

We noted the following issues as part of our audit.

Key finding 1: Financial Pressures

- ▶ The Council has put in place arrangements to achieve financial resilience.
 - ▶ Looking forward, the forecast challenge for the Council is a cumulative £75m budget gap up to 2017/18, which is a significant pressure on its finances.
 - ▶ Processes are in place to address this gap. Significantly the Council has put in place arrangements so that the savings are more clearly linked to the overall medium term aims and objectives of the Council that have been formally agreed as of July 2014. This includes the strategy to transform the delivery of the Council services
 - ▶ Although the Council has historically achieved its service-based savings, it does not yet have a track record of achieving a transformational change programme. The programme is also an ongoing process, with elements continuing to be developed and delivered to an outline delivery timetable for the first tranches. As such, the scale of the savings achievable by the transformation programme are yet to be fully quantified and compared to the current overall forecast need. However, the programme has been specifically resourced, including being led by an officer experienced in implementing change management programmes. There is provision in the financial plans to re-invest the 2013/14 savings and other funds into the programme and other infrastructural changes where these are required, for example in changing IT infrastructure, to enable differing ways of working and engagement with the public. There is a commitment to ongoing communication and progress updates with Members.
 - ▶ The development of the transformation programme will require the continuing commitment of both officers and members. The transformation programme and its resultant savings is likely to remain a focus of our work in future years.
-

2.3 Objections received

We received no objections to the 2013/14 accounts from members of the public.

2.4 Whole of government accounts

We reported to the National Audit office, on 30 September 2014, the results of our work performed in relation to the accuracy of the consolidation pack the Authority is required to prepare for the whole of government accounts.

We reported only the uncorrected error regarding MRP referred to above, as this was above the NAO's reporting threshold of £1 million.

2.5 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 complies with CIPFA / SOLACE guidance.

We have no issues to report.

2.6 Use of other powers

We identified no issues during our audit that would necessitate using powers under the Audit Commission Act 1998, including reporting in the public interest.

3. Control themes and observations

As part of our audit of the financial statements, 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 communicated to those charged with governance at the Authority, as required, significant deficiencies in internal control.

We had no issues to report for 2013/14.

We reflected in our report the potential future challenge for the Council due to significant changes in the finance team. However, we highlighted the opportunity in these changes to bring a fresh perspective to the processes and content of the Statement of Accounts.

4. Audit Fees

A breakdown of our fee is shown below.

	Final fee 2013/14 £'000	Planned fee 2013/14 £'000	Scale fee 2013/14 £'000
Total Audit Fee – Code work	189,216	189,216	189,216
Certification of claims and returns ¹	29,036	29,036	29,036

Our actual fee is in line with the agreed fee.

We undertook no non-audit work at the Council in 2013/14.

Notes:

¹ Our fee for certification of grants and claims is yet to be finalised for 2013/14 as the work is ongoing. We plan to report this to those charged with governance within our Annual Certification Report for 2013/14

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Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

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