

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF EASTLEIGH BOROUGH COUNCIL

## Disclaimer of opinion

We were engaged to audit the financial statements of Eastleigh Borough Council for the year ended 31 March 2023. The financial statements comprise the:

- Movement in Reserves Statement,
- Comprehensive Income and Expenditure Statement,
- Balance Sheet,
- Cash Flow Statement,
- the related notes 1 to 54 including a summary of significant accounting policies,
- Collection Fund and the related notes 1 to 3.

The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2022/23 as amended by the Update to the Code and Specifications for Future Codes for Infrastructure Assets (November 2022).

We do not express an opinion on the accompanying financial statements of the Authority. Because of the significance of the matter described in the basis for disclaimer of opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

## Basis for disclaimer of opinion

The Accounts and Audit (Amendment) Regulations 2024 (Statutory Instrument 2024/907) which came into force on 30 September 2024 requires the accountability statements for this financial year to be approved not later than 13 December 2024.

The audit of the 2021/22 financial statements for the Authority was not completed for the reasons set out in our opinion on those financial statements dated 5 December 2024.

As set out in our '**report on the Authority's proper arrangements for securing economy, efficiency and effectiveness in the use of resources**' section of this audit report, our ability to perform the audit was impacted by the Authority's commercial investment which increased the complexity of the financial statements and the finance team's ability to produce and support materially accurate 2022/23 financial statements.

This, combined with the backstop date and the wider requirements of the local audit system reset, meant we did not have the required resources available to complete the detailed audit procedures that would be needed to obtain sufficient appropriate audit evidence to issue an unmodified audit report on the 2022/23 financial statements.

In addition, information was received during the course of the audit that indicated the potential for non-compliance with laws and regulations. Due to the imposed backstop date, we were unable to perform sufficient further audit work to determine whether this matter has any impact on the financial statements.

Therefore, we are disclaiming our opinion on the financial statements.

## **Matters on which we report by exception**

Notwithstanding our disclaimer of opinion on the financial statements, we have nothing to report in respect of whether the annual governance statement is misleading or inconsistent with other information forthcoming from the audit, performed subject to the pervasive limitation described above, or our knowledge of the Authority.

We report to you if:

- we issue a report in the public interest under section 24 of the Local Audit and Accountability Act 2014 (as amended)
- we make written recommendations to the audited body under Section 24 of the Local Audit and Accountability Act 2014 (as amended)
- we make an application to the court for a declaration that an item of account is contrary to law under Section 28 of the Local Audit and Accountability Act 2014 (as amended)
- we issue an advisory notice under Section 29 of the Local Audit and Accountability Act 2014 (as amended)
- we make an application for judicial review under Section 31 of the Local Audit and Accountability Act 2014 (as amended).

We have nothing to report in these respects.

## **Report on the Authority's proper arrangements for securing economy, efficiency and effectiveness in the use of resources**

We report to you if we are not satisfied that the Authority has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2023.

On the basis of our work, having regard to the Code of Audit Practice 2024 and the guidance issued by the Comptroller and Auditor General in November 2024, we have identified the following significant weaknesses in the Authority's arrangements for the year ended 31 March 2023.

### **Significant weaknesses in arrangements**

*We have identified four significant weaknesses in arrangements for the year ended 31 March 2023. These are:*

1. *Weaknesses relating to the capacity and expertise within the finance function to identify, assess and manage risks to the Authority's financial sustainability due to the complexity of the Authority's commercial property and housing development activities and associated level and nature of borrowing.*

#### Weakness identified

There is a need for further capacity and expertise in the Authority's finance team to support its increasingly complex financial planning and the significant pressure on the Council's finances over the medium term.

#### The evidence on which our view is based

The additional accounting, financial management and risk management complexities relative to the majority of lower tier local government bodies brought about by the commercial property and housing development activities of the Authority, and associated level of external borrowing, a significant proportion of which is held short-term. Changes in the wider UK economy at the reporting date, and specifically increased inflation, increased interest rates, and lower demand and falling house prices put further pressure on the Authority's finances as a result of its housing development activity.

### The impact on the Authority

The level of financial risk faced by the Authority may result in difficulties in obtaining affordable short-term finance or reductions in revenue and capital spending plans. Insufficient appropriate capability and capacity within the finance function increases the risk that identification, assessment and management of financial sustainability risks is insufficient.

### Action required by the Authority

The Authority should increase capacity within the finance function and other areas to better support its increasingly complex financial planning arrangements and scale of its commercial activity, particularly in relation to housing development and the need for strategic treasury management in respect of related borrowing. This should allow it to more quickly assess and articulate the impact of current and expected changes in market conditions on its financial plans and risks, take mitigating actions as necessary and report to members and other stakeholders in a greater level of detail. Increased capacity within finance and other areas of the Council will also be necessary to support the Council's proposal to re-establish and then properly maintain a Housing Revenue Account.

The level of financial risk faced by the Authority and the related need for further capacity in the Authority's finance team to support its increasingly complex financial planning is evidence of significant weaknesses in proper arrangements for how the body ensures that it identifies all the significant financial pressures that are relevant to its short and medium-term plans and builds these into them.

## *2. Value for Money issues arising from the Authority's nitrate credit trading scheme*

### Weakness identified

The Authority did not have a clear understanding of the accounting requirements of its nitrate credit trading scheme and the consequence of those on its medium-term financial planning arrangements, both prior to it entering into the initial purchase of land used to generate credits under the scheme and then after credits were actually sold.

### The evidence on which our view is based

Our review showed that the approach adopted for accounting for nitrates credits was not in accordance with the requirements of relevant accounting standards and The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, and the Authority has amended its financial statements in respect of this. The detailed consideration of the accounting requirements should have been undertaken prior to the Authority entering into the initial purchase of land used to generate credits under the scheme.

### The impact on the Authority

In not undertaking a detailed consideration of the accounting requirements prior to entering into the initial purchase of land the Authority risked its Medium-Term Financial Plan being prepared inaccurately and did not allow a fully informed decision to be taken on whether the scheme should be entered into.

### Action required by the Authority

The Authority should ensure that proper and comprehensive due diligence is undertaken to fully understand the potential accounting impacts of arrangements entered into that have a significant impact on the finances of the Authority prior to entering into those arrangements. This is particularly true for arrangements in new areas where accepted accounting practice has not yet been clearly established. This will provide a better understanding of the required accounting entries and disclosures in the Authority's financial statements and allow for the financial impacts of those arrangements to be accurately reflected in the Authority's medium term financial plans.

This is evidence of significant weaknesses in arrangements for:

- How the body ensures it makes properly informed decisions, supported by appropriate evidence and allowing for challenge and transparency. This includes

- arrangements for effective challenge from those charged with governance/audit committee.
- How the body ensures that it identifies all the significant financial pressures that are relevant to its short and medium-term plans and builds these into them.
3. *Governance and procurement risks associated with the One Horton Heath development.*

#### Weakness identified

During the course of the audit, instances of potential non-compliance with laws and regulations and other weaknesses in internal control relating to the Authority's One Horton Heath Housing development were brought to our attention. The matters related specifically to:

- Weaknesses in internal control over payments made to contractors.
- Breaches of contract standing orders and potential wider non-compliance with procurement law.
- Wider weaknesses in governance arrangements for the One Horton Heath development.

#### The evidence on which our view is based

An investigation into the matters by Internal Audit and further consideration of that investigation by EY specialists found the matters reported to be partially valid.

#### The impact on the Authority

Weaknesses exist in the internal control and governance of the One Horton Heath scheme, which exposes the Authority to risk of financial loss or fraud. Those weaknesses are potentially more pervasive across the Authority.

#### Action required by the Authority

The Authority should:

- Ensure it has a framework of necessary policies, procedures and training in place to identify and address the risk of fraud and carry out investigations to the standard required to enable enforcement if required.
- Broaden the scope of investigative work in relation to the potential non-compliance with laws and regulations and other weaknesses in internal control to more fully consider the potential impact of both the allegations and findings to date on decision making and governance for both the One Horton Heath development specifically, and the Authority more generally.
- Update relevant policies to explicitly consider the need to involve external audit where relevant and appropriate to do so.

This is evidence of significant weaknesses in arrangements for:

- How the body ensures it makes properly informed decisions, supported by appropriate evidence and allowing for challenge and transparency. This includes arrangements for effective challenge from those charged with governance/audit committee.
- How the body monitors and assesses risk and how the body gains assurance over the effective operation of internal controls, including arrangements to prevent and detect fraud.
- Where the body commissions or procures services, how the body ensures that this is done in accordance with relevant legislation, professional standards and internal policies, and how the body assesses whether it is realising the expected benefits.

4. *Capacity and expertise within the Internal Audit service, to respond to wide ranging investigations into potential non-compliance with laws and weaknesses in internal control*

#### Weakness identified

During 2023, potential non-compliance with laws and regulations and other weaknesses in internal control relating to the Authority's One Horton Heath Housing development were identified by management and brought to our attention. A review by EY specialists of the initial Internal Audit investigation into the matters identified highlighted weaknesses in the scope of Internal Audit work to investigate the allegations, the methodology applied and the depth and validity of evidence supporting findings and conclusions.

#### The evidence on which our view is based

The review by EY specialists of the Internal Audit investigation. A Capital Review of the Authority commissioned by the Department for Levelling-Up, Housing and Communities and undertaken by the Chartered Institute of Finance and Accountancy also recommended strengthening Internal Audit through enlarging the team or having specialised reviews.

#### The impact on the Authority

The Internal Audit function does not have the required expertise and capacity to comprehensively and promptly investigate and report on the potential non-compliance with laws and regulations and other weaknesses in internal control. The Internal Audit function does not have sufficient capacity and expertise to provide assurance over governance and internal control arrangements for the Authority's wider commercial activity.

#### Action required by the Authority

The Authority should:

- Ensure that Internal Audit has the required expertise and capacity to comprehensively and promptly investigate and report on potential non-compliance with laws and regulations and other weaknesses in internal control, and that findings are underpinned by detailed testing. Where investigative work undertaken suggests wider potential weaknesses in governance, internal control, non-compliance with law and regulation or material fraud the Authority should ensure that the scope of work is expanded to properly address and provide assurance in relation to this.
- Ensure that Internal Audit has the required expertise and capacity to provide assurance over governance and internal control arrangements for the Council's wider commercial activity, and in particular the One Horton Heath development given its scale and financial significance to the Council.

This is evidence of significant weaknesses in arrangements for how the body monitors and assesses risk and how the body gains assurance over the effective operation of internal controls, including arrangements to prevent and detect fraud.

### **Responsibility of the Chief Financial Officer**

As explained more fully in the Statement of the Chief Financial Officer's Responsibilities set out on page 11, the Chief Financial Officer is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2022/23 as amended by the Update to the Code and Specifications for Future Codes for Infrastructure Assets (November 2022), and for being satisfied that they give a true and fair view and for such internal control as the Chief Financial Officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Chief Financial Officer is responsible for assessing the Authority's ability to continue as a going concern, disclosing, as applicable, matters

related to going concern and using the going concern basis of accounting unless the Authority either intends to cease operations, or has no realistic alternative but to do so.

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

### **Auditor's responsibilities for the audit of the financial statements**

Our responsibility is to conduct an audit of the Authority's financial statements in accordance with International Standards on Auditing (UK) and to issue an auditor's report.

However, because of the matter described in the basis for disclaimer of opinion section of our report, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

We are independent of the Authority in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard and the Code of Audit Practice 2024 and we have fulfilled our other ethical responsibilities in accordance with these requirements.

### **Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources**

We have undertaken our review in accordance with the Code of Audit Practice 2024, having regard to the guidance on the specified reporting criteria issued by the Comptroller and Auditor General in November 2024, as to whether Eastleigh Borough Council had proper arrangements for financial sustainability, governance and improving economy, efficiency and effectiveness. The Comptroller and Auditor General determined these criteria as those necessary for us to consider under the Code of Audit Practice in satisfying ourselves whether Eastleigh Borough Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2023.

We planned our work in accordance with the Code of Audit Practice. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether, in all significant respects, Eastleigh Borough Council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We are required under Section 20(1)(c) of the Local Audit and Accountability Act 2014 (as amended) to satisfy ourselves that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

We are not required to consider, nor have we considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

### **Certificate**

We certify that we have completed the audit of the accounts of Eastleigh Borough Council in accordance with the requirements of the Local Audit and Accountability Act 2014 (as amended) and the Code of Audit Practice issued by the National Audit Office.

## Use of our report

This report is made solely to the members of Eastleigh Borough Council, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014 (as amended) and for no other purpose, as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

  


*Janet Dawson (Key Audit Partner)*  
*Ernst & Young LLP (Local Auditor)*  
*London*  
*5 December 2024*

The following footnote does not form part of our Auditor's Report.

Additional information related to the disclaimer of opinion is set out in our Completion Report for Those Charged with Governance dated 22 November 2024, available on the Authority's website, which includes further explanations about the implementation of the statutory instrument which led to the disclaimer of our opinion on the financial statements.