



## London Borough of Tower Hamlets

### Report to the Audit Committee on the audit for the year ended 31 March 2019

Issued on 17 January 2022 for the meeting on 27 January 2022 and re-issued on 20 January 2023 for the meeting on 26 January 2023  
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# Contents

## Final report

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1. Key messages	4
2. Our audit explained	10
3. Significant audit risks	12
4. Other areas of judgement	24
5. Use of resources	42
6. Control observations	50
7. Purpose of our report and responsibility statement	59

## Appendices

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A. Audit adjustments	61
B. Independence and fees	79
C. Our other responsibilities explained	81
D. Summary of the more significant updates since the issue of the January 2022 version of this report	82
E. Proposed wording of the modifications to our audit report	85
F. Draft management representation letter	89

# 1. Key messages

# Key messages

## The key messages in this report

We have pleasure in presenting our report to the audit committee of the London Borough of Tower Hamlets (the Council) on our work on the audit of the financial statements for the year ended 31 March 2019. This report should be read in conjunction with our earlier reports presented at meetings of the committee in July 2019, November 2020, April 2021 and January 2022.

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### **Status of our work**

Our audit is now substantially complete with the following procedures remain outstanding. We anticipate that some of these matters will be completed by the Audit Committee meeting on 26 January and we will update the Committee accordingly:

- Officers' assessment of the useful economic lives assigned to infrastructure assets in the light of recent guidance issued by CIPFA
- Finalisation of our work on employee remuneration disclosures (as set out in the "Other audit judgements" section of this report) on receipt of further information and confirmation of changes made to the disclosures in the draft statement of accounts
- We have reported disclosure misstatements relating to the comparative amounts for dedicated schools grant and to income from service recipients in Appendix A, Audit Adjustments. We have discussed with officers whether these can be remediated in the final version and will conclude on the impact on our opinion if this is not possible.
- There is an historic difference between the capital financing requirement and related balance sheet amounts of £16m which we are discussing with officers.
- Clearance of a small number of open points, in particular in relation to net pension liability, financial instrument fair value disclosure, schools reserves transfers, and certain factual inputs to the valuation of non-current assets, together with performance of other procedures required at closedown of the audit
- Finalisation of internal quality control review processes and internal consultations in relation the scope of our audit
- Review of the final version of the draft statement of accounts, including: updates to disclosures on infrastructure assets taking into account recent guidance issued by CIPFA; additional disclosures to explain issues giving rise to audit qualifications and the council's position on these; updates, if any, to employee remuneration disclosures and dedicated schools grant note comparative; updates to the Annual Governance Statement
- Receipt and evaluation of memorandum documenting the process undertaken by officers to support representations, including any tailoring needed where officers conclude that the council is not in a position to provide the requested representation
- Receipt of audit certificates for the years ended 31 March 2017 and 31 March 2018
- Finalisation of our audit report, taking into account the actual and potential qualification items set out in the "Key messages" section of this report, any further items arising from completion of other open items and finalisation of wording
- Update of our subsequent events review through to the date of signing and receipt of signed management representation letter.

We will provide an oral update on these items at the meeting.

Completion of the audit has been delayed well beyond the original deadline of 31 July 2019 due to the time taken by the council to investigate and resolve issues identified during our original field visit and subsequently, the quality of the council's record keeping and the slow pace at which officers have responded to audit requests. More recently, it has taken time to complete the final stages of our audit due to the volume and significance of issues identified over the period of the audit, the time needed to evaluate the cumulative impact of these on our audit and changes made by officers to the accounts and the impact of this and other factors on our assessment of engagement risk and developing and executing our response plan.

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# Introduction

## The key messages in this report

<b>Status of our work (continued)</b>	<p>This report updates a report presented to the audit committee in January 2022. We previously issued progress reports in July 2019, November 2020 and April 2021 which described challenges encountered in the audit process for the 2018/19 audit and we attended other meetings of the audit committee to give oral updates. Audit committee members have also received updates from officers and a report from an external consultant on the closure process for the 2018/19 statement of accounts.</p> <p>This report repeats information previously communicated, but we have reported in this way to provide a complete picture of our findings, areas of judgement and final conclusions. For reference, at Appendix D we have provided a summary of the more significant matters arising since the issue of our previous report presented to the committee in January 2022.</p>
<b>Key areas of audit judgement</b>	<p>The key judgements in the audit process related to:</p> <ul style="list-style-type: none"><li>• The appropriateness of expenditure capitalised in the year</li><li>• The valuation of properties</li><li>• The valuation of a provision for the cost of settling appeals against rateable values made by business ratepayers</li><li>• The treatment of an historical amount of £20m previously carried in payables</li><li>• The appropriateness of restating comparative information and opening balances for various items</li><li>• The valuation of the council's pension liabilities</li><li>• The accounting for an indemnity given to Tower Hamlets Homes Limited (THHL) in respect of pension contributions</li><li>• The recognition basis for various income streams</li><li>• The impact of deficiencies in records relating to officer remuneration and related party disclosures</li><li>• The appropriateness of asset lives assigned to infrastructure assets</li><li>• The decision on whether to prepare group accounts</li></ul> <p>We report our conclusions on these areas in sections 3 and 4.</p>
<b>Findings and conclusion</b>	<p>We have summarised uncorrected misstatements at Appendix A, Audit Adjustments. We will be requesting the council's confirmation that the effects of uncorrected misstatements and disclosure deficiencies are immaterial, both individually and in aggregate, to the financial statements as a whole (see Appendix F, Draft management representation letter).</p> <p>We expect our opinion will be qualified in respect of the following matters:</p> <ul style="list-style-type: none"><li>• The council has not consolidated the financial statements of its subsidiaries, Tower Hamlets Homes Limited and King George V Fields Trust and other interests. Had consolidated accounts been prepared, elements of these accounts would have been materially different to the council's single entity accounts. We expect our opinion on the council's financial statements will be qualified for this matter as the failure to consolidate all subsidiaries is a departure from the requirements of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 (the Code).</li></ul>

# Introduction

## The key messages in this report

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### **Findings and conclusion (continued)**

- In its analysis of movements on the council's net pension liability in its draft 2019/20 accounts, the council recorded an experience item (which relates to the correction of assumptions to align with actual experience) of £116m and an adjustment to the council's share of pension assets of £29m. It is likely that material components of these items relate to the true-up from estimates to actuals in relation to the three year inter funding valuation period to 31 March 2019. As it provides information about circumstances present at 31 March 2019, this is an adjusting post balance sheet event. As the accounts have not been adjusted to account for these items in the correct period, our audit report will be qualified as the amounts involved are material.
- The council did not obtain, or is now unable to locate, sufficient information on interests held by councillors during the financial year. As a result, the council is unable to confirm whether the information provided to us on related party relationships is complete. We have therefore been unable to determine whether all related party transactions have been disclosed in accordance with the requirements of the Code.
- We have identified several issues relating to the compilation of disclosures on employee remuneration. The issues are set out on page 40 and relate to the collection of information relating to staff employed at schools which use third party payroll providers and its consolidation with information relating to other employees. Officers have confirmed their intention to remediate for some of the issues which have been identified. We are waiting for responses to certain questions and an updated version of the accounts before finalising the scope of the qualification.

Our January 2022 report also set out further qualification points in relation to:

- The accounting for an indemnity given to Tower Hamlets Homes Limited. As explained in our oral presentation to the audit committee meeting in January 2022, this matter was under review at that time and has now been resolved and will not result in a qualification – further details are set out on page 27.
- Note 8 to the financial statements, which reconciles Net Expenditure in the Comprehensive Income and Expenditure Statement to the Expenditure Chargeable to General Fund and Housing Revenue Account amounts for the year. In our January 2022 report, we said that we expected to qualify our opinion as officers had advised they were unable to provide supporting analyses or reconciliation to the accounting records. Since then, officers have reconstructed the note and supporting information and, as a result, we have been able to complete our procedures. Again, therefore, our report will not be qualified in respect of this matter.

We have set out at Appendix E the proposed wording of the modification to our audit report.

We recommend the audit committee request a paper setting out the actions which have been taken to ensure that the circumstances giving rise to the qualifications have been rectified for future years' accounts. We also recommend the council consider including narrative within the financial statements to explain the issues giving rise to the qualifications and its position on these.

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# Introduction

## The key messages in this report

<b>Other information included in the statement of accounts</b>	<p>We have reviewed the council's narrative report and annual governance statement to consider whether they are misleading or inconsistent with other information known to us from our audit work.</p> <p>We will report by exception that information in the narrative report is materially misstated in relation to the matters giving rise to the qualifications in respect of the failure to prepare group accounts and the accounting for certain pension gains, as described on the previous page.</p> <p>Officers have updated the narrative report for deficiencies reported in July 2019 and January 2022. We have set out remaining matters in relation to the Annual Governance Statement in Appendix A, Audit Adjustments. The council is updating the Annual Governance Statement and we will conclude once we have received this.</p>
<b>Duties as public auditor</b>	<p>We did not receive any questions or objections from local electors in respect of the 2018/19 statement of accounts.</p> <p>We have not identified any matters that would require us to issue a public interest report. We have not had to exercise any other audit powers under the Local Audit and Accountability Act 2014.</p>
<b>Use of resources</b>	<p>As reported in our January 2022 report, we expect our conclusion on the council's use of resources will be qualified in respect of:</p> <ul style="list-style-type: none"><li>• financial reporting arrangements. This is, in particular, due to the volume and significance of changes required to the original draft statement of accounts and the long delay in finalising the accounts for publication</li><li>• arrangements relating to children's services as improvements in arrangements which resulted in a rating of "Good" in Ofsted's reinspection of the service in 2019/20 were not in place throughout the whole of 2018/19.</li><li>• arrangements for managing risks effectively and establishing a sound system of internal control. This is because of the significance of matters identified and reported through the internal audit programme and annual governance statement process relating to arrangements in place during 2018/19.</li></ul>
<b>Whole of government accounts</b>	<p>As the finalisation of the council's statement of accounts for 2018/19 has been delayed beyond the publication of the Whole of Government accounts for that year, we are no longer required to provide a report to the National Audit Office on the consistency of the council's consolidation return with its statement of accounts and other matters.</p>
<b>Management representation letter</b>	<p>As required by auditing standards, we request written representations in connection with our audit. A draft of the representations we are requesting has been included in Appendix F, Draft management representations. In view of changes in council staffing and challenges experienced in providing information over the course of the audit, the council will need to devote sufficient time to, and take particular care in, implementing controls that will allow the council to verify the accuracy of the representations requested and thus to provide such representations faithfully and after due process. The council will also need to consider what changes are needed to the requested representations in areas where we expect to qualify our opinion.</p>

# Introduction

## The key messages in this report

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### **Control observations**

We summarise significant and other control deficiencies which have come to our attention in Section 6, Control observations.

Reflecting the volume, significance and pervasiveness of misstatements identified during the course of the audit, the number and significance of these control observations are greater than we report at most other local authorities.

The common root cause of these observations has been a lack of capability and capacity with the finance function which has led to: a lack of capability and/or desire to understand and analyse the accounting basis for transactions; the failure to establish an effective system of quality assurance; and weaknesses in financial control and reporting, including controls over general ledger maintenance, documentation of key judgements and compliance with presentation and disclosure requirements in preparing the statement of accounts.

Over the last two years, the interim Corporate Director – Finance and Resources has reported progress on an improvement plan which is designed to address these and other underlying systemic issues. The council has also invested time in investigating and responding to specific accounting issues identified in the course of the audit and building better processes to prevent their reoccurrence. However, as a result of the timing of many of these actions, we have needed to repeat many of these same points in our equivalent report on the 2019/20 council audit.

Notwithstanding this, there were clear improvements in the quality of information received for the purpose of our 2019/20 audit, although it is also apparent that some disciplines, including preparation of detailed accounting papers and effective quality assurance processes are yet to be embedded and the council still needs to demonstrate that it can carry out its annual financial reporting tasks at pace, including responding to audit requests.

We recommend the committee request a report from officers on the status of actions already taken which address specific recommendations made by us in Section 6, together with the plan to address residual items.

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### **Fees**

We have set out the scale fee and variations to the original scale fee which have so far been agreed with the council and with Public Sector Audit Appointments Limited on page 80. This takes account of time spent in the period to 31 January 2021. Since then, a substantial amount of time has been incurred to bring the 2018/19, as well as the 2019/20, audits to their current state (£312k in total for the 2018/19 and 2019/20 audits, together, in the period 1 February 2021 to 31 December 2022) and we will be seeking to agree a further fee variation in relation to this and further time incurred in finalising the audit.

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### **Audit of pension scheme financial statements**

We reported separately to the Audit Committee in January 2021 on our audit of the financial statements of the pension scheme. There are no additional key findings to report from further work performed subsequently and therefore we have not prepared an updated report for this meeting. There are a small number of points to close-off.

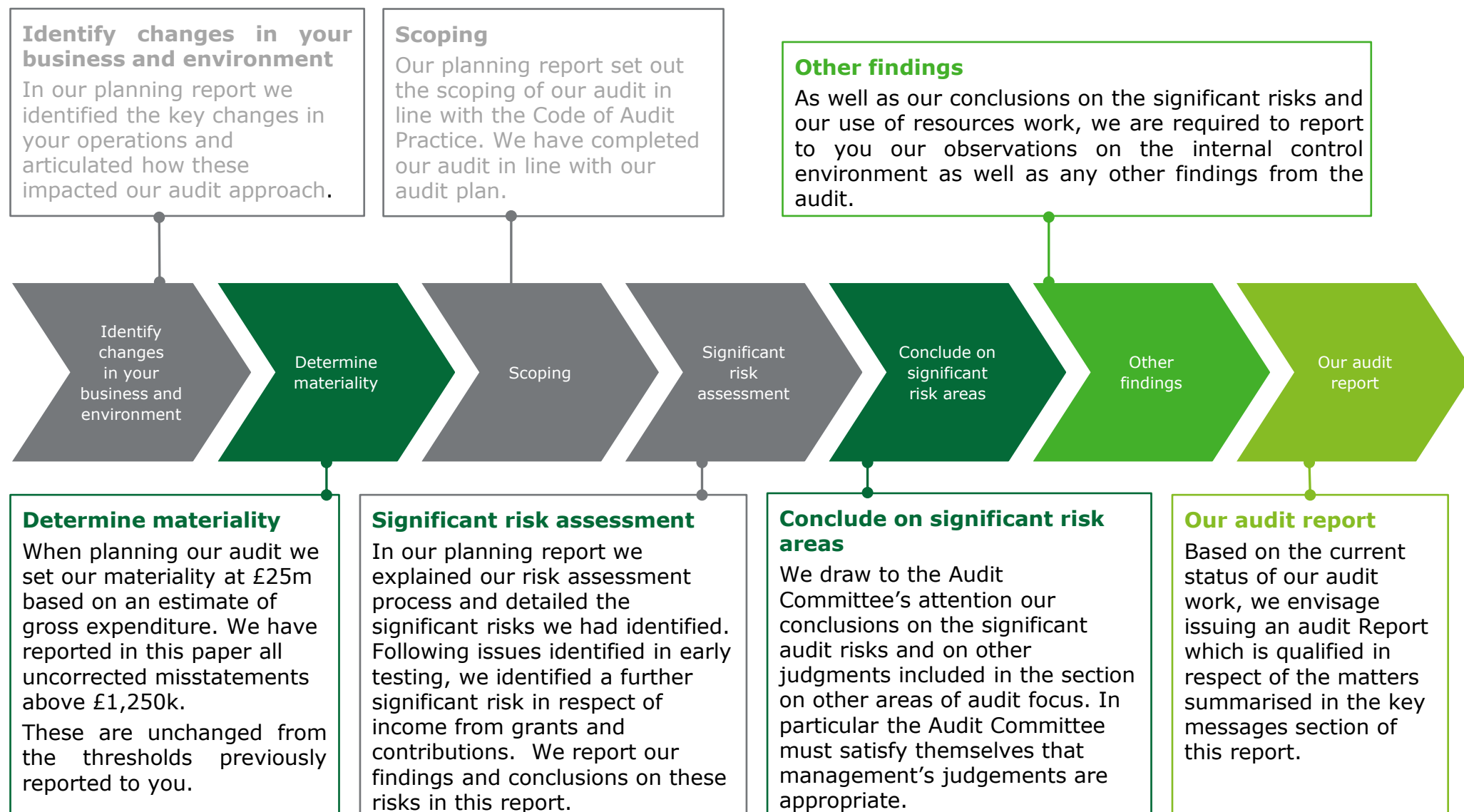
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## 2. Our audit explained

# Our audit explained

We tailor our audit to your organisation and your strategy



### 3. Significant audit risks

# Significant audit risks

## Valuation of properties

### Risk and Deloitte challenge and response

#### Risk

The Council is required to hold property assets within Property, Plant and Equipment at valuation. The valuations are by nature significant estimates which are based on specialist and management assumptions and which can be subject to material changes in value.

This has been pinpointed to the (a) risk of inappropriate methodology or assumptions used in the valuation of schools and other specialised assets, in particular: the application of the modern equivalent assets principle; the judgement on land values; and the approach to estimating the allowance for the physical deterioration and obsolescence (b) the risk of inappropriate methodology or assumptions in the valuation of council dwellings in particular: the application of the beacon approach; and the selection of comparators; the risk that the carrying value is materially misstated because assets which have not been revalued at the reporting date have changed materially in value since the date of last valuation.

#### Deloitte challenge and response

We have tested the design and implementation of controls within the valuation process.

With the assistance of our internal valuation specialist we have performed the following procedures to respond to the significant risk or in support of that work:

- Assessed the qualifications, experience, objectivity and independence of the valuer
- Tested factual inputs, such as building areas, to source documentation
- Assessed the appropriateness of the methods and assumptions used by the valuer
- Tested a sample of individual asset valuations
- Tested the posting of the valuation to the accounting records.
- Assessed Officers' rationale for concluding that there was no material change between the data valuation and the reporting date for those assets not revalued at the reporting date.

### Conclusions

#### Conclusion on the design and implementation of key controls

The valuation of properties has not been well controlled. Whilst the Council is taking steps to remediate the position, the following significant control deficiencies were present in the production of the 2018/19 draft statements of accounts:

- The Council did not have controls to ensure that information provided to the valuer for the purpose of his valuation was complete and accurate and the design of controls over subjective inputs to the valuation is not clear.
- We have not been able to obtain documentation to be clear how changes in individual asset values have been scrutinised and followed up with the valuer. This would require formalising the criteria for selection of individual asset values for investigation, consistently applying these criteria and then documenting the conclusion on exceptions for review and approval.
- The calculation and recording of entries relating to the valuation is performed in the fixed asset register. The fixed asset register is maintained on an excel spreadsheet. Typical spreadsheet controls we would expect to see over the design and maintenance of a spreadsheet used for the initiation and recording of significant financial transactions have not been adopted.
- There was a lack of control over key judgments in the valuation process, in particular how the modern equivalent asset principle was to be applied to each class of asset (see below).
- Officers' process for assessing whether there had been a material change on assets not selected for revaluation at the reporting date was not adequate. Further information all this is given below.

We have responded to these control deficiencies by increasing the seniority of staff involved in the audit of this area, through the use we have made of specialists and requesting officers take remedial action.

We also draw attention to the recommendations made in relation to the valuer's report in our April 2021 report.

#### Conclusion on our substantive audit procedures

Our testing and subsequent investigations carried out by officers has identified a number of issues, as set out overleaf.

# Significant audit risks

## Valuation of properties (continued)

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### Deloitte challenge and conclusion

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#### Issues relating to land and building area assumptions

- For assets valued on a depreciated replacement cost basis, land and building areas should reflect the size and layout of the building and ancillary land were it to be re-provided on a least cost basis, using a modern design and on an optimised site (the “modern equivalent asset”). However, it is common and acceptable to use the actual areas of the existing asset, but we encourage the council to give valuers instructions in the future to follow the latest guidance on the use of the modern equivalent asset principle in depreciated replacement cost valuations. For developed land areas for schools (i.e. the footprint of the buildings together with ancillary built on land such as playgrounds and car park) we understand that the areas used for the original valuation at 31 March 2019 were derived from either the building footprint or gross development value of the building, but did not receive a complete explanation. The approach did not comply with the modern equivalent asset principle and resulted in areas which were as a whole significantly less than the actual developed land areas for the existing assets. Officers have obtained a second updated valuation using the actual areas for the existing assets.
- The valuation of school buildings uses information on their gross internal area. That data is provided by the Council to the valuer. Officers identified discrepancies with site plan information for the sample items selected by us and in the light of this, extended their investigation to cover the building areas for all schools. A second updated valuation has been obtained for the schools affected.
- Together these adjustments related to an increase in the valuation of schools of £118m at 31 March 2019.
- The same information on building areas was used in the valuations at 31 March 2017 and 31 March 2018. As a result, officers have restated building valuations at these earlier reporting dates using the revised actual building area information. The same information on developed land areas was also used in the valuation at 31 March 2018. The position for the valuation at 31 March 2017 is less straight forward rather than developing separate assumptions for land area and price per hectare. For that valuation, the valuer calculated the developed land area as a percentage of the building. We have concluded this approach is not appropriate. Officers have restated the valuation at 31 March 2017 using the information on site areas and price per hectare used in the 31 March 2018 valuation. At 1 April 2017 this is partially offset by the effect of correcting a formula error in the original valuation calculation which is discussed on the next page. The restatements, together, led to an increase in schools non-current assets at 31 March 2018 of £268m and 1 April 2017 of £421m.

#### Issues relating to price per hectare for land assumption

- The valuation of land used in preparing the published accounts for 2017/18 assumed a value of £17.8m per hectare for developed land. The same assumption was used for the valuation at 31 March 2019 in the initial version of the 2018/19 accounts. Subsequently, within the 2018/19 accounts, the valuation at 31 March 2018 has been updated for a change in the assumption from £17.8m to £11.1m per hectare. We agreed that the new assumption fell with a reasonable, albeit broad, range based on the range of values observable in the market. We considered the position for earlier years. Following further discussion with the valuer, we concluded that this was a change in estimate, rather than the correction of an error. This is because:
  - Based on research carried out by the valuer and other information considered by our valuation specialist, transaction values are highly dependent on the density of the subsequent development and we have concluded that both original and revised price per hectare both fall within the wide range of observed market prices.
  - The transactions which the valuer has relied on for the lower price per hectare relate to market transactions completed after the date of approval of the 2017/18.

# Significant audit risks

## Valuation of properties (continued)

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### Deloitte challenge and conclusion

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#### Issues relating to the classification of assets for valuation purposes

- Two assets were surplus, but were classified in other land and buildings within the Property, Plant and Equipment note. In addition to the disclosure misstatement, surplus assets are required to be valued on a different basis, which reflects the property's highest alternative use, rather than its existing (or previous) use. The Council has obtained new valuations for these properties on the correct valuation basis which has resulted in an increase to their previously recorded values at 31 March 2019 of £12.2m. As the properties have been surplus for a number of years, the Council has also obtained revised valuation at earlier reporting dates with similar increases. The accounts for both years have been updated for these changes, including restatement of comparative information. Officers performed a review and did not identify any further surplus assets included in operational categories.

#### Issues relating to the allowance for physical deterioration and other obsolescence

- In arriving at the valuation of assets recorded at depreciated replacement cost, an allowance is made for physical deterioration and all relevant forms of obsolescence. The valuer has adopted a straight line approach in applying obsolescence. Whilst this is not incorrect, it is, nonetheless, a simplistic approach.
- The restated value of school buildings at 31 March 2017 (see previous page) includes the effect of correcting a formula error in the valuation calculation which resulted in no allowance for physical deterioration and other obsolescence being applied to professional fees included in the valuation. The impact of this error was to originally overvalue non-current assets by £21m at 31 March 2017.

#### Issues relating to other factual inputs to valuation calculations

- For certain schools, the build cost per square metre for the incorrect type of school was used. We have proposed adjustments of £1.0m-£1.4m at the balance dates involved in Appendix A, Audit Adjustments, which remain uncorrected.
  - Discrepancies with site plans were identified in information given to the valuer on site areas. We estimated by extrapolation the possible error across other assets not sampled to be £3.1m. This has been accumulated in Appendix A, Audit Adjustments.
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# Significant audit risks

## Valuation of properties (continued)

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### Deloitte challenge and conclusion

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#### Issues relating to non-current assets which were not subject to valuation at the reporting date

- Properties acquired for use as temporary accommodation during 2018/19 were not included in the valuation programme. Following our challenge, these have now been valued resulting in a reduction in their value at 31 March 2019 of £11.1m reflecting their new use, as well as a falling residential market. Properties acquired in 2017/18 for use as temporary accommodation were similarly excluded from valuation at 31 March 2018. A net revaluation loss of £18.5m was recorded on their first-time valuation in 2018/19, at a valuation date of 1 April 2018. It is likely this loss was incurred in 2017/18 and would have been recognised in the accounts for that year had a valuation been undertaken. This error has also been corrected. At the same time, an error in the presentation of gains and losses on valuation of temporary accommodation has been corrected. In the original version of the accounts, the acquisition cost for temporary accommodation acquired in 2017/18 and 2018/19 was allocated in full to the building component. On first time valuation in 2018/19, the new valuation was apportioned between building and land components. The valuation resulted in a valuation loss overall. The failure to apportion the original purchase cost between land and building components, resulted in the recording of a gain on the land component (equal to the amount of the land valuation), recognised in other comprehensive income and subsequently transferred to the revaluation reserve, and a higher than otherwise loss on the building component, charged to the Place Directorate in the net cost of services and subsequently transferred to the Capital Adjustment Account. As these gains and losses result from the way in which items have been recorded, rather than underlying changes in the components, an adjustment to net off the gain on the land component against the loss on the building component within other comprehensive income has now been made, in addition to the adjustment discussed above to record adjustments in the correct period. As a result, other gross expenditure on Place is has been reduced by £15.1m in 2018/19.
- The Code does not require properties to be revalued on an annual basis, but does require valuations to be carried out where there has been a material change. Assets measured at current value which were not included in the 2018/19 valuation programme totalled £220.5m. In addition, assets valued as part of the 2018/19 valuation programme with an effective date of 1 April 2018 and where the valuation was not updated at the reporting date totalled £110.3m.
- The Council assesses whether there has been a material change over the financial year through its review of the market review report commissioned from its valuer. We challenged the appropriateness of officers' approach as:
  - Officers had not evaluated the possible cumulative change since the date of the last valuation of properties (noting that for some properties this is earlier than the start of the financial year)
  - Officers had not quantified the possible effect of market changes in the market review report on property values.
- Officers have subsequently performed work to address both these points and have calculated an estimate of change since the last date of valuation for those assets measured at current value but not revalued at the reporting date which is significantly below our materiality threshold. The analysis considered only general market changes and did not consider the possibility of material change caused by factors specific to individual properties. In addition, the analysis was based on a market review report prepared by the council's valuer which for properties recorded at existing use value, appeared to only provide a view as to whether there had been a material change during the year, but did not provide an estimate of any increase or decrease in value where the change was not considered to be material. As a result, it was not clear that the analysis took properly into account the possibility of cumulative change which was material. We performed additional procedures in response to these gaps and were satisfied that there had not been a material change.

# Significant audit risks

## Valuation of properties (continued)

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### Deloitte challenge and conclusion

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- These procedures included having regard to the results of the 2019/20 valuation programme. The programme included the revaluation at 31 March 2020 of approximately half of those assets not revalued at 31 March 2019. The recorded gain on these assets is not indicative of an earlier, material change.
  - A valuation of council dwellings was carried out at 1 April 2018. Officers did not commission a second valuation at 31 March 2019, but instead applied an index to take account of market changes during the intervening period. Whilst we concluded that the index used was reasonable, we challenged officers on how the council had calculated the closing carrying value using this index. As a result of this challenge, we proposed an adjustment to reduce the closing value by £4m which remains uncorrected (see Appendix A where we provide further detail).
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# Significant audit risks

## Management override of controls

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### Risk and our response

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#### Risk

Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Notwithstanding that the council officers may not be subject to the same types of pressure and incentives in relation to financial statements when compared to the management of a corporate entity, we nevertheless concluded that there was a heightened level of risk of fraudulent financial statements as a result of:

- The increased opportunity for manipulation of the accounts as a result of weaknesses in control, in particular management review controls over estimates and approval of journals (see "Conclusion on the design and implementation of key controls" on the next page)
- The identification of transactions where the rationale was not fully clear (see "Significant transactions", below).

#### Deloitte response and challenge

We have responded to the heightened risk of fraudulent financial statements as a whole by:

- Increasing the seniority of staff in the audit
- Carrying out an additional internal review process of the audit work performed
- Understanding the controls over member conduct

Our response to particular areas of the audit is set out below.

#### Journals

- We have tested the design and implementation of controls in relation to journals.
  - We have made inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments.
  - We have used our proprietary data analytics tool to test a sample of journals, based upon identification of items of potential audit interest. Our analysis has covered all journals posted in the year.
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# Significant audit risks

## Management override of controls

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### Risk and our response

#### Significant transactions

We did not identify any material transactions outside the normal course of business or where the business rationale was not clear. However we draw to the attention of audit committee members to two lower value transactions examined as part of our journal entry testing:

- A transaction involved recording a contribution from an NHS entity of £3m immediately prior to the year end. We concluded that the transaction was artificial and intended to be unwound and therefore an adjustment has now been made to reverse it. We concluded this based on:
  - The way in which the transaction was characterised in correspondence between the two parties
  - The absence of a written agreement on how the contribution was to be applied by the council (which is a requirement of the governing legislation)
  - The existence of a second transaction, subsequent to the reporting date, where a contribution was made by the council to the NHS entity in the same amount (i.e. having the effect of repaying the original contribution). Again, a written agreement was not put in place recording how the contribution was to be applied, this time by the NHS entity.

We performed additional procedures to respond to the risk of similar transactions involving the local health body.

- The release of an historic credit balance of £20m, initially to the General Fund. As set out in more detail on pages 30-31, we were unable to obtain information on the council's rationale for the original transaction in the 2018/19 accounts or the previous treatment adopted in the accounts for earlier years. The accounting treatment in the original version of the financial statements resulted in earlier recognition and retention of a higher amount compared to the final accounting treatment.

#### Accounting estimates

- We have performed design and implementation testing of the controls over key accounting estimates and judgements.
  - The key judgements in the financial statements are those selected as significant audit risks and other areas of audit interest as summarised on page 5, including the NNDR appeals provision; the pension liability and debt provisions. In designing our work we considered the overall sensitivity of the financial statements to different types of judgement.
  - We reviewed accounting estimates for biases that could result in material misstatements due to fraud. We note that overall the changes to estimates in the period were balanced and did not indicate a bias to achieve a particular result.
  - We tested accounting estimates and judgements, focusing on the areas of greatest judgement and value. Our procedures included comparing amounts recorded or inputs to estimates to relevant supporting information from third party sources.
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# Significant audit risks

## Management override of controls (continued)

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### Conclusions

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#### **Conclusion on the design and implementation of key controls**

Journals are raised through two routes. As explained more fully in section 6, Control observations, “bulk upload” route does not require approval of journals before posting. This is a significant control deficiency.

There is no requirement to prepare management position papers to explain and support estimates and we have referred to various examples throughout this report where this has not been done or where the analysis is incomplete. The failure to prepare documentation which fully explains and supports key estimates with associated management review also represents a significant control deficiency.

#### **Conclusion on our substantive audit procedures**

Our overall conclusion on estimates is as follows:

- The council has made various changes to estimates in the original version of the accounts. We conclude that misstatements arose due to errors in factual inputs to estimate calculations or as a result of the initial analysis being inadequate, rather than intentional manipulation of financial information.
  - Entries relating to the valuation of PPE and related depreciation charges and gains and losses on disposal and pension liabilities do not impact on the usable reserves of the council and we would generally expect that there is little or no incentive for the council to manipulate this information.
    - The property valuation as a whole is towards the prudent end of a reasonable range because the land value used for assets at depreciated replacement cost is at the lower end of the range we would expect. This assumption is more prudent than the equivalent assumption at 31 March 2018 and contributed to the overall reduction in the carrying value of PPE compared to the prior year. Pension liabilities are also towards the more prudent end of a reasonable range. This is because, the council’s actuary, in their methodology for deriving inflation rate assumptions, did not make a common adjustment to allow for an assumed inflation rate premium within observed market data. The method used by the actuary has not changed from the prior year and therefore involved a similar level of prudence in the position at 31 March 2018.
    - Conversely, the remaining useful economic lives of council dwellings (an average of 54 years) has been set towards the upper end of the range we would regard as reasonable of 30 to 60 years, resulting in a comparatively low depreciation charge. The remaining useful economic life for non residential properties is assumed, on the advice of the council’s valuer, to be 50 years, regardless of age or condition of the property. As this results in a depreciation charge of only £14m, we concluded that we did not expect this simplification to result in a material misstatement but are not able to quantify.
  - Entries relating to judgements which do impact on the amount of usable reserves were generally centred and consistent with prior year (following revision where relevant) and did not show evidence of bias. Changes in approach resulted in an increase in the NNDR appeals provision and a reduction in two bad debt provisions, in comparison to the prior year. We have proposed an adjustment to increase the NNDR appeals provision further, as summarised in Appendix A, Audit Adjustments.
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# Significant audit risks

## Capitalisation of expenditure

### Risk and Deloitte challenge and response

#### Risk

The Council has a substantial capital programme, including revenue expenditure which, for funding purposes, is treated in the same way as capital expenditure (REFCUS).

Determining whether or not expenditure should be capitalised can involve judgement as to whether costs should be capitalised under International Financial Reporting Standards.

The Council has greater flexibility over the use of revenue resource compared to capital resource. There is also, therefore, an incentive for officers to misclassify revenue expenditure as capital.

#### Deloitte response and challenge

We have tested the design and implementation of controls to ensure that only capital expenditure which meets the conditions for capitalisation is accounted for as such.

We have tested a sample of items capitalised (including amounts in REFCUS) to ensure they are valid and meet the conditions for capitalisation.

### Conclusions

#### Conclusion on the design and implementation of key controls

As reported previously, we were not able to identify a documented internal control to prevent or detect the incorrect classification of revenue spend as capital. This represents a significant control deficiency.

We have responded to this deficiency by increasing the seniority of staff involved in this work.

#### Conclusion on our substantive audit procedures

We did not identify any items from our testing which had been inappropriately capitalised.

Our previous reporting referred to exceptions identified in our testing relating to the classification within the PPE note of refurbishments and the potential impact on subsequent accounting for this expenditure. We explain how this issue was resolved in Appendix D.

# Significant audit risks

## Income from grants and other contributions

### Risk and Deloitte challenge and response

#### Risk

Our early testing identified issues in relation to grants and other contributions. We have pinpointed the significant risk to:

- Contributions by leaseholders to major works which in the original version of the accounts were recognised in the comprehensive income and expenditure statement on a cash basis. Under IFRS 15 Revenue from contracts with customers, revenue is either recognised over time or at a point in time depending on an analysis of how performance obligations in the contract are satisfied. In this case, the obligation to carry out the works is satisfied over time and therefore contributions should have been recognised as spend on the capital project was incurred.
- Community infrastructure levy which in original version of the accounts (and in previous years) was recognised in the comprehensive income and expenditure statement when invoiced. Revenue should be recognised when payment is due under the relevant legislation, in this case on commencement of the development.

Officers have carried out an exercise for the purpose of both the 2018/19 and 2019/20 accounts to re-analyse both leaseholder contributions and community infrastructure levy across all periods presented in these statements.

There is a risk that leaseholder contributions and community infrastructure may not be recognised in the correct period as a result of errors in the execution of this exercise.

Recognition of grant income and contributions is not inherently complex nor does it involve significant judgement. Errors were also identified in the recognition of grants where grant income had been deferred inappropriately and where grant debtor and creditor control accounts had not been properly reconciled. As these balances, after adjustment, were not material, we concluded that there was not a significant risk of material misstatement associated with the recognition of other grant income.

#### Deloitte response and challenge

We have tested the design and implementation of controls to ensure that grant income and contributions are recognised in the correct period.

We carried out focused testing on the exercise carried out by officers to implement a change in recognition basis for major works across all periods presented in the 2018/19 and 2019/20 statements of accounts.

Our procedures in respect of contributions from leaseholders to major works included:

- Re-calculating accrued income at 31 March 2019, 31 March 2018 and 1 April 2017 for a sample of leaseholders, agreeing inputs to that calculation to records of individual and block gross values and capital expenditure records and testing whether recognition principles have been correctly applied, based on the timing of the related capital expenditure.
- Testing the completeness of income recorded in 2018/19 by tracing from the items in the capital programme to income records for the relevant year.

Our procedures in respect of community infrastructure levy (again to test the exercise carried out by officers), included:

- Understanding the Council's process for capturing and recording the commencement of developments
- Testing accrued income at 31 March 2019, 31 March 2018 and 1 April 2017 to commencement notices, invoice and subsequent receipt of cash
- Testing income in 2018/19 to commencement notices, invoice and subsequent receipt of cash
- Tracing a sample of developments from the Exacon system (used to record information on projects which have commenced) to income records.

# Significant audit risks

## Income from grants and other contributions

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### Conclusions

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#### **Conclusion on the design and implementation of key controls**

The Council has prepared and shared with us process notes in relation to grant income and contributions. We are not clear from these what controls operate within this process to ensure that grant income and contributions are recognised in the correct period and in practice errors have been identified. This represents a significant control deficiency.

We have responded to this deficiency by increasing the seniority of staff involved in this work.

#### **Conclusion on our substantive audit procedures**

Our procedures on contributions from leaseholders to major works did not identify any exceptions.

Our testing of community infrastructure levy identified the incorrect accrual of income of £2.8m at 1 April 2017 relating to a development which did not commence until 2017/18. This has now been corrected.

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## 4. Other areas of judgement

# Other areas of judgement

## Prior year adjustments

### Area of judgement and conclusion

Our initial work during 2019, and subsequent investigations carried out by officers, identified accounting issues impacting on prior periods.

Officers concluded on the basis of these investigations that comparative information for 2017/18 and opening balances at 1 April 2017 and 1 April 2018 should be restated.

The table below summarises the restatements made and provides references to where the circumstances and accounting issues giving rise to these restatements have been discussed in either this report or an earlier reports presented to the committee in April 2021 (the "April report") or in January 2022 (the "January report").

Description of misstatement	Reference	Effect on net assets at 1 April 2017		Effect on 2017/18 total comprehensive income			Effect on net assets at 31 March 2018	
		Assets	Liabilities	Income from services	Spend on services	Other	Assets	Liabilities
		£m	£m	£m	£m	£m	£m	£m
<b>Correction of property related errors</b>								
PPE valuation	Pages 12-16	425.0	-	-	(6.9)	160.3	271.7	-
Academy conversion	April report	-	-	-	-	75.8	(75.8)	-
<b>Correction of income recognition errors</b>								
Leaseholder contributions	Pages 21-22	18.0	6.1	-	-	(2.2)	10.6	15.7
Community infrastructure levy	Pages 21-22	9.4	-	-	-	(2.4)	10.3	1.5
Grant and contributions income recognition	January report	(2.8)	15.5	(1.1)	-	(1.4)	(3.7)	18.9
<b>Correction of presentation errors</b>								
Bank accounts in credit offset	January report	70.2	(70.2)	-	-	-	51.0	(51.0)
Classification of investments*	January report	-	-	-	-	-	-	-
Offset of internal income and expenses	Page 22	-	-	55.3	(55.3)	-	-	-
<b>Correction of omission of liabilities</b>								
Teacher discretionary pension award	April report	-	(9.4)	-	-	-	-	(9.4)
<b>Correction of other errors</b>								
Accounting for schools balances	Pages 28-29	1.6	-	7.0	0.3	-	(1.9)	(3.8)
Other corrections		-	-	1.7	0.4	(2.5)	(0.3)	0.7
<b>Total</b>		<b>521.4</b>	<b>(58.0)</b>	<b>62.9</b>	<b>(61.5)</b>	<b>227.6</b>	<b>261.9</b>	<b>(27.4)</b>

\*Investments totalling £57m at 31 March 2018 and £30m at 1 April 2017 have been reclassified from short term (i.e. current) to long term (i.e. non-current) investments.



# Other areas of judgement

## Prior year adjustments (continued)

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### Area of judgement and conclusion

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The decision on whether to restate prior periods typically involves two key areas of judgement.

- Firstly prior period information is only restated where there has been a change in accounting policy or to correct for a material error. Corrections of errors are distinguished from changes in accounting estimates. Accounting estimates by their nature are approximations that may need revision as additional information becomes known. The first area of judgement can therefore be in determining whether or not an item is a prior period error.

Our principal challenges were in two areas:

- In relation to the selection of an appropriate value per hectare for developed land. We discuss this further on page 13.
- As part of the 2018/19 accounts process, a valuation of council dwellings was carried out at an effective date of 1 April 2018. This resulted in a valuation which was £113m (10%) lower than the carrying amount at 31 March 2018. This raises a question as to whether the change arises from a change in accounting estimate, for example due to further information becoming available after the date of approval of the 2018/19 accounts, or whether it relates to an error in the carrying amount at 31 March 2018.

The valuation at 31 March 2018 was derived from a valuation of council dwellings performed at 1 April 2017 which was then updated to 31 March 2019 by applying an index of 4.5% to account for the estimated market increase over 2017/18. The uplift was applied in line with advice in a market review report issued by the council's valuer in April 2018.

We have inspected the market change report which explains that reported index is derived solely from Land Registry information. The Land Registry information for the London Borough of Tower Hamlets shows a reduction and not an increase over 2017/18. The scale and direction of the change in valuation between the two full valuations (i.e. 1 April 2017 and 1 April 2018) is consistent with the information currently observed in the Land Registry information.

Land Registry information is updated continuously and retrospectively – however, the scale of the implied change would be unusual (both overall and for the various data points referenced in the valuer's report). The valuer has been contacted by the council for his comments but he has not been able explain further as we understand he did not retain a copy of the data on which his market review report was based.

Whilst we cannot determine what information was shown in the Land Registry record at the time the valuer prepared his market change report in April 2018, the valuation should reflect information available at the time of approval of the accounts (in July 2018). Given the four month interval, we consider it unlikely that a valuation performed at this point would have resulted in a valuation which was significantly different to the valuation which was subsequently performed at 1 April 2018, but we cannot rule this out. The predecessor auditor did not identify any issues based on the information considered by them at that time. In view of the absence of clear evidence that this results from a failure to consider information available at the time of approval of the 2017/18 financial statements, we have not proposed a restatement.

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# Other areas of judgement

## Prior year adjustments (continued)

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### Area of judgement and conclusion

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- The second area of judgement is whether a prior period error is material. IAS 8.42 requires restatement only of material prior period errors. Immaterial prior period errors shall not be corrected through restatement of comparatives. Officers have decided to correct all prior period errors identified.

Adjustments to the valuation of properties (£272m at 31 March 2018 and £425m at 1 April 2017 – see page 13) and to derecognise academies at 31 March 2018 (£76m) are 11, 17 and 3 times materiality set for planning purposes, respectively and we regard as material.

In our report to the audit committee in December 2020, we highlighted this as an area where we would normally expect management to prepare a position paper setting out and explaining their view and requested that this be done. This has not been done and the position on whether other adjustments are individually material involves greater judgement.

In the case where more than one prior period error has been identified, the accounting guidance requires consideration of the collective effect of errors, as well as whether they are individually material. Where a material prior period error is being corrected through restatement of comparative balances, this does not automatically mean that any other prior period errors identified should also be corrected regardless of their materiality. However, in this case, in view of the volume and size of other errors identified, we consider the approach taken by officers is, in general, reasonable and has been applied consistently and without bias.

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# Other areas of judgement

## Indemnity given to THHL in respect of future pension costs

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### Area of judgement and conclusion

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Staff who transferred from the Council to Tower Hamlets Homes Limited (THHL) continued to be members of the Local Government Pension Scheme administered by the council.

At that time, the council entered into a management agreement with THHL in which it agreed to meet the cost of benefits accrued by transferring employees up to the date of their transfer.

On 31 March 2009, the then Corporate Director, Resources appears to have extended this obligation by writing to the Board of THHL and agreeing that the Council "indemnifies THHL in respect of all liabilities that have arisen or may arise from pension obligations".

On the basis of this letter, the Council has recorded a pension liability equal to the full amount of the liability relating to the THHL section of the London Borough of Tower Hamlets Pension Scheme (i.e. the liability recorded relates to the cost of settling benefits accrued from individuals' service both before and after their transfer to THHL). In turn, THHL has recorded both a liability and reimbursement asset of the same amount.

In the version of this report issued to the January 2022 meeting of the audit committee, we gave a provisional view on the accounting but highlighted in our oral presentation that we were considering this matter further.

We have concluded that the existing approach in the council financial statements is appropriate on the following basis:

- The London Borough of Tower Hamlets Pension Scheme involves the sharing of risks between entities under common control (i.e. the council and THHL), notwithstanding consolidated accounts are not currently prepared. As a result, guidance on the accounting for "group plans" is applicable.
  - The letter sent on 31 March 2009 amounts to a "contractual agreement or stated policy" for charging the net defined benefit cost for the group plan as a whole to individual group entities.
  - The council should, as a result, recognise in its individual financial statements, the net defined benefit cost charged in accordance with the terms of the 31 March 2009 letter – i.e. the costs relating to both its section and the THHL section of the scheme.
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# Other areas of judgement

## Schools' balances

### Area of judgement and conclusion

Officers identified errors in relation to the recording of cash and other transactions involving schools.

These issues arose because of:

- The complex system of entries used to record disbursements and other flows between the council and individual schools
- The use of only a single general ledger control account within the main council ledger to record the balances for some seventy different bank accounts, together with, we understand, a failure to perform a full reconciliation between the general ledger control account on the one hand and the total of the reconciled cash books for the individual schools on the other.

Following investigation, officers have recorded the following restatement of comparative information:

£m	Restatement to correct classification errors	Other restatements	Total restatement
Short term debtors	(8.2)	0.5	(7.7)
Cash and cash equivalents	12.0	(6.2)	5.8
Short term creditors	(3.8)	-	(3.8)
General Fund	-	7.8	7.8
Schools reserves	-	(2.1)	(2.1)
Gross income	-	0.3	0.3
Gross expenditure	-	7.0	7.0

Officers have also made changes to the original version of cash and cash equivalents and other balances at 31 March 2019.

Our procedures have focused on changes to cash balances and has included:

- Discussion of the nature of changes made between original and final versions of the accounts
- Requesting a full reconciliation between the general ledger control account and the individual reconciled cash book balances
- Performing procedures to test the completeness of cash book amounts included in that reconciliation
- Performing tests on the reconciled cash balances on a sample basis.
- Inspection of documentation relating to other accounts balances.

# Other areas of judgement

## Schools balances (continued)

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### Area of judgement and conclusion

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We found that:

- In relation to other restatements of comparative information (see table on previous page), we have not been able to obtain full information on the changes made to income and expenditure in 2017/18 or to the amount of reserves at 31 March 2018. We understand the approach taken by officers was to adjust school reserves to agree to the total of the individual school reserves on returns made by schools, adjusted for known errors identified by officers' investigation. The General Fund balance was then treated as a balancing amount in agreeing to the adjusted net asset position and resulting in a reduction in the closing General Fund reserve at 31 March 2018 of £7.0m.
- There are differences between the reconciled cash position and amended general ledger control account balance of £699k, £934k, £2,625k and £1,560k at 31 March 2020, 31 March 2019 and 31 March 2018 and 1 April 2017 respectively. It was apparent from these unresolved differences that correcting journals posted to the general ledger control account were incomplete.
- The reconciled cash position incorrectly included amounts due from HMRC of £1,246k, £1,644k, £1,189k and £1,499k at 31 March 2020, 31 March 2019, 31 March 2018 and 1 April 2017, respectively. Officers have informed us that these amounts relate to input tax on schools expenditure for the final month or two months of each year which are to be reclaimed from HMRC. Officers' investigation also found that, as a result of an oversight, amounts relating to Feb/March 2020, Feb/March 2019 and Feb/March 2018 input tax had not been subsequently reclaimed and remain outstanding. The updated accounts include a journal to reclassify amounts from cash and cash equivalents to short term debtors to the extent that officers believe that amounts remain recoverable.
- Our sample of reconciling items in individual cash book reconciliations identified a high rate of error (approximately half at 31 March 2019), where payments were deducted from the cash balance before their release, resulting in the understatement of both cash and short term creditors or included invalid entries which should be released to revenue accounts. Officers have not quantified the error and therefore no adjustment has been made. The amount of unpresented cheques and BACS is £8,127k, £7,309k and £25,712k at 31 March 2019, 31 March 2018 and 1 April 2017, respectively, representing the maximum amount of error at each reporting date.

In view of the uncertainty over the correct balance, we have not proposed adjustment but draw audit committee members attention to the fact that there is uncertainty over cash balances at each reporting date presented.

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# Other areas of judgement

## Release of credit balance

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### Area of judgement and conclusion

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We have previously reported to you on a release of a credit of £20.0m which had been brought forward on the balance sheet as part of a larger credit balance relating to the collection of taxes. Our conclusion on this is unchanged and no further information on the transaction has come to light subsequently. We have repeated our conclusion here, however, in order to give a complete picture within this report on all areas of identified judgement that remain.

Officer's subsequent investigation of the balance concluded that:

- The amount had accumulated over a period of several years and related to posting errors involving the bad debt provision for business rates arrears. The amount represented the part of the provision which was identified to be in excess of requirement as a result of the posting errors.
- This position was identified in 2014/15 and the amount which was in excess of requirement was transferred to an account included in Short term creditors.
- In the original version of the 2018/19 accounts, authorised for issue in May 2019, an entry was made to release the credit to the General Fund.
- As the amount was originally charged to the Collection Fund as a bad debt provision and was now in excess of the required amount, the liability should have been released in the Collection Fund and not to the General Fund.

On the basis of this conclusion:

- Officers wrote to MHCLG in September 2019 for guidance and MHCLG have agreed that the amount can be accounted for as an in-year release of the provision in the Collection Fund. This means that the benefit of the reversal is subject to the 100% local retention and pan London pooling arrangements applicable to 2018/19.
- Correcting entries have been made in the Council accounts and supplementary Collection Fund statement in line with the guidance from MHCLG.

We inspected officers' concluding report prepared as a basis for these entries. We concluded that:

- The information provided through officers' investigation is not sufficient to determine which original entries (if any) were erroneous.
- The analysis of entries giving rise to the original credit supports that the credit relates to the collection and disbursement of business rates.
- Our work on the Collection Fund does not identify the need for a balance to be held (either amounts due to business rates payers; bad debt provision; or amounts due other preceptors arising from transactions in the period).
- Whilst the quality of records means that the position is not certain, it is, as a result, probable that the amount: forms part of the Collection Fund balance sheet; is in excess of any requirement; and should be released to the Collection Fund.
- The credit has been released on the bad debt expense line within the Collection Fund supplementary statement. Officers have explained why this is the appropriate classification, but the evidence for this (or alternate) classifications is very limited. However, the amount is immaterial to the presentation of the Collection Fund.

# Other areas of judgement

## Release of credit balance

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### Area of judgement and conclusion

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Our procedures also included considering whether it was appropriate to account for the release of the credit as a current year item in the Council's accounts or whether opening balances and prior year information should be restated. Officers have told us that they have been unable to determine the reason for the decision taken in 2014/15 to carry forward the "excess" provision amount, rather than release to the Collection Fund.

We have concluded:

- As the excess provision amount was substantially accumulated during a period when the council was acting as an agent for central government in the collection of all business rates, it is reasonable to conclude that officers, at that time, considered it was likely that amounts previously deducted from past remittances to central government in relation to the excess provision would need to be paid to central government in the future and therefore that it was appropriate to carry this credit balance on the balance sheet. The lack of adequate contemporaneous documentation (as explained further below) increases the amount of judgement involved in this accounting decision.
- The release of the credit therefore arises from a change in estimate arising from the department's clarification of its expectations.
- It is therefore appropriate to account for the release in 2018/19 and not by restatement of opening balances.

Officers' investigations identified a brief comment in a working paper in 2014/15 on the accounting treatment. However, this did not adequately explain either the preceding treatment or the rationale for transferring the credit to a separate, short term creditor account. Similarly, we have not been able to obtain documentation which explains the decision to carry forward this credit at subsequent year ends or which explains either the decision to release the credit in 2018/19 or the initial decision to release this to the General Fund and not the Collection Fund.

This type of documentation forms an important part of the Council's accounting records and the absence of the documentation and appropriate internal scrutiny of the decision-making represents a significant control deficiency.

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# Other areas of judgement

## Preparation of group accounts

### Area of judgement and conclusion

Authorities with interests in subsidiaries, associates and/or joint ventures are required to prepare group accounts in addition to their single entity financial statements unless their interest is considered not material.

The council has subsidiaries but has not prepared group accounts as officers have concluded that group accounts would not be materially different to the council's single entity accounts.

The two principal subsidiaries are THHL, a wholly owned subsidiary, and King George V Fields Trust, for which the council is corporate trustee. We have summarised information from their published accounts to the right. Other subsidiaries, individually and in aggregate, are less significant.

The analysis includes entries which would be made in preparing group accounts to eliminate transactions between group components. This is in order to illustrate the extent to which group accounts would be different to the council's single entity accounts.

£m	THHL	KGVFT	Eliminations	Other adjustments	Total
Revenue	(31.9)	(1.4)	31.9		(1.4)
Expenditure	31.1	1.2	(31.9)		0.4
Deficit on provision of services	(0.8)	(0.2)	-		(1.0)
Total comprehensive income	0.7	(0.2)	(1.5)		(1.0)
Total assets	16.6	16.7	(11.0)	5.2	27.5
Total liabilities	(12.4)	(0.1)	11.0	-	(1.5)
Net assets	4.2	16.6	-	5.2	26.0

We presented a similar table in the version of this report presented to the audit committee's meeting in January 2022. The table has been updated to also include adjustments (in the column "other adjustments") that would be required on consolidation to align KGVFT's accounting policies with the council's. This quantifies and resolves an issue relating to the treatment of expenditure on the Mile End Park which was also reported in our report to the January 2022 meeting.

Officers prepared a management position paper which analyses both quantitative and qualitative considerations and concludes that the group accounts would not be materially different to the council only accounts. The paper did not consider all relationships which may fall within the group boundary and the analysis of whether entities fell within the group boundary was cursory and insufficient. The paper did not take into account other consolidation adjustments which may be required to achieve conformity with the council's accounting policies.

The net assets of group accounts would be materially different to the council's single entity accounts. As group accounts have not been prepared, we expect to qualify our report in respect of this matter (see Appendix E).



# Other areas of judgement

## NNDR appeals provision

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### Area of judgement and conclusion

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We have previously reported in relation to the original version of the accounts:

- The Council has made a provision of £1.3m for the estimated cost of appeals made by business ratepayers to their bills.
- We had been provided with an analysis prepared by an external adviser which indicates a provision requirement of £8.9m for appeals made against the 2010 ratings list, of which the Council's share would be £5.8m.
- No provision has been made for appeals against the 2017 Ratings List.

We further reported in relation to an updated version of the accounts circulated to the audit committee for the January 2021 meeting:

- Officers had increased the appeals provision at 31 March 2019 by £12.8m. This was determined as an amount equal to the Council's share of the reversal of the credit of £20m discussed earlier (resulting in the aggregate of these two adjustments having no impact on the Collection Fund surplus). The resulting provision was £14.0m (council's share £9.0m) for appeals against the 2017 ratings list and £8.0m (council's share £5.1m) for appeals against the 2010 ratings list.
- Whilst a revised provision calculation had not been prepared, the Council had supported its view that the revised provision is reasonable by reference to a comparison with other authorities. The comparison with other authorities shows that the revised provision remains towards the bottom (but no longer at the extreme) end of the range - but other points on that range might give a provision that was materially higher.

Subsequent to the meeting in April, officers have provided an updated analysis which estimates the provision required using historical information on the proportion of appeals which are successful and average refund amounts as a proportion of rateable value. The calculation (after correcting for a computational error) suggests a provision which is £3.9m (council's share £2.5m) lower than the recorded amount. As the calculation provided an evidence based estimate, we focused our work on this.

Our procedures in relation to the provision for appeals against the 2017 ratings list included making the following challenges:

- The calculation took into account appeals received up to 31 March 2019 and made no allowance for claims received or expected after this date. The council has formed the general view that it is unable to form a reliable estimate of the appeals which have not yet been made. This is because (i) ratings lists typically have different types and profile of issues relating to them (ii) the check and challenge process introduced for the 2017 ratings list is designed and expected to impact on ratepayer appetite to appeal against rateable values. As a result, there is insufficient information on which to model expected future appeals. Whilst we conclude that this view is reasonable, in this instance, due to the delay in the accounts and audit process, there is a longer period of post balance sheet information available.
  - The calculation used historical information in relation to appeals determined prior to 31 March 2019 and not the full data set available to the council. As a consequence, data sets for some appeals types are very small and may be less accurate.
  - The data includes apparent duplicates or instances where the same business ratepayer has appealed on multiple grounds and we may not expect the effect to be additive.
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# Other areas of judgement

## NNDR appeals provision

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### Area of judgement and conclusion

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In our report to the January 2022 audit committee, we estimated the effect of adjusting for these matters would be to increase the provision at 31 March 2019 by £9.8m, of which the council's share would be £6.3m. This was based on a data set at January 2021. We have subsequently obtained and analysed data through to September 2022. Whilst further appeals have been received in the intervening period, the amounts refunded have fallen well short of expectations based on experience to January 2022. As a result we have updated our estimate of the effect for adjusting for these matters to £1.6m. As the council's share of this difference (£1.0m) is clearly trivial and well within the range of possible values observed in the data, we no longer propose an adjustment.

Officers have performed a similar calculation in relation to the provision for appeals against the 2010 ratings list. Based on information used in the calculation, appeals against the 2010 ratings list had been settled subsequent to the reporting date at a cost of £11.3m. The provision made against these appeals was £6.1m (i.e. an over provision of £5.2m compared to officer's calculation and £4.7m against the recorded amount, of which the council's share is £3.0m). The outturn information in principle provides better information than the analysis of historical trends on which officers' provision calculation was based and we have therefore proposed this as an adjustment, but note that we have not been able to verify the data used in the officers' calculation. As the amounts involved are not material, we do not regard this as a material limitation of our audit scope.

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# Other areas of judgement

## Pension liability relating to the Tower Hamlets Pension Fund

### Background

The Council participates in the fund it administers, as well as the Local Government Pension Scheme fund administered by the London Pension Fund Authority (LPFA). Our comments on this page deal with the much larger liability relating to the Council's own pension fund and not to the liability relating to the LPFA fund.

The Council's pension liability is affected by the McCloud legal cases in respect of potential discrimination in the implementation of transitional protections following changes in public sector pension schemes in 2015. Subsequent to year-end, the Government was denied leave to appeal the case, removing the uncertainty over recognition of a liability. The actuary has not estimated the impact on the Council's liability but we understand has advised the Council that he does not expect the impact would be significant.

### Deloitte response

- We obtained a copy of the actuarial report for the Council Pension Fund produced by Hymans Robertson, the scheme actuary, and agreed in the disclosures to notes in the accounts.
- We assessed the independence and expertise of the actuary supporting the basis of reliance upon their work.
- We reviewed and challenged the assumptions made by Hymans Robertson, including benchmarking as shown in the table opposite.
- We assessed the reasonableness of the Council's share of the total assets of the scheme with the Pension Fund financial statements.
- We have reviewed and challenged the calculation of the impact of the McCloud case on pension liabilities.
- We performed substantive analytical procedures on movements.
- We reviewed the disclosures within the accounts against the Code.

	Council	Benchmark	Comments
Discount rate (% p.a.)	2.40%	2.36%	Centred
Consumer Price Index (CPI) Inflation rate (% p.a.)	2.50%	2.25%	At prudent end of reasonable range
Salary increase (% p.a.) (over RPI inflation)	-1.2%	n/a	Entity specific assumption. See below

### Deloitte commentary on findings to date

The Council has not adjusted the pension liability for the impact of the McCloud/Sargeant rulings, in view of the advice from its actuary that adjusting for this would not have a significant impact. The scale of impact is in particular driven by assumptions on future salary increases and the age of the membership. The salary increase assumption used to calculate the pension liability relating to the Tower Hamlets Pension Scheme is towards the lower end of what local government employers have assumed and the average age of the active membership is 52 years is comparatively high – both these factors indicating a smaller impact. We have estimated the impact to be an increase in the pension liability of £1.6m and have proposed this as an adjustment.

The lower assumed salary increase is not inconsistent with recent experience or assumptions made in the Council's Medium Term Financial Strategy and the Council has confirmed that this is their best estimate.

The investment returns in 2018/19 used in the original actuarial calculation were determined by the actuary using information at an earlier date (30 September 2018) and rolled forward on the basis of estimated investment returns for the remainder of the year. The estimate of investment returns was optimistic. The actuary has now revised his calculations based on the actual plan assets shown in the draft pension scheme accounts. This has resulted in a reduction to the net pension liability of £16m and has been corrected in the final version of the accounts.

As set out in more detail in the separate report on the pension scheme audit, stale prices by the custodian to value one of the scheme's investment. The impact, if adjusted, would be to decrease the net pension liability on the council's balance sheet by £1.0m and we have proposed this as an adjustment.

# Other areas of judgement

## Pension liability relating to the Tower Hamlets Pension Fund

### **Deloitte commentary (continued)**

The actuary has not allowed for an assumed risk premium in market information used to derive inflation rate assumptions. It is now common practice to adjust for an inflation risk premium. As this has not been done, the inflation assumptions are at the prudent end of the range we consider to be reasonable. A reduction of the interest rate to a more centred assumption would reduce the liability by approximately £80m. As this is nevertheless within a reasonable range, we have not proposed an adjustment.

The council should take account of further information which becomes available after the initial preparation of the accounts which relates to circumstances present at the reporting date:

- Although the council is aware of the Goodwin case, we understand that it has not allowed for any additional costs as a result of the ruling. In our view, it should be allowed for, as a past service cost. Based on general information that we have for LGPSs, we understand that the impact could be of the order of 0.2% of the defined benefit obligation, i.e. around c.£4m, and have recorded this as a judgemental, uncorrected misstatement in Appendix A, Audit Adjustments.
- In rolling forward the pension liability to 31 March 2020 for the purpose of the 2019/20 accounts, the council recorded other experience gains in the draft accounts for 2019/20 of £114m. The actuary has not been able to provide a detailed analysis of the experience item, but has explained that it reflects: actual experience (in relation to, for example, membership movements and pay changes) being different over the period between funding valuations (i.e. from 1 April 2016 to 31 March 2019); the effect of data updates and corrections since the 2016 funding valuation; gains resulting from the pension increase order during the year ended 31 March 2020 being lower than assumed at 31 March 2019; and the inclusion of additional liabilities from allowing for full indexation in relation to the equalisation of guaranteed minimum pay benefits. It is likely that the majority of the experience gain relates to the true-up from estimates to actuals in relation to the inter funding valuation period to 31 March 2019. Similarly, investment gains in the draft 2019/20 accounts include a gain of £29m relating to a revision to pension assets allocated to the council at 31 March 2019. As these items provide information about circumstances present at 31 March 2019, this is an adjusting post balance sheet event. As the 2018/19 and 2019/20 accounts have not been adjusted to account for the experience item in the correct period, our audit reports on both years will be qualified as the amounts involved are material.

# Other areas of judgement

## Infrastructure assets

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### Area of judgement and conclusion

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There has been discussion at a national level on the accounting for subsequent expenditure on infrastructure assets (for example the cost of renewing a road surface) and specifically whether local authorities should be assessing if there is any undepreciated cost remaining on the balance sheet for the replaced components which need to be derecognised.

The council holds infrastructure assets of £108.6m at 31 March 2019, principally in relation to highways.

It is worth noting that this is not the full cost of the council's infrastructure assets as assets in existence at the time of implementation of capital accounting systems at 1 April 1994 were brought in under transitional rules, often at nil or negligible value.

Similar to most local authorities, the council has adopted the network model for measuring depreciated replacement cost. Whilst the council's fixed asset register differentiates assets by year of purchase and by broad category (highways, street lighting, bridges, tunnels and other infrastructure), it does not differentiate by individual component. Entries are made to the records to add annual spend to the brought forward spend from previous years and to deduct depreciation. Replaced parts are generally assumed to have been fully depreciated with the result that their derecognition does not require an adjustment to the net book value. At a national level, CIPFA explains that this assumption is consistent with the economic model because local authorities have not had sufficient resources to do anything other than undertake replacement or renewal expenditure when parts of the infrastructure assets are worn out.

Whilst this assumption is not unreasonable, it relies on the assignment of appropriate useful economic lives to the broad categories of infrastructure asset to be effective. After further consideration we concluded we had insufficient assurance in relation to the assigned lives to be confident that there was not a material, undepreciated value of components at 31 March 2019 which had been replaced but which have not been removed from the register.

At a national level, retrospective changes have now been made to the financial reporting framework which resolve the issue of undepreciated cost remaining on the balance sheet for components which have been replaced:

- The government laid a statutory instrument (effective from 25 December 2022) which gives authorities the option of deeming disposals to be at nil carrying amount.
- CIPFA have issued an update to the Code which gives authorities the option of removing separate disclosure of the cost and accumulated depreciation in relation to infrastructure assets.

Officers have informed us of their intention to apply both these options and to make the necessary changes to disclosures in the draft financial statements. CIPFA have issued further guidance on disclosures and at the time of writing officers were updating the financial statements to do this.

Whilst the changes to the financial reporting framework resolve the issue of infrastructure assets remaining on the balance sheet even though they have been replaced (because the period of use is shorter than the assigned UEL), it does not resolve the issue that depreciation and carrying amount reported will be incorrect up to the point of replacement if inappropriate UELs have been used. CIPFA have published information on typical UELs to and the lives assigned by the council generally fall within the ranges in this publication. Officers are currently carrying out an exercise which looks more closely at the composition of the balance and we will conclude once we have received and reviewed this.

# Other areas of judgement

## Infrastructure assets

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### Area of judgement and conclusion

The dispensation in the statutory instrument relates only to financial years beginning on or before 1 April 2024 and will therefore require action by the council if the government does not extend this period. We therefore recommend the council remain alert to future pronouncements and ensure that its accounting records are updated and maintained in a way which enables it to comply with changes in the financial reporting framework from 1 April 2024 as well as forming a reliable basis for estimating an appropriate annual depreciation charge in the meantime.

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# Other areas of judgement

## Related parties

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### Area of judgement and conclusion

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The council is required to disclose transactions and outstanding balances with related parties. This is to ensure that financial statements contain the disclosures necessary to draw attention to the possibility that the reported financial position and results may have been affected by the existence of related parties.

Related parties are defined in the Code so as to include members and senior officers of the council (designated by the Code as members of key management personnel), their close family and entities controlled or jointly controlled by the councillors, senior officers or members of their close family.

The guidance notes to the Code also recommends this information is reported where the a councillor, senior officer or member of the close family is also a member of key management personnel of another entity and it is likely that the person would be able to affect the policies of both entities in their mutual dealings.

The council's process for identifying external interests of members involves scrutiny of the register of member interests maintained under the council's constitution and an annual circularisation of members for the purpose of related party disclosures. Officers have informed us that they do not hold returns from the annual circularisation for all members and also have not retained a full history of interests registered by members. There are also differences in scope between requirements in relation to the register of interests and the definition of related interests within the Code.

The circularisation of key management personnel in relation to their interest and those of their close family (or obtaining equivalent information from other sources, including the register of interests) is a key part of the council's process in identifying related parties and there are no alternative procedures we can perform in the absence of this information.

The council has also not been able to provide an understanding of some of the relationships which it has identified, sufficient to determine if they are related parties.

Related party transactions and balances may be material and there is likely to be significant user interest in transactions with entities controlled by elected members or where there may be actual, or a perception of, significant influence on decision-making.

As a result we regard this limitation in audit scope as material and expect to qualify our conclusion in respect of this matter (see Appendix E).

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# Other areas of judgement

## Officer remuneration

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### Area of judgement and conclusion

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The Code requires disclosure of the number of employees receiving remuneration of more than £50,000 in bands of £5,000.

The disclosure (including comparative information) has been updated as the original version did not include information for staff at schools which had opted out of the corporate payroll arrangement and the comparative information has been restated for a similar misstatement.

We have raised a number of issues with officers over the adjusted disclosure note:

- Officers prepared a revised disclosures based on returns submitted by the schools using outsourced providers. As a result of a formula error, the staff reported on these returns were counted into the disclosure twice. The council has advised that it intends to correct the disclosure for this error and we have therefore not included in the scope of our expected qualification or in Appendix A, Audit Adjustments.
- For a sample of schools we obtained payroll reports to verify returns made and found variances between the total of these reports and total staff costs in returns submitted by those schools and consolidated into the accounts. We requested information on how officers have assurance over the completeness and accuracy of the payroll reports in the light of the unreconciled differences. We have been unable to obtain a reconciliation or other evidence which provides assurance over the completeness of payroll reports.
- Information returned by certain schools was not divided into the same bands as in the note and we were unable to obtain information regarding estimates used by the Authority to allow for the differences in format.
- Remuneration disclosures are stipulated by the Accounts and Audit Regulations. These Regulations require information to be disclosed based on the legal form of contractual arrangements of staff. Therefore, even though the Code requires that staff costs for all local authority maintained schools are reported in the Comprehensive Income and Expenditure Statement, where the council is not the employer (and the person is not the employee of the council), then for the staff of schools, typically voluntary aided and foundation schools, their contract of employment will take precedence in the disclosures. We have challenged the council on how this guidance has been applied in drafting the disclosure.

The financial statements also discloses the remuneration of individual senior officers. As a result of the differences between the Authority's main accounting system and detailed payroll records, we were also unable to determine whether there were staff paid over £150,000 in the year ended 31 March 2019 who had not been disclosed in the note.

The financial statements also discloses information about the number, type and value of exit packages. The Authority did not receive returns from 33 schools for the year ended 31 March 2019 on exit payments to staff at these schools. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

Taking into account the enhanced user interest disclosures relating to staff remuneration, we regard the variances as material in the context of this disclosure and therefore expect to qualify our audit report in respect to this matter. We have included wording on the audit report modification in Appendix F which we will update once we have concluded our remaining enquiries and testing and received the final version of the disclosure.

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## 5. Use of resources

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources

## Background

Under the National Audit Office's Code of Audit Practice, we are required to report whether, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

The Code and supporting Auditor Guidance Notes require us to perform a risk assessment to identify any risks that have the potential to cause us to reach an inappropriate conclusion on the audited body's arrangements. We are required to carry out further work where we identify a significant risk - if we do not identify any significant risks, there is no requirement to carry out further work.

## Our risk assessment

We set out the risk assessment procedures we had performed and our further planned procedures in our audit planning report. We also set out in our audit planning report the two areas of significant risk identified by our risk assessment procedures performed at that point. These risks both related to the risk that matters giving rise to the previous year's qualified conclusion are also relevant to the current year. The prior year qualifications related to: an Ofsted rating of inadequate for children's services; and the council's best value improvement plan.

At the time of issue of our 2019/20 audit planning report our 2018/19 audit was ongoing. We used the report to update you on two further risks we had identified which required further evaluation to determine if they were significant risks:

- A risk relating to the council's administration of the London Borough of Tower Hamlets local government pension scheme in the light of reports which the council has needed to make to the Pensions Regulator. We have now completed that risk assessment work, including consideration of the further matters which we have recommended the council report to the Pensions Regulator and gained an understanding of the council's arrangements in relation to administration of the pension scheme. We concluded on the basis of this further risk assessment work that there was not a significant risk in respect of our value for money conclusion and therefore have not performed further work.
- We also determined that the volume and nature of misstatements identified during the audit process for the 2018/19 financial statements, as well as the time taken to investigate and resolve issues identified, represented a risk of weaknesses in financial reporting arrangements. We concluded this was a significant risk to our value for money conclusion.

We have now completed other risk assessment work, including reviewing the revised version of the 2018/19 Annual Governance Statement and internal audit reports issued as part of both the 2018/19 and 2019/20 internal audit programmes. On the basis of this further risk assessment work we have identified the following additional risk to our value for money conclusion:

- There is a risk that there is a material weakness in arrangements to manage risks effectively and maintain a sound system of internal control.

We set out information on the significant risks and our response on the following pages.

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)

Risk title	Ofsted rating of inadequate for children's services
<b>Risk description</b>	<p>In their inspection report published on 7 April 2017, Ofsted rated children's services in Tower Hamlets as "inadequate". This overall assessment incorporated inadequate ratings for the following assessment categories: children who need help and protection; and leadership, management and governance. Our predecessor concluded that these circumstances provided evidence of weaknesses in proper arrangements.</p> <p>There is a risk that the matters giving rise to the previous year's qualified conclusion are also relevant to the current year.</p>
<b>Procedures performed</b>	<p>We have read the original inspection report and reports from subsequent monitoring visits and discussed with the Corporate Director responsible for children's services.</p> <p>We have also read the Council's disclosures made about this issue in the Annual Governance Statement.</p>
<b>Conclusion on risk</b>	<p>We conclude that our VFM conclusion should be qualified in respect of this matter. This is because:</p> <ul style="list-style-type: none"> <li>• Children's services are an important and high profile service</li> <li>• The Council's rating from its regulator was "inadequate" during 2018/19</li> <li>• Whilst it is apparent from both the Council's own internal monitoring and monitoring visits that the CQC have carried out that improvements have been made, these arrangements were not in place throughout the year and in particular the Ofsted inspection reports from the early part of 2018/19 identify some areas where there had been limited improvement.</li> </ul>

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)

Risk title	Financial reporting arrangements
<b>Risk description</b>	<p>In our 2019/20 audit plan, we identified an additional risk in relation to financial reporting.</p>
	<p>The Council's statement of accounts has been significantly delayed and there has been a period of uncertainty over the true financial performance in 2018/19 and amount of resources available at 31 March 2019 while officers investigate and quantify potential or actual misstatements in the draft statement of accounts. The Council has recognised in its updated draft annual governance statement for 2018/19 that there significant deficiencies in controls over financial reporting.</p> <p>There is a risk that these matters indicate material weaknesses in financial reporting arrangements. Reliable and timely financial reporting that supports the delivery of strategic priorities is a key component of informed decision-making.</p>
<b>Procedures performed</b>	<p>We have evaluated:</p> <ul style="list-style-type: none"> <li>• the volume, size and significance of adjustments required to the original version of the statement of accounts and their cause.</li> <li>• the control observations made in the course of our work.</li> <li>• the report commissioned by the Council into the 2018/19 accounts closure and audit process.</li> </ul>

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)

## Risk title

## Financial reporting arrangements (continued)

### Conclusion on risk

We conclude that our VFM conclusion should be qualified in respect of this matter. This is because:

1. The length of time taken to provide information and explanations to support transactions in the accounts; to investigate issues which have arisen; and prepare amended financial statements leading to an expected delay in excess of three years from the target date for issue of our opinion of 31 July 2019.
2. The volume, size and pervasiveness of corrections required in relation to both current and prior period information reported in the statement of accounts originally authorised for issue in May 2019, in particular correction to or prolonged uncertainty over the amount of usable reserves available to meet future spending requirements and therefore strategic objectives (or timing in recognition of these resources) (see the appendix to this document for a summary of the changes made). Of particular note are:
  - In the original accounts a reversal of a creditor was recorded in the general fund and not the collection fund. The correction of the error, together with the correction of an error in the estimate for appeals to business rates, resulted in a reduction in council revenue resources of £20m.
  - The earlier recognition of capital resources of £30m in respect of contributions from leaseholders to major works and £20m due from developers in respect of community infrastructure levy and other government grants of £26m.
  - The restatement of prior period accounts, including the restatement of PPE by £425m at 1 April 2017 and £196m at 31 March 2018.
  - The Council commissioned an independent report into the accounts closure process which identified weaknesses in the accounts closure process, including weaknesses in the leadership of that process.
  - These and other weaknesses in related accounting and business processes, including the following resulted in material misstatement of the accounts and delays in the accounts and audit process:
    - Inadequate controls in areas of significant risk of material misstatement which resulted in material misstatement including controls over journals, controls over the valuation of properties and controls over the calculation of estimates.
    - Inadequate control reconciliation processes, in particular in relation to the reconciliation of the schools disbursement account resulting in prolonged uncertainty over the amount of schools cash balances.
    - Inadequate VAT accounting processes resulting in the under claim for input tax of £4m.
    - Inadequate training of staff resulting in incorrect application of the Council's accounting policies, in particular in relation to the recognition of income.

We note that this has also been identified as a significant control deficiency in the council's annual governance statement. However, the wording requires updating to reflect the final position and we recommend that this is done.

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)

Risk title	System of risk management and internal control
<b>Risk description</b>	<ul style="list-style-type: none"> <li>• There is a risk that there is a material weakness in arrangements to manage risks effectively and maintain a sound system of internal control. This is because:               <ul style="list-style-type: none"> <li>◦ Whilst in respect of 2018/19, the Head of Internal Audit was able to provide reasonable assurance that the council had adequate systems of governance, risk management and internal control, the scope of that opinion was limited as the internal audit programme had not addressed IT risks. In addition, arrangements were not in place for the independent audit of risk and insurance functions which were the responsibility of the Head of Internal Audit during the 2018/19.</li> <li>◦ There were 11 (37%) internal audit reviews where the arrangements under review were given a rating of limited assurance.</li> <li>◦ In 2019/20, the Head of Internal Audit was able to provide only limited assurance that the council had adequate systems of governance, risk management and internal control. The 2019/20 opinion took into account: the results of work which fell outside the scope of the opinion given in 2019/20 (including audit of IT risks and the system of risk management); audits relating to field work carried out in 2018/19 but where the report had not been finalised by the time of the Head of Internal Audit opinion in July 2019; audits selected for review in 2019/20 as part of the cyclical audit programme; and other matters which have subsequently come to light from other review or management processes, including in relation to financial reporting and pensions administration. It is likely that some or all of the weaknesses which resulted in the limited assurance opinion in 2019/20 were also present in 2018/19.</li> <li>◦ The annual governance statement reports on nine "significant governance issues".</li> </ul> </li> </ul>
<b>Procedures performed</b>	<p>We have evaluated:</p> <ul style="list-style-type: none"> <li>• The significance of the subject matter and findings reported for individual audits given a limited assurance rating by internal audit (both in the 2018/19 and, where relevant, the 2019/20 internal audit programmes)</li> <li>• The significance of governance issues reported in the annual governance statement</li> <li>• Considered other matters, including progress on past recommendations and the resourcing and scope of the internal audit programme.</li> </ul>
<b>Conclusion on risk</b>	<p>We conclude that our VFM conclusion should be qualified in respect of this matter. This is because:</p> <ul style="list-style-type: none"> <li>• whilst the council has designed and implemented risk management arrangements these are not operating effectively; and</li> <li>• the internal audit programme and annual governance statement process has identified a significant number of governance issues and internal control deficiencies in areas which are significant either quantitatively or where the council is exposed to material reputational damage. Some aspects of governance arrangements were not included in the scope of the internal audit programme due to resource constraints.</li> </ul>

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)

Risk title	Best value improvement plan
<b>Risk description</b>	<p>During 2017/18, the Council was subject to Directions issued by the Secretary of State which required the Council to set up a Best Value Improvement Board; submit quarterly progress reports on the Best Value Improvement Plan to the Secretary of State; and set up an independent review of the achievement of the Best Value Improvement Plan with a report to be provided to the Secretary of State by 1 August 2018.</p> <p>Our predecessor noted that not all actions were confirmed as completed or on track and anticipated that the impact of the work would not yet be embedded and concluded that these circumstances provided evidence of weaknesses in proper arrangements.</p> <p>There is a risk that the matters giving rise to the previous year's qualified conclusion are also relevant to the current year.</p>
<b>Procedures performed</b>	<p>During 2018/19, the Council completed the actions specified in Directions. On the basis of the peer challenge review submitted to the Secretary of State, the Directions were lifted.</p> <p>Our conclusion is given in respect of arrangements throughout the year and not just at the year end. We have reviewed the peer challenge review report and considered the scope and findings. We have also considered the significance of issues open at the start of the year and the timeline for their closure during the year.</p>
<b>Conclusion on risk</b>	<p>The areas of concern in the original PwC report do not involve individually significant areas of financial spend or key services but raised important questions about governance which are relevant to the sub criterion of "Acting in the public interest, through demonstrating and applying the principles and values of sound governance". These were developed further around this same theme within the Best Value Improvement Plan.</p> <p>It is apparent that in the specific areas covered by the original PwC investigation, and the Best Value Improvement Plan, that the Council has made significant progress in earlier years, resulting in the end of the intervention and the return in 2017/18 of the Council's functions (which had been carried out since 2015 by special commissioners).</p> <p>Whilst we recognise that a number of the actions were not complete at 1 April 2018, these were not individually significant to our conclusion or in aggregate. The LGA peer review (carried out in the first quarter of 2018/19) concluded satisfactorily on each of these areas and, of more significance, concluded there had been a significant improvement in the culture of the organisation.</p> <p>We have therefore concluded that these circumstances do not provide evidence that the Council does not have proper arrangements in 2018/19.</p> <p>The peer review identified other issues, which in part reflect the need to scale back the Council's "belt and braces" response to the original PwC investigation and subsequent intervention (including retention of decision making at a senior level to enable more agile decision-making), together with new issues raised by the Peer Challenge team, including development of IT. The Council has agreed an action plan to address the issues raised by the review (including a review of the scheme of delegation and wider constitution) which are being monitored by a member committee set up for this purpose and has earmarked reserves to support the IT development. Therefore we have not identified these matters as significant weaknesses in arrangements relevant to our conclusion.</p>

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)

## **Conclusion**

We expect that our conclusion will be qualified on an “except for” (and not “adverse”) basis in respect of three matters:

- As reported in our July 2019 report to the audit committee, our report will be qualified in respect of children’s services as Ofsted’s 2018 report and subsequent monitoring reports provide evidence (notwithstanding the improvement trajectory, subsequently confirmed in their re-inspection report) that proper arrangements to secure to secure economy, efficiency and effectiveness in the use of resources were not in place throughout the whole of the period covered by our conclusion.
- Financial reporting arrangements in view of the volume and size of changes required to the original version of the statement of accounts and time taken to resolve issues identified.
- Risk management and the system of internal control in view of weaknesses identified in the operating effectiveness of the system of risk management and the number and significance of issues identified in the system of internal control.

We have set out the expected form of the conclusion in Appendix E.



## 6. Control observations

# Control observations

During the course of our audit, we have identified a number of internal control findings. We have set out below our observations and recommendations. In some instances, this repeats information previously reported but we have included here in order to give a complete picture in this report of our key findings from the audit.


Reflecting the volume, significance and pervasiveness of misstatements identified during the course of the audit, the number and significance of these control observations are greater than we report at most other local authorities.

The common root cause of these observations has been a lack of capability and capacity with the finance function which has led to: a lack of capability and/or desire to understand and analyse the accounting basis for transactions; the failure to establish an effective system of quality assurance; and weaknesses in financial control and reporting, including controls over general ledger maintenance, documentation of key judgements and compliance with presentation and disclosure requirements



in preparing the statement of accounts.

Over the last two years, the interim Corporate Director – Finance and Resources has reported progress on an improvement plan which is designed to address these and other underlying systemic issues. The council has also invested time in investigating and responding to specific accounting issues identified in the course of the audit and building better processes to prevent their reoccurrence. However, as a result of the timing of many of these actions, we have needed to repeat many of these same points in our equivalent report on the 2019/20 council audit.



Notwithstanding this, there were clear improvements in the quality of information received for the purpose of our 2019/20 audit, although it is also apparent that some disciplines, including preparation of detailed accounting papers and effective quality assurance processes are yet to be embedded and the council still needs to demonstrate that it can carry out its annual financial reporting tasks at pace, including responding to audit requests.

Area	Observation and recommendation
<b>Quality of draft financial statements</b> 	<p><b>Observation</b></p> <p>The initial draft statement of accounts which were published for public inspection and presented for audit were not of the expected standard. Issues noted included:</p> <ul style="list-style-type: none"><li>• Narrative report not compliant with Code guidance</li><li>• Inconsistencies between primary statements and notes in the financial statements;</li><li>• Inconsistencies between notes in the financial statements</li><li>• Cash flow statement notes which were incomplete</li><li>• Accounting policies not updated for the adoption of IFRS 9 and IFRS 15</li><li>• Accounts disclosures not updated for the adoption of IFRS 9 and IFRS 15 and other 2018/19 changes in the Code</li><li>• Omission of other disclosures required by the Code (a disclosure checklist was completed but did not identify all of the disclosure omissions).</li></ul> <p>Together these indicate significant deficiencies in the financial reporting and close process.</p> <p><b>Recommendation</b></p> <p>We recommend the Council reviews the year-end reporting and close process, including:</p> <ul style="list-style-type: none"><li>• preparation of a skeleton draft of the financial statements ahead of year-end, reviewed against the Code for any changes in the year and for the disclosure requirements for any new or changed activities of the Council;</li><li>• documentation and quantification of judgments in respect of materiality of disclosure requirements in preparing the accounts;</li><li>• Line-by-line review of the completed CIPFA disclosure checklist by a second officer;</li><li>• documented and reviewed internal checks of internal consistency;</li><li>• completion of the CIPFA “pre-audit checks on draft year-end accounts” checklist; and</li><li>• documented and reviewed internal tie back and referencing of the draft financial statements to supporting working papers.</li></ul>



# Control observations (continued)

Area	Observation and recommendation
<b>Preparation of accounting papers</b> 	<p><b>Observation</b></p> <p>Accounting papers were not prepared to explain and support key judgements and estimates, including the ongoing pertinence of judgements made in previous years or were not sufficiently detailed to explain and support those judgements and estimates. It is good practice (and the expectation of the Financial Reporting Council) for organisations to prepare accounting papers in respect of key matters in the application of accounting standards, in particular for matters of judgement or of estimation complexity. Typically these would include consideration of the relevant requirements of the accounting standards and the Code, the fact pattern (including details of relevant terms of contracts etc.), an assessment of how the standards apply in this context, consideration of potential alternative treatments, the proposed approach to measurement/calculation of accounting entries required, and the required disclosures.</p> <p>The preparation of accounting papers both supports accurate financial reporting, including facilitating both internal and external review and challenge, and provides a resource to ensure institutional knowledge in the organisation.</p> <p>We make additional specific observations about the management position paper on group accounts at page 30.</p> <p><b>Recommendation</b></p> <p>We recommend the Council adopts an approach of preparing papers for any key accounting judgements or issues arising. We also recommend that accounting papers are presented to the same meeting of the audit committee at which the draft statement of accounts are approved (if not earlier) for scrutiny and to inform the audit committee's approval of the draft statement of accounts</p>
<b>Accounts closure - resourcing and processes</b> 	<p><b>Observation</b></p> <p>Very few of the requested documents were provided at the start of our original audit visit. We needed to request the finance team to follow-up on a number of items provided as breakdowns did not tie to the trial balance, were not in the level of detail requested, or it was not clear how the working papers provided related to the request. Subsequent requests for information have not been turned around on an acceptable timescale.</p> <p>The accounts closure plan allocated preparer and reviewer to each task, including control account reconciliations. In a number instances the same individual was allocated as both preparer and reviewer for a particular task.</p> <p>Errors, for example in the accounting for community infrastructure levy, the recognition of grant income and contributions from leaseholders to major works, the preparation of school bank reconciliations and cut-off of capital expenditure between periods provide evidence that officers did not have a full understanding of the tasks assigned to them.</p> <p>Errors were identified in supporting working papers which we would expect to be identified through a review by a second officer.</p> <p><b>Recommendation</b></p> <p>We recommend that the Council considers the resourcing of the closure process, the assignment of tasks, the training needs of those involved in the process and the quality assurance processes to be applied to the draft financial statements and supporting working papers. We also recommend the Council considers whether there are year end processes which can be streamlined or pulled forward to earlier in the year.</p>




# Control observations (continued)

Area	Observation
<b>New accounting standards – IFRS 9 and 15</b> 	<p><b>Observation</b></p> <p>Whilst we understand that officers discussed the impact of adoption of the new standards during the closure process, they did not initially prepare accounting papers on the transition to IFRS 9 and 15. An accounting paper was subsequently prepared to support the transition to IFRS 15, but contained various errors. The initial draft accounts were not updated for changes in disclosure requirements from IFRS 9 and 15. The recognition of leaseholder contributions to major works was not in accordance with IFRS 15 and required adjustment.</p> <p>The council has not made all of the disclosures required by IFRS 15, in particular the amount of revenue and assets and liabilities within the scope of IFRS 15.</p> <p><b>Recommendation</b></p> <p>We recommend:</p> <ul style="list-style-type: none"> <li>• Officers consider what changes are required to its chart of accounts to facilitate identification and reporting of the amount of income, assets and liabilities within the scope of IFRS 15</li> <li>• going forwards the Council prepares a clear project plan for the implementation of new or changed accounting guidance. We recommend that accounting papers are prepared to record officers' rationale in areas of judgement and these are subject to a management review process.</li> </ul>
<b>Reconciliation of general ledger control accounts and segregation of duties</b> 	<p><b>Observation</b></p> <p>General ledger control accounts were not reconciled in a number of instances and reconciling differences adequately resolved. This resulted in various misstatements. This included the control accounts for schools bank accounts; corporate bank accounts; utility costs; Northgate system; and grant control accounts. A control account was not set up for three bank accounts.</p> <p><b>Recommendation</b></p> <p>We recommend:</p> <ul style="list-style-type: none"> <li>• A separate control account is set up for each bank account</li> <li>• Responsibility for each control account is assigned to a named preparer and reviewer (with those roles allocated to different officers)</li> <li>• The frequency and timescale for preparation and review of reconciliations is set down in written instructions to staff</li> <li>• A monitoring arrangement is designed to ensure reconciliations are carried out and reviewed in accordance with instructions and any exceptions reported to senior management for action.</li> </ul>

# Control observations (continued)

Area	Observation
<b>Valuation of properties</b> 	<p><b>Observation</b></p> <p>The valuation of properties is dependent on officers' assumptions (or input from officers in forming assumptions) including the location and functional obsolescence of the existing properties and information provided by officers, including the number, type and condition of council dwellings and the floor space of schools. A paper was not prepared and reviewed setting out assumptions made (or information provided to the valuer to inform their formation of assumptions).</p> <p>There are also no formal controls operating to ensure the completeness and accuracy of other information provided to the valuer.</p> <p>We have not been provided with information about the Council's review of the reasonableness of the outcome of the valuation in 2018/19.</p> <p>In our April 2021 report we made a number of observations about the valuer's reports. In addition we note in relation to the valuation of council dwellings that, where only limited comparable evidence is available and/or an expected value range is used to determine appropriate beacon values, it would be useful for any comments from agents to be summarised in the spreadsheet to demonstrate the valuer's reasoning in selecting the beacon value.</p> <p>The calculation and recording of entries relating to the valuation is performed in the fixed asset register. The fixed asset register is maintained on an excel spreadsheet. Typical spreadsheet controls we would expect to see over the design and maintenance of a spreadsheet used for the initiation and recording of significant financial transactions have not been adopted.</p> <p>The process to support the assumption in the original version of the accounts that there had not been a material change in valuation of assets not selected for revaluation at the reporting date was not adequate.</p> <p>The valuation at 31 March 2019 was determined by officers from the finance team using information on market changes during 2018/19 provided by the valuer. We have set out at page 14 our concerns over the way in which the closing carrying value was determined.</p> <p>The closing valuation for one asset was incorrect as information for the preceding reporting date was entered in error.</p>
<b>Elimination of internal recharges</b> 	<p>Internal recharges should be eliminated from the presentation of income and expenditure in the Comprehensive Income and Expenditure Statement. The process of doing this is complicated because the coding structure adopted does not enable the finance team to readily identify postings within income and expenditure. Our testing identified charges of £47m which had not been fully netted down.</p> <p>We recommend that the coding structure is amended to facilitate elimination of internal recharges in the Comprehensive Income and Expenditure Statement and to readily demonstrate that this has been done in full.</p>



# Control observations (continued)

Area	Observation
<b>Valuation of properties (continued)</b> 	<p><b>Recommendation</b></p> <p>We recommend the Council:</p> <ul style="list-style-type: none"> <li>• prepare and maintain a schedule which sets out the information which is provided to the valuer (including management assumptions and information provided to the valuer to inform assumptions made by the valuer) and identifies the controls over each category of information.</li> <li>• design and document their review of the outcome of the valuation. This would require formalising the criteria for selection of individual asset values for investigation, consistently applying these criteria and then documenting the conclusion on exceptions for review and approval.</li> <li>• discuss the various points made about the valuation report and supporting working papers and request the valuer addresses these in future years.</li> <li>• implement standard spreadsheet controls within the fixed asset register. This principle should be applied to any other spreadsheets used in the preparation of any other significant information in the statement of accounts.</li> <li>• prepare a paper to support the decision not to value particular assets prior to publishing its draft statement of accounts.</li> <li>• ensure all valuations are performed and implemented by a qualified valuer to avoid/minimise the extent of management judgement required in updating the accounts (e.g. in applying the outcome of a market review)</li> <li>• Consider what controls should be implemented to prevent/detect data input errors.</li> </ul>
<b>Classification of expenditure as capital</b> 	<p><b>Observation</b></p> <p>We were not able to identify a documented internal control to prevent or detect the incorrect classification of revenue spend as capital.</p> <p>Whilst we did not identify any exceptions, the classification of expenditure between revenue and capital can involve the exercise of judgement. Projects which are of a capital nature can involve both revenue and capital elements which need to be accounted for differently.</p> <p><b>Recommendation</b></p> <p>We therefore recommend the Council implements such a control.</p>
<b>Annual review of asset lives</b> 	<p><b>Observation</b></p> <p>Accounting standards require that the estimate of the useful life of an item of property, plant and equipment is reviewed at least at the end of each financial year. If expectations differ from previous estimates, the asset life should be revised. Asset lives for infrastructure assets were not subject to review and required amendment following consultation with the relevant service department.</p> <p><b>Recommendation</b></p> <p>Schedule an annual review of asset lives into the work programme of the finance team. That work should involve consultation with the relevant service team.</p>

# Control observations (continued)

Area	Observation
<b>Journals</b>	<b>Observation</b> <p>Journals either pass through workflow approval process or are processed through a separate “bulk upload” process. The latter are principally posted to the general ledger system by officers in the Operations team based on requests submitted by other teams in finance.</p> <p>Checks are performed by the Operations team to confirm that journals have been accurately entered to the general ledger system in accordance with the submitted request, but the scope of these checks does not include confirming that the journal is for a valid business and accounting reason and that the values and proposed entries are accurate. The Operations team does not hold a list of individuals authorised to submit a journal request and are not required to see evidence that the journal has been approved by a second officer. Journals may therefore be posted by the Operations team which have not been subject to review and approval within the originating team. Individual teams may have established their own working practices relating to the approval of journals, but as the Council has not communicated common standards to be applied, arrangements for the approval of journals and controls to ensure compliance with those standards, if any, will not be consistent across teams. As standard documentation for journal requests is not required, a record of who has prepared and who has approved the journal request is not consistently maintained and in practice it has not been possible to determine in all cases whether the journal has been approved and who has prepared and who has approved the journal before submission to the Operations team. As a result it is not possible in all cases to determine whether, in practice, there has been appropriate segregation of duties or whether the journal has been approved by an officer who is authorised to do so.</p> <p>A small number of officers have been given access to raise this journal type within the Chief Accountant’s team. There are no controls to prevent the posting of journals by these individuals which have not been approved by a second officer who is authorised to do so.</p> <p>In relation to other journal types which pass through a workflow approval process, some processes use CSV files which are picked up by automated processes on Agresso. If inappropriate users were given access to the CSV files, then the contents can be altered prior to being picked up by the automated processes scheduled and posted to general ledger.</p> <b>Recommendation</b> <p>We recommend that the Authority re-visits which journal types and amounts can be posted without approval by a second officer and implement controls which prevent or detect the posting of journals which have not been approved in accordance with those agreed arrangements.</p>

# Control observations (continued)

Area	Observation
<b>Recognition of grants and contributions</b> 	<p><b>Observation</b>  Errors were identified in the recognition of grants and contributions.</p> <p>The appropriate recognition of grants and contributions depends on the identification of conditions within the grant agreement. Correctly distinguishing between conditions and restrictions can involve judgement.</p> <p><b>Recommendation</b>  We recommend:</p> <ul style="list-style-type: none"> <li>• grant agreements are reviewed on notification of entitlement and a preliminary assessment made of whether there are conditions attached to the grant. This assessment is documented and subject to review by a second officer.</li> <li>• The decision is reflected in the type of general ledger code set-up to record the grant.</li> <li>• For grants or contributions involving conditions, a working paper is prepared showing the calculation of the amount to be recognised and which is subject to review by a second officer.</li> </ul>
<b>IT controls</b> 	<p><b>Observation</b>  We noted:</p> <ul style="list-style-type: none"> <li>• Password parameters applied to access the active directory do not match company policy in the following categories:  Minimum Length and Expiry</li> <li>• A data leakage risk assessment has not been performed</li> <li>• User access reviews are not performed.</li> </ul> <p><b>Recommendation</b>  We recommend an action plan is developed to address these weaknesses.</p>



# Control observations (continued)

Area	Observation
Other matters	<p>We note the following additional observations:</p> <ul style="list-style-type: none"> <li>• Employment contracts held by the council for three sampled employees had not been signed by the employee. This may cause issues in enforcing particular contractual terms.</li> <li>• Our sample testing identified an invoice raised in October 2014 for £298k, due from NHS England, where insufficient information was held to support for audit purposes that the amount was valid and recoverable. Also as a consequence there was insufficient information to enforce its recovery.</li> <li>• Our journals testing identified a single journal which was out of balance (a net credit of £2,595) due to the omission of a VAT entry. Officers have informed us that Agresso should automatically an additional entry to the Error Suspense Account (E9999) where the journal is out of balance but this did not occur. This should be followed up with the supplier.</li> <li>• Leaseholder contributions to major works did not include an accrual for contractor retentions where relevant. Whilst the effect at 31 March 2019 was clearly trivial (£1.1m) and we have therefore not proposed an adjustment, this should be considered for future periods in the event that is more significant.</li> <li>• The transfer to schools reserves in 2018/19 had not been reconciled to the aggregate of surplus/deficits on individual schools, required significant additional analysis to do so and could not be reconciled in full. Coding should be reviewed to facilitate such a reconciliation.</li> <li>• Sample items included land which was still registered in the name of the previous holder (the London Residuary Body and the Inner London Education Authority). We recommend the position is regularised.</li> </ul>

Low Priority

Medium Priority

High Priority

The purpose of the audit was for us to express an opinion on the financial statements. The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters being reported are limited to those deficiencies that we have identified during the audit and that we have concluded are of sufficient importance to merit being reported to you.

## 7. Purpose of our report and responsibility statement

# Purpose of our report and responsibility statement

## Our report is designed to help you meet your governance duties

### What we report

Our report is designed to help the Audit Committee and the Board discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA (UK) 260 to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes the results of our work on key audit judgements and other insights we have identified from our audit.

### What we don't report

As you will be aware, our audit was not designed to identify all matters that may be relevant to the Council.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

### The scope of our work

Our observations are developed in the context of our audit of the financial statements. We described the scope of our work in our audit plan and again in this report.

This report has been prepared for the Audit Committee and Council, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose.

We welcome the opportunity to discuss our report with you and receive your feedback.

The logo for Deloitte LLP, featuring the company name in a stylized, handwritten-style script.

**Deloitte LLP**

St Albans

20 January 2023

# Appendices

# Appendix A: Audit adjustments

## Unadjusted misstatements

The following uncorrected misstatements have been identified up to the date of this report which we request that you ask management to correct as required by ISAs (UK).

		Debit/ (credit) in surplus on provision of services £m	Debit/ (credit) in net assets £m	Debit/ (credit) prior year reserves £m	Debit/ (credit) OCI/Equity £m	Gross expenditure on services £m
<b>Current year misstatements</b>						
Impact of McCloud/Sargeant rulings	[1]	1.6	(1.6)	-	-	1.6
Impact of stale prices in pension assets	[2]	-	(1.1)	-	1.1	-
NNDR appeals provision	[3]	3.0	(3.0)	-	-	-
Roll forward of valuation of council dwellings	[4]	4.0	(4.0)	-	-	4.0
Impact of Goodwin case	[5]	4.0	(4.0)	-	-	4.0
Unreconciled difference on schools cash control account	[6]	(1.3)	1.3	-	-	(1.3)
Incorrect net down of income and expenditure (£1.5m)	[7]	-	-	-	-	(1.5)
Error in unit building cost input	[8]	-	1.4	-	(1.4)	-
Reduce provision for H&SE penalties	[9]	(1.9)	1.9	-	-	(1.9)
<b>Total current year misstatements</b>		<b>9.4</b>	<b>(9.1)</b>	<b>-</b>	<b>(0.3)</b>	<b>4.9</b>
<b>Prior year misstatements identified in the current year</b>						
Invalid PFI grant balance	[10]	(2.2)	-	2.2	-	-
Error in unit building cost input	[8]	-	-	(1.0)	1.0	-
Unreconciled difference on schools cash control account	[6]	(2.7)	-	2.7	-	(2.7)
<b>Total prior year misstatements identified in the current period</b>		<b>(4.9)</b>	<b>-</b>	<b>3.9</b>	<b>1.0</b>	<b>(2.7)</b>
<b>Total</b>		<b>4.5</b>	<b>(9.1)</b>	<b>3.9</b>	<b>0.7</b>	<b>2.2</b>

# Appendix A: Audit adjustments

## Unadjusted misstatements

[1] As explained on pages 35-36, the pension liability does not take into account the impact of the McCloud/Sargeant rulings.

[2] Stale prices have been used by a custodian to value one of the pension scheme's assets, resulting in an overstatement of plan assets.

[3] As explained on pages 33-34, the NNDR appeals provision does not take into account information received after the reporting date which is relevant to the circumstances at the reporting date.

[4] Council dwellings were revalued by a valuer with an effective date of 1 April 2018. The council's finance team rolled this forward to 31 March 2019 by adjusting for additions, disposals, depreciation and transfers to other categories during 2018/19, together with applying an index, advised by the valuer, to take account of market change over the year. The approach results in adding to the original valuation the excess of additions over depreciation (£4m). This methodology does not allow for the effect of the social housing discount applied in arriving at the existing use valuation for social housing and assumes that the effect on the valuation of spend on replacements has outweighed the impact of wear and tear and passage of time – which is not supported.

[5] A legal challenge has been made against the Government in respect of unequitable benefits for male dependants of female members (based on service after 1988) following the earlier Walker ruling. An Employment Tribunal on 30 June 2020 has upheld the claim. This should result in an additional liability being recognised. Although tribunal ruling was not made until 2020/21, in our view the tribunal decision should be treated as an adjusting event, with the estimated impact recognised as a past service cost in the 2018/19 Comprehensive Income and Expenditure Statement. Based on general information that we have for LGPS's, we understand that the impact could be of the order of 0.2% of the defined benefit obligation, i.e. around c.£4m.

[6] The total of the cash books for individual schools at 31 March 2019 is £1.3m higher than the general ledger control account and at 31 March 2018 is £2.7m lower than the general ledger control account. Officers have not been able to reconcile these differences. As the council is only able to support the individual cash book amounts, we have proposed adjustments to agree to the totals of the individual cash book amount.

[7] A journal was incorrectly posted which had the effect of reducing income and expenditure in the service analysis in the Comprehensive Income and Expenditure Statement by £1.5m on the Corporate costs and central items line.

[8] In the revised valuation for certain schools, the build cost for the wrong category of school (secondary, primary etc) was used. This had the effect of undervaluing schools by £1.4m, £1.0m and £2.7m at 31 March 2019, 31 March 2018 and 1 April 2017, respectively.

[9] The council made provision for possible Health and Safety Executive penalties. One case was determined in 2020/21 for a lower amount than provided and in a second case a penalty is no longer considered probable given the elapse of time.

[10] PFI grant is received in full in the year to which it relates and should be recognised in full in that year. As a result, no amounts should be carried forward at year end. Amounts were incorrectly carried forward in short term debtors at 31 March 2018 and 1 April 2017 of £2.2m and £3.1m, respectively.

# Appendix A: Audit adjustments

## Unadjusted misstatements

In addition, we bring to your attention the following possible misstatements. We have not proposed that the financial statements are adjusted for these items as these are projections or other estimates of the possible misstatement and we are not able to quantify the actual adjustment, if any, which is required. We have taken account of these in evaluating whether the accounts are materially misstated as a whole and included a representation in the management representation letter to confirm management's view that any adjustment required to correct these misstatements is not material in aggregate with proposed adjustments in the previous table.

	Note	Debit/ (credit) in CIES £m	Debit/ (credit) in net assets £m	Debit/ (credit) prior year reserves £m	Debit/ (credit) OCI/Equity £m	Expenditure on gross services £m
Accruals which are not valid or in excess of amount due	[1]	(2.5)	2.5	-	-	(2.5)
Expenditure in excess of amount payable	[2]	(6.8)	6.8	-	-	(6.8)
Precepts recorded twice in expenditure analysis (£1.9m)	[3]	-	-	-	-	-
Incorrect set of income against expenditure (£14.1m)	[4]	-	-	-	-	14.1
Invalid items in schools bank account reconciliations	[5]	(4.1)	4.1	-	-	(4.1)
Differences between detailed pay records and general ledger (£1.4m)	[6]	-	-	-	-	-
Discrepancies between floor plans and build areas provided to valuer	[7]	3.1	(3.1)	-	-	-
<b>Total current year projected misstatements</b>		<b>(10.1)</b>	<b>10.1</b>	<b>-</b>	<b>-</b>	<b>0.8</b>

In addition, The council has restated opening balances and comparative information as follows:

- An increase in schools' reserves at 1 April 2018 by £2.1m to agree to the aggregate of individual returns from schools, after correcting adjustments for known errors in the returns.
- A reduction in the General Fund balance at 1 April 2018 by £7.8m to account for the impact of adjustments made to other asset, liability and reserve accounts.
- An increase in expenditure for the year ended 31 March 2018 by £7.0m and reduced income by £0.3m.

The council has not been able to provide full information on the changes made to income and expenditure in 2017/18 or to the amount of reserves at 31 March 2018, including a full reconciliation of opening to closing schools reserves. As a result, the allocation of these entries between schools and general fund reserves and between income and expenditure may not be accurate.

# Appendix A: Audit adjustments

## Unadjusted misstatements

[1] Officers carried out an exercise to evaluate whether accruals were valid and recorded in the correct amount in response to errors identified by our sample testing. The exercise did not cover the whole of the population. Errors identified by the exercise were corrected. The projected error in the part of the population not covered by officers' exercise was £1,450k. In addition, the exercise identified accruals totalling £687k where we were not able to obtain sufficient information to determine whether the accrual amount was valid and recorded in the correct amount.

The further projected error relating to items which could not be supported is £363k. The total projected error for accruals which are not valid or could not be substantiated is £2,499k.

[2] Sampling of other service expenditure identified a payment which was £155k higher than the amount due but had been expensed in full. The projected error across all accruals is £6.8m. No similar errors were identified in our sample.

[3] In expenditure analyses provided to us, expenditure on precepts and other levies of £1,859k is included twice. We have not been able to determine what adjustment, if any, is required in respect of this item.

[4] Sampling of other service expenditure identified grant income which had been incorrectly set off against expenditure of £521k. The projected error across all credits to other service expenditure is £14.1m.

[5] Our sample of reconciling items in individual cash book reconciliations identified a high rate of error (approximately half) at 31 March 2019, where payments were deducted from the cash balance before their release, resulting in the understatement of both cash and short term creditors or included invalid entries which should be released to revenue accounts. Officers have not quantified the error and therefore no adjustment has been made. The amount of unpresented cheques and BACS at 31 March 2019 was £8,127k, representing the maximum amount of error at each reporting date and the projected error approximately half of this amount, this projection being the amount included in the table.

[6] Detailed payroll reports for a sample of schools which had opted out of the council's corporate payroll arrangement could not be reconciled to the council's general ledger. The amounts recorded in the detailed payroll records for this sample was £184k more than the amount recorded in general ledger. The projected variance across all schools which had opted out of the corporate payroll arrangement was £1.4m.

[7] Discrepancies were identified between floor plans and build area information provided by the council to the valuer and used as an input in the valuation. The projected variance across remaining assets was £3.1m.



# Appendix A: Audit adjustments

## Corrected misstatements

Officers have corrected for various misstatements identified over the course of the audit. We nonetheless communicate them to you to assist you in fulfilling your governance responsibilities, including reviewing the effectiveness of the system of internal control.

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Property, plant and equipment	2,262.0	2,358.9	96.9	<ul style="list-style-type: none"> <li>• Removal of Millennium Project asset (-£16.2m) [See page 32]</li> <li>• Removal of other assets owned by KGVFT (-£9.7m) [See page 32]</li> <li>• Removal of other duplicated assets (-£2.6m) [See April 2021 report]</li> <li>• Recognise cottages not previously in fixed asset register (+£4.7m)</li> <li>• Correct schools valuations (+£117.9m) [See pages 12-16]</li> <li>• Change basis of valuation for surplus assets (+£12.2m) [See April 2021 report]</li> <li>• Value temporary accommodation purchased in 2018/19 original carried at cost (-£11.1m) [see note 1]</li> <li>• Change in asset lives of infrastructure assets (-£4.5m) [See note 2]</li> <li>• Correct early cut-off error on capital expenditure (+£3.4m)</li> <li>• Recognise parcels of council owned land at voluntary aided school sites not previously recorded (+£3.6m)</li> <li>• Other non significant net adjustments to Property, plant and equipment (-£0.8m)</li> </ul>
Heritage assets	18.8	18.8	-	
Long term investments	67.5	60.5	(7.0)	<ul style="list-style-type: none"> <li>• Reclassify fixed term deposits to Short-term investments (-£7.0m) [See note 3]</li> </ul>
Long term debtors	1.2	1.2	-	
Short term investments	242.6	269.7	27.1	<ul style="list-style-type: none"> <li>• Reclassify fixed term deposits from Long-term investments (+£7.0m) [See note 3]</li> <li>• Reclassify deposits which do not meet the definition of cash equivalent from Cash and cash equivalents (+£20.1m) [See note 4]</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Short term debtors	146.3	150.2	3.9	<ul style="list-style-type: none"> <li>• Correct errors in the recognition of CIL (+£15.2m) [See pages 21-22]</li> <li>• Adjustments involving schools cash balances (-£7.8m) [See page 28]</li> <li>• Correct errors in recognition of leaseholder contributions (+£6.7m) [See pages 21-22]</li> <li>• Adjustments to bad debt provisions (+£6.7m) [See note 5]</li> <li>• Correct error in accounting for Council Tax collection costs (+£3.1m) [See note 6]</li> <li>• Write-off errors on control accounts (-£1.1m) [See note 7]</li> <li>• Set off provision relating to transaction with local health body against receivable (-£3.0m) [see page 18]</li> <li>• Correct errors in the mapping of the trial balance to the accounts (-£17.1m) [see note 10]</li> <li>• Release balances on grant control accounts which do not represent valid debtors (-£5.9m) [see note 11]</li> <li>• Recognise receivable from the London business rates pool (+£6.5m) [see note 12]</li> <li>• Reclassify balances on individual customer accounts which are in credit to short term creditors (+£5.9m) [see note 10]</li> <li>• Debit and credit amounts with individual business rate payers inappropriately presented gross in short term debtors and short term creditors (-£5.0m) [see note 10]</li> <li>• Other non significant net adjustments to Short-term debtors (-£0.3m)</li> </ul>
Cash and cash equivalents	103.2	143.2	40.0	<ul style="list-style-type: none"> <li>• Reclassify deposits which do not meet the definition of cash equivalent to Short term debtors (-£20.0m) [See note 4]</li> <li>• Reclassify bank overdrafts to current liabilities (+£58.8m) [See note 8]</li> <li>• Reclassify liability to third parties to short term creditors (+£1.1m)</li> <li>• Other non significant net adjustments to Short-term debtors (+£0.1m)</li> </ul>
Bank overdrafts	-	(58.8)	(58.8)	<ul style="list-style-type: none"> <li>• Reclassify bank overdrafts from current assets (-£58.8m) [See note 8]</li> </ul>
Short term borrowings	(4.2)	(2.4)	2.8	<ul style="list-style-type: none"> <li>• Reclassification of PFI/finance lease to short term creditors (+£2.8m) [See note 9]</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Short term creditors	(179.3)	(166.8)	12.5	<ul style="list-style-type: none"> <li>• Reclassification of PFI/finance lease from borrowings (-£2.8m) [See note 9]</li> <li>• Correct early cut-off error on capital expenditure (-£3.4m)</li> <li>• Correct other errors in the mapping of the trial balance to the accounts (+£17.1m) [see note 10]</li> <li>• Debit and credit amounts with individual business rate payers inappropriately presented gross in short term debtors and short term creditors (+£5.0m) [see note 10]</li> <li>• Reclassify balances on individual customer accounts which are in credit from short term debtors (-£5.9m) [see note 10]</li> <li>• Recognise grants which had been incorrectly deferred (+£8.6m) [see Note 14]</li> <li>• Account for other preceptor share of £20m creditor released (-£7.2m) [see pages 30-31]</li> <li>• Correct errors in the recognition of CIL (+£4.6m) [see pages 21-22]</li> <li>• Adjustments to accruals (-£5.3m) [see note 14]</li> <li>• Write-out interest incorrectly accrued on developers contributions (+£1.5m) [see note 15]</li> <li>• Reclassify liability to third parties from cash and cash equivalents (-£1.1m)</li> <li>• Other non significant net adjustments to short-term creditors (+£1.4m)</li> </ul>
Provisions (current and non current)	(13.4)	(30.1)	(16.7)	<ul style="list-style-type: none"> <li>• Set off provision relating to transaction with local health body against receivable (+£3.0m) [see page 18]</li> <li>• Release other provisions where no liability (+£2.9m) [see note 16]</li> <li>• Increase in NNDR appeals provision (-£12.6m) [see pages 33-34]</li> <li>• Recognise other additional provisions (-£10.0m) [see note 16]</li> </ul>
Long term borrowing	(72.3)	(72.3)	-	
Pension liabilities	(661.6)	(690.9)	(29.3)	<ul style="list-style-type: none"> <li>• Recognise liability for past discretionary award of enhanced benefits for teachers (-£9.4m) [See April 2021 report]</li> <li>• Adjust for effect of variation between estimated and actual investment returns (-£16.4m) [See pages 35-36]</li> <li>• Adjustment for cash ceiling on LPFA scheme pension liability (-£3.5m)</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Capital grants receipts in advance	(128.0)	(89.4)	38.6	<ul style="list-style-type: none"> <li>Correct errors in recognition of leaseholder contributions (+£22.7m) [See pages 21-22]</li> <li>Correct errors in recognition of developers contributions (+£13.3m) [See note 17]</li> <li>Correct errors in recognition of capital grants (+£2.6m) [See note 17]</li> </ul>
Deferred liabilities	(58.6)	(58.6)	-	
Deferred income – receipts in advance	(0.5)	(0.5)	-	
General Fund reserve (unallocated)	(26.8)	(17.5)	9.3	<ul style="list-style-type: none"> <li>Restatement of opening balance (+£7.1m) [See pages 24-26]</li> <li>Adjustments to bad debt provisions (-£4.2m) [See note 5]</li> <li>Correct error in accounting for Council Tax collection costs (-£3.1m) [See note 6]</li> <li>Write-off errors on control accounts (+£1.1m) [See note 7]</li> <li>Release balances on grant control accounts which do not represent valid debtors (+£5.9m) [see note 11]</li> <li>Recognise receivable from the London business rates pool (-£6.5m) [see note 12]</li> <li>Adjustments involving schools cash balances (+£2.0m) [See pages 28-29]</li> <li>Recognise grants which had been incorrectly deferred (-£4.1m) [See note 12]</li> <li>Account for release of unsupported creditor in the Collection Fund and not the General Fund (+£20.0m) [see pages 30-31]</li> <li>Adjustments to accruals (+£4.3m) [see note 14]</li> <li>Write-out interest incorrectly accrued on developers contributions (-£1.5m) [see note 13]</li> <li>Release other provisions where no liability (-£2.9m) [see note 14]</li> <li>Recognise other additional provisions (+£1.0m) [see note 16]</li> <li>Council decision to adjust amounts allocated to earmarked reserves (-£9.9m) [see note 18]</li> <li>Other non significant net adjustments to the unallocated general fund reserve (+£0.1m)</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Earmarked reserves	(132.8)	(126.5)	6.3	<ul style="list-style-type: none"> <li>Restatement of opening balance (-£3.6m) [see pages 24-26]</li> <li>Council decision to adjust amounts allocated to earmarked reserves (+£9.9m) [see note 18]</li> </ul>
Housing Revenue Account reserve	(53.7)	(44.6)	9.1	<ul style="list-style-type: none"> <li>Recognise other additional provisions (+£9.0m) [see note 16]</li> <li>Other non significant net adjustments to the Housing Revenue Account reserve (+£0.1m)</li> </ul>
Schools reserves	(23.3)	(25.8)	(2.5)	<ul style="list-style-type: none"> <li>Restatement of opening balance (-£2.3m) [see pages 24-26]</li> <li>Other non significant net adjustments to schools reserves (-£0.2m)</li> </ul>
Capital grants unapplied reserve	(94.1)	(158.5)	(64.4)	<ul style="list-style-type: none"> <li>Restatement of opening balance (-£48.9m) [see pages 24-26]</li> <li>Correct errors in recognition of leaseholder contributions (-£3.1m) [See pages 21-22]</li> <li>Correct errors in recognition of developers contributions (-£4.5m) [See note 17]</li> <li>Correct errors in recognition of capital grants (-£0.7m) [see Note 17]</li> <li>Correct errors in recognition of CIL (-£7.9m) [See pages 21-22]</li> <li>Adjustments to bad debt provisions (-£2.5m) [See note 5]</li> <li>Council decision to adjust amount of capital grants unapplied reserve used to finance capital expenditure to finance additional accrued capital expenditure (+£2.6m)</li> <li>Other non significant net adjustments to the capital grants unapplied reserve (+£0.6m)</li> </ul>
Capital receipts reserve	(190.9)	(190.7)	0.2	<ul style="list-style-type: none"> <li>Other non significant net adjustments to the capital receipts reserve (+£0.2m)</li> </ul>
Capital adjustment account	(1,426.2)	(1,422.0)	4.2	<ul style="list-style-type: none"> <li>Restatement of opening balance (+£14.4m) [see pages 24-26]</li> <li>Council decision to adjust amount of capital grants unapplied reserve used to finance capital expenditure to finance additional accrued capital expenditure (-£2.6m)</li> <li>Revision of useful economic lives of infrastructure assets (+£4.5m) [see note 2]</li> <li>Corrections to valuations (-£12.1m) [see pages 12-16]</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Revaluation reserve	(483.0)	(584.9)	(101.9)	<ul style="list-style-type: none"> <li>Restatement of opening balance (-£282.5m) [see pages 24-26]</li> <li>Recognise parcels of council owned land at voluntary aided school sites not previously recorded (-£3.6m)</li> <li>Corrections to valuations (+£184.2m) [see pages 12-16]</li> </ul>
Collection Fund Adjustment Account	10.9	11.2	0.3	<ul style="list-style-type: none"> <li>Account for release of unsupported creditor in the Collection Fund and not the General Fund (-£12.8m) [see pages 30-31]</li> <li>Increase in NNDR appeals provision (+£12.6m) [see pages 33-34]</li> <li>Other non significant net adjustments to the Collection Fund Adjustment Account (+£0.5m)</li> </ul>
Financial Instrument Adjustment Account	17.4	17.4	-	
Pension reserve	676.0	705.4	29.5	<ul style="list-style-type: none"> <li>Recognise liability for past discretionary award of enhanced benefits for teachers (+£9.4m) [See April 2021 report]</li> <li>Adjust for effect of variation between estimated and actual investment returns (+£16.4m) [See pages 35-36]</li> <li>Adjustment for cash ceiling on LPFA scheme pension liability (+£3.5m)</li> <li>Other non significant net adjustments to the Pension reserve (+£0.2m)</li> </ul>
Accumulated Absences Adjustment Account	3.0	3.0	-	
Pooled Investments Adjustment Account	-	0.6	0.6	<ul style="list-style-type: none"> <li>Correct for incorrect use of statutory override (+£0.6m)</li> </ul>
Financial Instrument Revaluation Reserve	0.6	-	(0.6)	<ul style="list-style-type: none"> <li>Correct for incorrect use of statutory override (-£0.6m)</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Net cost of services	394.5	418.5	24.0	<ul style="list-style-type: none"> <li>• Revision of useful economic lives of infrastructure assets (+£4.5m) [see note 2]</li> <li>• Adjustments to bad debt provisions (-£4.2m) [See note 5]</li> <li>• Correct error in accounting for Council Tax collection costs (-£3.1m) [See note 6]</li> <li>• Write-off errors on control accounts (+£1.1m) [See note 7]</li> <li>• Release balances on grant control accounts which do not represent valid debtors (+£5.9m) [see note 11]</li> <li>• Adjustments involving schools cash balances (+£2.0m) [See pages 28-29]</li> <li>• Recognise grants which had been incorrectly deferred (-£4.1m) [see note 13]</li> <li>• Account for release of unsupported creditor in the Collection Fund and not the General Fund (+£20.0m) [see pages 30-31]</li> <li>• Adjustments to accruals (+£4.3m) [see note 14]</li> <li>• Release other provisions where no liability (-£2.9m) [see note 16]</li> <li>• Recognise other additional provisions (+£10.0m) [see note 16]</li> <li>• Corrections to valuations (-£12.1m) [see pages 12-16]</li> <li>• Correct error in presentation of Tower Hamlets Homes pension liability transactions (+£3.4m)</li> <li>• Various adjustments have been made to correct errors in the presentation of items between financial statement lines within net cost of services, in particular for recharge income and expenditure, resulting in income and expenditure being double-counted [see April 2021 report]</li> </ul>
Other operating income and expenditure	(7.7)	(7.7)	-	
Financing and investment income and expenditure	38.7	(37.2)	(1.5)	<ul style="list-style-type: none"> <li>• Write-out interest incorrectly accrued on developers contributions (-£1.5m) [see note 15]</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

Financial statement line	Original version £m	Current version £m	Change £m	Principal recorded adjustments and reference to further information
Taxation and capital and non specific government grants	(327.7)	(352.6)	(24.9)	<ul style="list-style-type: none"> <li>• Recognise receivable from the London business rates pool (-£6.5m) [see note 12]</li> <li>• Increase in NNDR appeals provision (-£12.6m) [see pages 33-34]</li> <li>• Account for release of unsupported creditor in the Collection Fund and not the General Fund (+£12.8m) [see pages 30-31]</li> <li>• Correct errors in the recognition of CIL (-£7.9m) [See pages 21-22]</li> <li>• Correct errors in recognition of leaseholder contributions (-£3.1m) [See pages 21-22]</li> <li>• Adjustments to bad debt provisions (-£2.5m) [See note 5]</li> <li>• Correct errors in recognition of developers contributions and capital grants (-£5.2m) [See note 17]</li> <li>• Other non significant net adjustments to Taxation and capital and non specific government grants (-£0.5m)</li> </ul>
Other comprehensive income and expenditure – gains/losses on valuation of PPE	321.3	136.5	(184.8)	<ul style="list-style-type: none"> <li>• Corrections to valuations (-£184.8m) [see pages 12-16]</li> </ul>
Other comprehensive income and expenditure – remeasurement of pension liabilities	57.4	75.5	18.1	<ul style="list-style-type: none"> <li>• Recognise liability for past discretionary award of enhanced benefits for teachers (+£9.4m) [See April 2021 report]</li> <li>• Adjust for effect of variation between estimated and actual investment returns (+£16.4m) [See pages 35-36]</li> <li>• Correct error in presentation of Tower Hamlets Homes pension liability transactions (-£3.4m)</li> <li>• Other non significant net adjustments remeasurement of pension liabilities (-£1.6m)</li> </ul>



# Appendix A: Audit adjustments

## Corrected misstatements (continued)

Note	Principal recorded adjustments
Officers' remuneration – other employees	<ul style="list-style-type: none"> <li>The original disclosure omitted 612 staff who are paid by schools which do not participate in the corporate payroll arrangement</li> <li>The comparatives were prepared on a similar basis and have now been restated</li> </ul>
Disclosures on liquidity risk	<ul style="list-style-type: none"> <li>The disclosure should provide information on the timing of cash flows for all contractual commitments in respect of financial liabilities. The original disclosure omitted fixed interest payments, understating future cash flows by £197.5m</li> <li>The comparatives were prepared on a similar basis and have now been restated</li> </ul>
Movements on Property, Plant and Equipment	<ul style="list-style-type: none"> <li>Properties acquired in the year for the provision of temporary accommodation were included in additions to other land and buildings. Where properties were not ready to bring into use, these were reclassified to assets under construction, shown on a separate reclassification line. The value of properties which were not ready for use (£40m) has been corrected to include additions to assets under construction and not other land and buildings, with transfers from assets under construction to other land and buildings recorded once the properties are ready for use.</li> </ul>
Cash flow statement	<ul style="list-style-type: none"> <li>In the originally published 2017/18 accounts, the purchase and proceeds of investments were presented net within the note on cash flows from investing activities. These cash flows do not meet the limited conditions in which cash flows can be reported on a net basis. An adjustment has been made to present the purchase of short term and long term investments of £292m on a separate line within the note on cash flows from investing activities. The comparatives were prepared on a similar basis and have now been restated.</li> <li>Cash flows from operating activities incorrectly included net proceeds from the sale of short term and long term investments (£49m) which should have been classified within cash flows from investing activities</li> <li>Cash flows with other preceptors relating to the council's billing functions were incorrectly classified in cash flows from operating activities and not cash flows from financing activities</li> </ul>

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

[1] The Council purchased residential accommodation during 2018/19 for provision as temporary housing. The properties are required to be carried at current value after initial recognition but were not included in the list of properties given to the valuer for valuation. Some of the properties were not in a condition where they could be used without works to the properties which were ongoing at the reporting date. These properties have been reclassified from other land and buildings to assets under construction and did not require valuation under the accounting rules for that class.

[2] As explained in the April 2021 report, we challenged the council on the useful economic lives (UEs) selected for infrastructure assets during our 2018/19 audit. Following consultation with the relevant service department, the UEs have been revised. The new lives have been applied prospectively from 1 April 2018.

[3] A fixed term deposit with maturity dates falling after 12 months of the relevant reporting date had been classified within long term (i.e. non-current) investments. Given its remaining period to maturity, it was expected to be realised within twelve months of the reporting date and therefore should have been classified within long term (i.e. current) investments.

[4] Instruments should only be classified as cash equivalents where there is no more than an insignificant risk of a change in value. This was not the case for certain instruments which have now been reclassified to short term investments.

[5] Following our challenge, officers have re looked at: (a) the provision against amounts outstanding from leaseholders in respect of major works. The original provision was calculated by applying percentages to categories based on age. Officers have concluded that this is not consistent with the approach taken in practice to collection including agreement of payment plans. Officers also concluded that it was not consistent with the leverage which the council has by virtue of its ability to decline to approve the transfer of the leasehold while there are amounts outstanding on the leaseholder's account with the council. As a result the bad debt provision has been reduced and capital grants unapplied account increased by £2.5m; (b) the provision for housing benefit overpayments repayable to the council. Based on a calculation using historical collection experience, the provision and net expenditure of services has been reduced and General Fund balance increased by £4.2m.

[6] Council Tax collection costs receivable were not recognised on the balance sheet due to an oversight, but were included in the calculation of a bad debt provision against both Council Tax arrears and debtors relating to the recovery of collection costs from taxpayers.

[7] The Council maintains control accounts for utility bills which require allocation to relevant cost centres (and in a small number of cases, other entities which occupying Council premises). The control accounts had not been correctly maintained and as a result costs had not been expensed or had not been billed to third parties and had become irrecoverable.

[8] In the original version of the accounts, bank overdrafts were set-off against deposit amounts. This was incorrect as the conditions for set off had not been met (the council did not have a legally enforceable right of set-off and/or the council did not intend to settle net). The adjustment transfers bank overdrafts to current liabilities.

[9] This is an adjustment officers chose to make to reclassify the current portion of PFI and finance lease obligations from short term borrowings to short term creditors.

[10] These adjustments summarise the correction of various errors in the mapping of debtor and creditor control accounts between short term debtors and short term creditors in the financial statements, including errors involving the grouping of amounts due to/from other preceptors and taxpayers in relation to the collection of local taxes, the incorrect allocation of a bad debt provision to short term creditors and the incorrect allocation of internal debtors to short term debtors, rather than to short term creditors to eliminate against the corresponding internal creditor balance. Adjustments also reclassify credit balances on individual customer accounts from short term debtors to short term creditors. In addition, various reclassification adjustments were needed at a note line level, within short term debtors and short term creditors.

[11] Spending in excess of the related dedicated schools grant of £4.5m was incorrectly carried forward in short term debtors and has now been expensed. The council has chosen to include in the updated financial statements as a negative earmarked reserve (see note 18). A further amount of £1.3m was carried forward on the PFI grant control account as a result of errors in postings to this account and has also now been expensed.

# Appendix A: Audit adjustments

## Corrected misstatements (continued)

[12] The council participated in the London business rates pool for the first time in 2018/19 which is hosted by the GLA and administered by the City of London Corporation. The council did not account for its share of the pool in the original version of the accounts and the amount receivable has now been accrued. Contributions to and distributions from the pool are not governed by statutory provisions and are therefore charged to or credited to the General Fund immediately.

[13] Grants were deferred although there were no conditions preventing their recognition, in particular an amount of £5.1m deferred in respect of Flexible Homelessness Grant. respectively. The adjustment includes amounts where the officers have been unable to locate information relating to the original grant and in the absence of information or record of subsequent contact from the grant funder have formed the view that there are no remaining conditions. The approach is not unreasonable, but as we advised in our report in April 2021, there is a residual risk that there are remaining conditions to be fulfilled and/or amounts are not be applied in accordance with the wishes of the grant funder. The adjustment involved the restatement of opening balances by £4.6m and adjustment to current year grant income of £4.1m.

[14] Various errors were identified in our original accruals sample. Officers carried out an exercise to review and adjust accruals and we performed procedures on amended accruals breakdowns. In addition to the adjustment made, we have projected a further possible error in relation to accruals items not sampled (see page 63).

[15] This removes interest which had been accrued on outstanding balances as the agreements did not contain an obligation on the council to maintain the value of the contribution in real terms.

[16] The original version of the accounts included a disclosure of a contingent liability relating to possible claims for re-imbursement of water charges. We challenged the Council on whether settlement was now probable following the outcome of a test case. Officers concluded that settlement was now probable and have recognised a provision (£9.0m) and charge to the Housing Revenue Account. In addition,

further provisions for other legal cases was made (£1.0m) following circularisation of the in house legal team. Conversely, we also identified provisions of £2.9m where no obligation to transfer economic benefits to a third party existed at the reporting date.

[17] Our sample testing identified developer contributions which had been deferred but where the agreement did not contain conditions preventing recognition. Officers performed a review and identified similar amounts which had been deferred at both 31 March 2019 and earlier reporting dates and have adjusted all periods presented for this misstatement. A similar error was identified in relation to a capital grant (disabled facilities grant) and again all periods presented have been corrected for this error.

[18] The council has chosen to make changes to the amounts set aside in earmarked reserves, in particular: (a) a reduction in the amount set aside in the business rates income equalisation reserve in order to mitigate the impact on the General Fund of changes required to the accounts in relation to a release of a creditor of £20.0m (see pages 30-31); (b) increases in the amounts set aside in the grants earmarked reserve as the council still intends that certain of the grant monies previously deferred and now released should remain available to the relevant services. To the extent that opening deferred grant income balances have been restated, opening earmarked reserve balances have also been restated; (c) transfer of the accumulated overspend on dedicated schools grant of £4.5m to earmarked reserves. The inclusion of a "negative" earmarked reserve within the overall credit balance within earmarked reserves is misleading, because, as a consequence of recording this amount in earmarked reserves, the amount available for other earmarked reserves is in effect reduced. However, the amount is immaterial and following a change in legislation, from 1 April 2020, such overspends are no longer fall on the General Fund.

# Appendix A: Audit adjustments

## Disclosures

### Disclosure misstatements

The following uncorrected disclosure misstatements have been identified up to the date of this report which we request that you ask management to correct as required by ISAs (UK).

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### Disclosure

#### Dedicated schools grant comparatives

The comparative information in the dedicated schools grant disclosure has apparent errors as it shows grant of £1.7m and no expenditure allocated to central expenditure but incorrectly shows an amount of £18.8m in the central expenditure column as deployed to schools. The amount of grant for 2018/19 which has been allocated to central expenditure is £84.4m.

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#### Conclusion on Annual Governance Statement

Whilst the governance statement relates to the governance system as it applied during the financial year, it should be updated for significant events or developments relating to the governance system that occur before the reporting date and the date on which the Statement of Accounts is signed by the responsible financial officer. The statement, prepared at an earlier date, has not been updated for example for milestones in action plans which are now past.

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#### Inconsistencies and other errors relating to Note 42, Income and Expenditure analysed by nature

There are differences between income and expenditure on services per CIES and the amounts shown in Note 42, Income and Expenditure analysed by Nature. Gross income from services and gross expenditure on services using information extracted from the Note 42 is £2.0m lower than the amount shown in the CIES. Similarly, in respect of the restated comparative information, gross income from services and gross expenditure on services using information extracted from the Note 42 is £2.0m lower than the amount shown in the CIES.

We are not able to determine whether the CIES or Note 42 requires correction.

From our review of the other service expenses ledger, we identified that the precepts and levies expense of £1,859k had incorrectly been double counted in both other service expenses and the precepts and levies note line within Note 41. Due to the deficiencies identified in the initial version of the accounts and lack of information available, officers were unable to whether there is an equal and opposite credit within other service expenses to offset this amount or if a true double count, where the other side of the entry would be.

In addition, whilst an adjustment has been made to correct for an error in the Comprehensive Income and Expenditure Statement involving the incorrect classification of an item of service cost within other comprehensive income, Note 42 has not been similarly adjusted. As a result employee benefit expenses are understated in Note 41 by £2205k.

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# Appendix A: Audit adjustments

## Disclosures

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### Disclosure

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#### **Revaluation reserve**

The unusable reserves note disclosure contains a reconciliation of the opening and closing revaluation reserve:

- 'Upward revaluation of assets' note line is overstated by £5,166k
  - 'Downward revaluation of assets' note line is understated by £4,123k.
- 

#### **Credit risk - quantitative disclosure**

Gross leaseholder debtors is understated and other debtors overstated by £1782k (at 31 March 2018 by £1565k).

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#### **Revenue from contracts with service recipients**

Revenue recognised from contracts with service recipients has not been disclosed separately from its other sources of revenue [Code: 2.7.4.5] and the amount has not been disaggregated into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors [Code 2.7.4.6].

Impairment losses recognised on receivables arising from contracts with service recipients have similarly not been disclosed separately from impairment losses from other contracts [Code: 2.7.4.5]

The opening and closing balances on receivables, contract assets and contract liabilities from contracts with service recipients has not been separately disclosed, together with disclosures related to these account balances [Code: 2.7.4.8].

The Council has not made any disclosures about the transition to IFRS 15 Revenue from Contracts with Customers [Code: 2.7.4.20].

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#### **Pooled budgets**

The Pooled Budgets note discloses expenditure equal to income from the Better Care Fund of £23,165k. The council has not separately monitored expenditure which, based on a high level review of account codes, may be £1.3m higher than the amount assumed and disclosed.

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# Appendix A: Audit adjustments

## Disclosures

### Other disclosure recommendations

Although the omission of the following disclosures does not materially impact the financial statements, we are drawing the omitted disclosures to your attention because we believe it would improve the financial statements to include them or because you could be subject to challenge from regulators or other stakeholders as to why they were not included.

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### Disclosure

#### Movements on provisions

The analysis of movements on provisions should distinguish between amounts used and unused amounts reversed in the year. The disclosure does not distinguish between these amounts and discloses instead the aggregate of these two amounts [Code: 8.2.4.2].

This is because the council has not been able to analyse movements on the provision for appeals against business rates, in turn because the council has not been able to distinguish between adjustments to business rates income as a consequence of a successful appeals and other adjustments to business rates income.

Adjustments to business rates income as a consequence of a successful appeals and other adjustments to business rates income are presented on separate lines within the supplementary collection fund statement (being "Impairment of debts/appeals for non-domestic rates" and "Income from non-domestic rates", respectively).

As the council has not been able to extract information to determine the correct allocation of adjustments between these lines, it has done so on the basis of estimates.

Based on information provided to us, we estimate that income from non-domestic rates and the charge for appeals for non-domestic rates in the collection fund supplementary statement may have been understated by £6.9m.

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#### Disclosures relating to the transition to IFRS 9

The Council has disclosed for each class of financial assets and financial liabilities the original measurement category and carrying amount determined in accordance with the Code's adoption of IAS 39 as at 1 April 2018, but has not disclosed the new measurement category and carrying amount determined in accordance with the Code's adoption of IFRS 9 [Code: 7.4.3.16].

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# Appendix B: Independence and fees

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the council and our objectivity is not compromised.
Fees	<p>Details of proposed fees for audit and non-audit services performed for the period have been presented separately in this appendix.</p> <p>The fees for the audit set out on the next page relate to the scale fee and variations to the original scale fee which have so far been agreed with the council and with Public Sector Audit Appointments Limited. Billing to date takes account of time spent in the period to 31 January 2021. Since then, a substantial amount of time has been incurred to bring the 2018/19 audit, as well as the 2019/20 audits, to its current state and we will be seeking to agree a further fee variation in relation to this.</p>
Non-audit services	<p>We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.</p> <p>We have carried out assurance work on two grants/returns made by the council in respect of 2018/19. We regard the threats to independence presented by these services to be insignificant and not to require safeguards.</p> <p>During 2018/19 we also provided property related advice which commenced prior to our appointment. Details of the fees earned during 2018/19 are given on the next page. Fees earned from the start of our appointment to completion of the contract were £23k. The service relates to a transaction involving compensation for the transfer of part of a park which is owned by Council. The compensation was expected to be less than £0.5m. The engagement was ongoing at the time of our appointment and involved advising on the amount of the compensation. This involves both valuation services and negotiation with the government agency who will pay the compensation. The service did not involve taking a management role and the outcome of that service has not been used in the preparation of the financial statements. The work has been carried out by partners and staff from a different office and service line to the audit engagement partner.</p>
Relationships	We are not aware of any relationships (other than the provision of non-audit services which are covered above) we have with the council, its members and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence.

# Appendix B: Independence and fees

The professional fees charged by Deloitte for the period from 1 April 2018 to 31 March 2019 are as follows:

	Current year £'000
Audit of the council	252
<b>Total audit</b>	252
Certification of grants and returns (Housing benefit subsidy and teacher pension return)	29
<b>Total assurance services</b>	29
Other non-audit services not covered above (Property related service – see previous page)	8
<b>Total other non-audit services</b>	8
<b>Total non-audit services</b>	37
<b>Total fees</b>	289
London Borough of Tower Hamlets pension scheme audit	17

As set out on the previous page, the fees for the audit set out on the next page relate to the scale fee and variations to the original scale fee which have so far been agreed with the council and with Public Sector Audit Appointments Limited. This takes account of time spent in the period to 31 January 2021. Since then, a substantial amount of time has been incurred to bring the 2018/19 audit, as well as the 2019/20 audits, to its current state. Additional costs in the period from 1 February 2021 to 31 December 2022 across both 2018/19 and 2019/20 council audits have been £312k. We will be seeking to agree a further fee variation in relation to this, as well as the further costs of finalising these audits incurred in 2023.



# Appendix C: Our other responsibilities explained

## Fraud responsibilities and representations

### Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.

### Required representations:

We have asked the Board to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the financial statements may be materially misstated as a result of fraud and that you have disclosed to us all information in relation to fraud or suspected fraud that you are aware of and that affects the entity.

We have also asked the Council to confirm in writing their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

### Audit work performed:

In our planning we identified the risk that operating expenses had been inappropriately capitalised and management override of controls as key audit risks.

During course of our audit, we have made enquiries of management and those charged with governance.

In addition, we have reviewed management's own documented procedures regarding fraud and error in the financial statements

We have reviewed the paper prepared by management for the audit committee on the process for identifying, evaluating and managing the system of internal financial control.

We will explain in our audit report (for all entities subject to audit) how we considered the audit capable of detecting irregularities, including fraud. In doing so, we will describe the procedures we performed in understanding the legal and regulatory framework and assessing compliance with relevant laws and regulations.

### Concerns:

We have brought to the attention of audit committee members on pages 17-18 a transaction which did not appear to have any economic substance.

# Appendix D: Summary of the more significant updates since the issue of the January 2022 version of this report

Item	Update
Our predecessor had not yet certified the closure of their audits for years ended 31 March 2018 and 31 March 2017. As the remaining matters were relevant and material to the statement of accounts for the year ended 31 March 2019, we advised that we did not propose to issue our opinion until these earlier audit certificates had been issued.	We understand that a draft of the audit certificates will be provided to the same meeting as this report and that these are expected to be signed shortly before issue of our opinion.
In our January 2022 report, we gave a provisional view on the accounting for an indemnity given by the council to THHL in respect of pension contributions for current and former staff of THHL and reported that this was a potential qualification matter. We also highlighted in our oral presentation that we were considering this matter further.	We have concluded that the existing approach is appropriate and explain the basis of this on page 27.
Since the issue of our report in January 2022, there has been a debate at a national level over the accounting for infrastructure assets and in particular over the possibility that infrastructure asset balances may include parts of the infrastructure which have been replaced and are no longer in operational existence.	The council is impacted by this issue as it does not have a process to identify and derecognise parts of its infrastructure which have been replaced. As a result, infrastructure assets which may contain parts which have been replaced, but we are not able to quantify the adjustment required. Further explanation is given on page 38.
<p>We explained in previous reports:</p> <ul style="list-style-type: none"> <li>• How the accounting for a lump sum contribution to the London Borough of Tower Hamlets Pension Scheme in 2017/18 of £43.4m was dependent on the resolution of a question of its lawfulness which had been raised by legal advice received by the council.</li> <li>• The council had received a second piece of legal advice which contradicted the initial advice and concluded that the wording in the rates and adjustment certificate provided the council with the necessary flexibility to make the lump sum payment.</li> <li>• The accounting adopted in the version of the accounts presented to the January 2022 committee for approval was consistent with the second piece of legal advice.</li> </ul>	<p>We have discussed the issue within the sector and consulted internally.</p> <p>We concluded that the approach taken by the council was reasonable and consistent with other local authorities.</p>

# Appendix D: Summary of the more significant updates since the issue of the January 2022 version of this report

Item	Update
<p>Our January 2022 report explained that:</p> <ul style="list-style-type: none"> <li>As part of the 2018/19 accounts process, a valuation of council dwellings was carried out at an effective date of 1 April 2018. This resulted in a valuation which was £113m (10%) lower than the carrying amount at 31 March 2018.</li> <li>This raised a question as to whether the change arises from a change in accounting estimate, for example due to further information becoming available after the date of approval of the 2018/19 accounts, or whether it relates to an error in the carrying amount at 31 March 2018.</li> <li>The valuation at 31 March 2018 was based on an earlier valuation at 1 April 2017 which had been updated by indexation. The council had sourced the index from the valuer. Land Register information now available is not consistent with the advice given by the valuer at the time.</li> <li>Land Registry information is updated continuously and retrospectively. The valuer did not retain a copy of the data on which his advice was based and it is not possible to determine retrospectively the information available at the time of approval of the 2017/18.</li> <li>We noted that that the council was discussing this with the predecessor auditor and we would conclude once we knew the outcome of this.</li> </ul>	<p>Whilst we cannot determine what information was shown in the Land Registry record at the time the valuer prepared his market change report in April 2018, the valuation should reflect information available at the time of approval of the accounts (in July 2018). Given the four month interval, we consider it unlikely that a valuation performed at this point would have resulted in a valuation which was significantly different to the valuation which was subsequently performed at 1 April 2018, we cannot rule this out. The predecessor auditor did not identify any issues based on the information considered by them at that time. In view of the absence of clear evidence that this results from a failure to consider information available at the time of approval of the 2017/18 financial statements, we have not proposed a restatement.</p>
<p>The narrative report had not been updated for significant events subsequent to the year end and, in particular, made no reference to the pandemic or to changes made to the council's medium term financial strategy in its latest iteration. We recommend officers update for these matters</p>	<p>The narrative report has been updated to address these and other issues reported.</p>
<p>Our January 2022 set out in an appendix a schedule of uncorrected misstatements and disclosure recommendations identified up to the date of that report.</p> <p>We presented these items into two tables, showing separately (A) those which officers did not propose to correct in the final version and (B) those misstatements which officers agreed would be corrected in the final version of the statement of accounts.</p>	<p>Officers have substantially updated the statement of accounts to correct the misstatements which they had undertaken to correct.</p> <p>We have included residual matters in a single schedule of uncorrected misstatements in Appendix A.</p>

# Appendix D: Summary of the more significant updates since the issue of the January 2022 version of this report

Item	Update
<p>In our January 2022 report we reported that:</p> <ul style="list-style-type: none"> <li>• Our sample testing had identified expenditure relating to refurbishments which included expenditure on fixtures, fittings and equipment, but which had been classified in its entirety within other land and buildings.</li> <li>• Our inspection of assets included within fixtures, fittings and equipment, which is substantially limited to previous purchases of refuse collection vehicles, suggests that this practice is common and has operated for a number of years.</li> <li>• In addition to the impact on disclosure information, the practical consequence of coding expenditure on fixtures, fittings and equipment in this way is that the expenditure will be written out of the Property, Plant and Equipment balance when next subject to valuation where the type of expenditure falls outside the scope of what is considered by the valuer in their valuation.</li> <li>• The council performed an exercise to estimate the effect of this and concluded that this was not a material matter. The exercise involved interrogating the breakdown of capital expenditure in 2018/19 and 2019/20 for the words "fixtures", "fittings" and "equipment". We do not expect that this technique is likely to identify the full extent of any issue.</li> </ul>	<p>The council has performed a further exercise which looked at expenditure on office accommodation and schools over a four year period. Officers concluded from their analysis that no significant spend on Fixtures, Fittings and Equipment had been capitalised in relation to office accommodation in this period but approximately £0.8m (representing c 2% of spend) had been capitalised within other land and buildings in relation to schools.</p> <p>Officers' exercise looked only at spend over the last four years and considers only certain categories of building and not all categories which may be impacted by this issue.</p> <p>Nonetheless we concluded that it provided better insight into the possible quantum of the issue and based on further analysis concluded that the extent of the issue was not likely to exceed £1-2m and concluded on this basis that this is not a material issue.</p>
<p>We had not received information for some of our sample items which we had requested to enable us to verify building area information provided to the valuer.</p>	<p>Outstanding information has been received and did impact on our previously reported conclusions.</p>
<p>Further investigation was needed to quantify adjustments, if any, needed to the recognition of "business rate related grant".</p>	<p>This was satisfactorily resolved in relation to the 2018/19 accounts.</p>

# Appendix E: Proposed wording of the modifications to our audit report

Item and page reference to explanation of circumstances that led to the expected modification	Proposed wording of modification
Failure to prepare group accounts (see page 33)	<p>The group has not prepared group accounts. Under the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19, the Authority should prepare group accounts as its interests are material in aggregate. Had group accounts been prepared, many elements in the accompanying consolidated financial statements would have been materially affected. The effects on the consolidated financial statements of the failure to consolidate have not been determined. Our opinion on the Authority's financial statements is also qualified for this matter as the failure to consolidate all subsidiaries is a departure from the requirements of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19. In addition, the strategic report and directors' report do not consider the effects of the failure to prepare group accounts.</p>
Measurement of pension obligations (see pages 36-37)	<p>Note 40 Pension Scheme discloses the plan assets and defined benefit obligations held by the Authority.</p> <p>The Authority's estimate of the defined benefit obligations of the Authority and the Authority's share of pension assets did not take into account information collected and analysed for the purpose of the triennial funding valuation of the London Borough Tower Hamlets Pension Scheme published on 31 March 2020 including: differences between past actuarial assumptions and actual experience or updates to membership information in the three year period to 31 March 2019; past errors in membership data; or the effect of assuming that all increases on Guaranteed Minimum Pensions for members reaching State Pension Age after 6 April 2016 will be paid for by LGPS employers; and the allocation of pension assets between participating employers.</p> <p>In our opinion, under International Accounting Standard 10 Events after the Reporting Period, the Authority should adjust its financial statements for the year ended 31 March 2019 for the effect of information which is now available from the triennial valuation exercise at 31 March 2019. It is not possible to determine with reasonable certainty the exact value of the adjustments which would be required as the Authority has not performed a calculation of the pension liability at 31 March 2019 using this information. In these circumstances, we are unable to quantify the effect of the departure from the accounting standard. The effect of this is also not disclosed in the narrative report.</p>

# Appendix E: Proposed wording of the modifications to our audit report

Item and page reference to explanation of circumstances that led to the expected modification	Proposed wording of modification
Related party disclosures (see page 39)	<p>Note 37 discloses information about related party relationships and transactions and outstanding balances with related parties. We were unable to obtain sufficient appropriate audit evidence concerning whether information for the year ended 31 March 2019 in respect of all relevant relationships had been reported as returns used to collect information on the interests of elected members and members of their close family were not obtained or could not be located. Consequently, we were unable to determine whether any adjustments the information disclosed were necessary.</p>
Officers remuneration (see page 40)	<p>Note 31 Officers Remunerations discloses the number of employees receiving remuneration of more than £50,000 in bands of £5,000. We were unable to obtain sufficient appropriate audit evidence regarding the headcount figures for the year ended 31 March 2019 and restated headcount figures for the year ended 31 March 2018 because information returned by certain schools was not in the same bands as the note and we were unable to obtain information to verify estimates used by the Authority to allow for the differences in format. In addition, we were unable to determine the effect of differences between the Authority's main accounting system and detailed payroll records provided to us on the headcount figures disclosed. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.</p> <p>Note 31 Officers Remuneration also discloses the remuneration of individual senior officers. As a result of the differences between the Authority's main accounting system and detailed payroll records, we were also unable to determine whether there were staff paid over £150,000 in the year ended 31 March 2019 who had not been disclosed in the note.</p> <p>Note 31 Officers Remuneration also discloses information about the number, type and value of exit packages. The Authority did not receive returns from 33 schools for the year ended 31 March 2018 on exit payments to staff at these schools. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.</p>

These modifications have the following implications for other sections of the audit report:

- Non preparation of group accounts - We have concluded that other information in the narrative report is materially misstated for the same reason with respect to the amounts or other items in the annual report affected by the failure to consolidate the Authority's subsidiaries.
- Measurement of pension assets and liabilities - We have concluded that where the other information refers to these, it may be materially misstated for the same reason.

# Appendix E: Proposed wording of the modifications to our audit report

Item and page reference to explanation of circumstances that led to the expected modification	Proposed wording of modification
<p>Value for money – financial reporting (see pages 44-45)</p>	<p>The finalisation and publication of the council’s statement of accounts for the year ended 31 March 2019 has been significantly delayed from the original target date of 31 July 2019. This is due to the time needed to investigate issues identified during the audit process and to prepare accounts. The Council’s investigation of these matters resulted in a period of prolonged uncertainty over the amount and timing of recognition of usable reserves available to meet future spending requirements and the council’s strategic objectives and a significant volume of corrections to the originally published draft statement of accounts. The corrections had the effect of increasing usable reserves at 31 March 2019 by £42m, unusable reserves by £68m, assets by £102m and liabilities by £8m.</p> <p>These conditions provide evidence that the Council did not have proper arrangements in place for reliable and timely financial reporting that supports the delivery of strategic priorities to support informed decision making.</p>
<p>Value for money - risk management and internal control (see page 46)</p>	<p>In the Annual Governance Statement, the Council has reported on significant governance issues identified from its annual review of effectiveness. The Annual Governance Statement reports that internal audit are under resourced and the Head of Internal Audit has reported there that he has limited the scope of his annual opinion on the system of internal control as he has not been able to consider IT risks. The Head of Internal Audit was not able to report on the Council’s system of risk management in 2018/19 pending the establishment of independent review arrangements for this and in 2019/20 has reported he can provide only limited assurance on its operating effectiveness. The Head of Internal Audit was able to provide only limited assurance in relation to 37% of the areas included in the 2018/19 internal audit programme. In three cases these related to follow-up reports where recommendations from the original report had not been satisfactorily actioned.</p> <p>These conditions provide evidence that the Council did not have proper arrangements in place to manage risks effectively and maintain a sound system of internal control.</p>

# Appendix E: Proposed wording of the modifications to our audit report

Item and page reference to explanation of circumstances that led to the expected modification	Proposed wording of modification
Value for money – childrens' services (see page 43)	<p>An Ofsted inspection of the Council's services for children in need of help and protection, children looked after and care leavers undertaken in January and February 2017, which reported in April 2017, rated children's services, overall, as inadequate. The inspection also reviewed the effectiveness of the Local Safeguarding Children Board ("LCSB") and rated this as inadequate. The Ofsted report raised concerns in relation to poor frontline practice and non-compliance with basic standards (including legal requirements) which in some cases left children at risk of harm. The report also highlighted that there was insufficient scrutiny by senior leaders and non-compliance was not sufficiently challenged. In addition, performance management and quality assurance systems were not underpinned by reliable management information due to social workers and managers not updating records on the electronic recording system. The LCSB in Tower Hamlets was judged to be inadequate, as it was not discharging all of its statutory functions. The report concluded that there was insufficient monitoring of the quality of frontline practice which meant that the board was not aware of the failings to protect children reported on in the review. The Annual Governance Statement describes improvements which the Council has made in response to these findings. These improvements were not in place over the full year.</p> <p>These conditions provide evidence that the Council did not have proper arrangements in place throughout the full year to understand and use appropriate and reliable performance information to support informed decision making and performance management; manage risks effectively and maintain a sound system of internal control; and work with third parties effectively to deliver strategic priorities.</p>



# Appendix F: Draft management representation letter

We set out below the draft representations requested from management for your information. We have highlighted in red those representation which in particular the council may consider need tailoring in the light of expected audit qualifications.

This representation letter is provided in connection with your audit of the financial statements of the London Borough of Tower Hamlets (the council) for the year ended 31 March 2019 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view of the financial position of the London Borough of Tower Hamlets as of 31 March 2019 and of the results of its operations, other recognised gains and losses and its cash flows for the year then ended in accordance with the CIPFA/LASAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 ("the Code").

We confirm, to the best of our knowledge and belief, the following representations.

## *Financial statements*

1. We understand and have fulfilled our responsibilities for the preparation of the financial statements in accordance with the Accounts and Audit Regulations 2015 and CIPFA/LASAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 ("the Code").
2. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.
3. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of IAS24 "Related party disclosures."
4. All events subsequent to the date of the financial statements and for which the applicable financial reporting framework requires adjustment of or disclosure have been adjusted or disclosed.
5. The effects of uncorrected misstatements and disclosure deficiencies

are immaterial, both individually and in aggregate, to the financial statements as a whole. A list of the uncorrected misstatements and disclosure deficiencies is detailed in the appendix to this letter *[Note: the final version of the schedules of uncorrected misstatements and disclosure deficiencies shown in Appendix A, Audit Adjustments in this report will be added to the final version of the management representation letter as the appendix referenced here]*.

6. We confirm that the financial statements have been prepared on the going concern basis and disclose in accordance with IAS 1 all matters of which we are aware that are relevant to the council's ability to continue as a going concern, including principal conditions or events and our plans. In making our going concern assessment we have adopted the 'continuing provision of service' approach and accordingly we are not aware of any material uncertainties related to events or conditions that may cast significant doubt upon the council's ability to continue as a going concern. There are no circumstances that we are aware of that would affect the appropriateness of the 'continuing provision of service' approach. We confirm the completeness of the information provided regarding events and conditions relating to going concern at the date of approval of the financial statements, including our plans for future actions.
7. All grants or donations, the receipt of which is subject to specific restrictions, terms or conditions, have been notified to you. We have evaluated whether the restrictions, terms or conditions on grants or donations have been fulfilled with and deferred income to the extent that they have not.

# Appendix F: Draft management representation letter

8. With respect to the revaluation of properties in accordance with the Code:
  - a) the measurement processes used are appropriate and have been applied consistently, including related assumptions and models;
  - b) the assumptions appropriately reflect our intent and ability to carry out specific courses of action on behalf of the council where relevant to the accounting estimates and disclosures;
  - c) where assets have been valued on a Modern Equivalent Asset basis, we have considered whether any changes are required to the Modern Equivalent Asset assumed in the valuation, or to the depreciated extent of the existing asset as a result of climate change, and we do not consider any changes are required to assumptions at this time;
  - d) the information supplied for the valuation of the council's property assets includes up to date rental and other relevant data to inform the valuation, and there are no circumstances we are aware of that would impact upon the valuation of assets (such as issues with condition) that have not been shared with the valuer.
  - e) we have considered the valuation of the council's Property, Plant and Equipment, and we are not aware of any other errors or inconsistencies, and the overall valuation movement recognised is in line with that expected from the work of the valuer.
  - f) the disclosures are complete and appropriate; and
  - g) there have been no subsequent events that require adjustment to the valuations and disclosures included in the financial statements.
9. We have considered the valuation of the Council's Property, Plant and Equipment that have not been subject to revaluation in year, and are not aware of any circumstances indicating an impairment or volatility in asset values (either in year, or on a cumulative basis since the last revaluation of the assets) that would suggest the carrying value is materially misstated as a result of it not being revalued.
10. We have reconsidered the remaining useful lives of the Council's Property, Plant and Equipment and confirm that the present rates of depreciation are appropriate to amortise the cost or revalued amount less residual value over the remaining useful lives.
11. We confirm that:
  - a) all retirement benefits and schemes, including funded or unfunded, approved or unapproved, contractual or implicit have been identified and properly accounted for;
  - b) all settlements and curtailments have been identified and properly accounted for;
  - c) all events which relate to the determination of pension liabilities have been brought to the actuary's attention;
  - d) the actuarial assumptions underlying the valuation of the scheme liabilities (including the discount rate used) accord with the Council's best estimates of the future events that will affect the cost of retirement benefits and are consistent with our knowledge of the business;
  - e) the actuary's calculations have been based on complete and up to date member data as far as appropriate regarding the adopted methodology; and
  - f) the amounts included in the financial statements derived from the work of the actuary are appropriate.
12. We have reviewed our provisioning for Non-Domestic Rates appeals and consider that the assumptions used reflect our best assessment of the liability in respect of appeals. There are no relevant facts or circumstances of which we are aware that we have not disclosed to you.
13. We have reviewed our provisioning for recoverability of non-exchange debtors, including in respect of Non-Domestic Rates, Council tax and Housing benefit overpayments, and consider the assumptions in respect of recoverability to reflect our best assessment of the recoverable amount of these balances. There are no relevant facts or circumstances of which we are aware that we have not disclosed to you.

# Appendix F: Draft management representation letter

14. We have made the following restatements to correct material misstatements in prior period financial statements that effect the comparative information:

- a) "PPE adjustments" as set out in Note 2 of the financial statements to correct errors in building and land areas used in valuation calculations; to remove assets which the council does not own or which duplicated other assets on the fixed asset register; to reclassify assets misclassified in other land and buildings to surplus assets and revalue at fair value; and to recognise assets which had been incorrectly omitted.
- b) "Leaseholder contributions" as set out in Note 2 of the financial statements to correct errors in the recognition of contributions from leaseholders to major works.
- c) "Government grants" as set out in Note 2 of the financial statements to correct errors in the recognition of grants and to correct errors in the maintenance of grant control accounts.
- d) "Schools balances" as set out in Note of the financial statement to correct errors arising from transactions with and relating to schools and to their consolidation into the financial statements
- e) "Community Infrastructure Levy" as set out in Note 2 of the financial statements to correct errors in the recognition of community infrastructure levy.
- f) "Teachers pension" as set out in Note 2 of the financial statements to correct an error relating to the omission of a pension liability relating to future direct payments to pensioners in respect of past

discretionary enhancements to benefits.

- g) "Bank offset" as set out in Note 2 of the financial statements to correct the incorrect set-off of bank overdrafts against deposits on the balance sheet.
  - h) "Other corrections" as set out in Note 2 of the financial statements
  - i) Restatement of information relating to employees receiving more than £50,000 in Note 32 Officers' remuneration to correct for the omission of certain higher paid staff and to remove from the disclosure senior staff disclosed in a separate disclosure
  - j) Restatement of information in Note 16 Financial Instruments relating to the maturity of financial liabilities to correct the basis on which the information is prepared to an undiscounted basis.
15. We have provided you with information on all subsidiaries, joint ventures and associates of the Council. We confirm our view that the Council's interests in subsidiaries, joint ventures and associates are individually and in aggregate not material and that as a result the preparation of group accounts is not required.

# Appendix F: Draft management representation letter

16. You have informed us of the following matters:

- a. Officers carried out an exercise to evaluate whether accruals were valid and recorded in the correct amount in response to errors identified by your sample testing. The exercise did not cover the whole of the population. Errors identified by the exercise were corrected. The projected error in the part of the population not covered by officers' exercise was £1450k. In addition, the exercise identified accruals totalling £687k where we were not able to obtain sufficient information to determine whether the accrual amount was valid and recorded in the correct amount. The further projected error relating to items which could not be supported is £363k. The total projected error for accruals which are not valid or could not be substantiated is £2499k.
- b. Sampling of other service expenditure identified a payment which was £155k higher than the amount due but had been expensed in full. You have informed us that the projected error across all accruals is £6.8m.
- c. In expenditure analyses provided to us, expenditure on precepts and other levies of £1859k is included twice. We have not been able to determine what adjustment if any is required in respect of this item.
- d. Your sampling of other service expenditure identified grant income which had been incorrectly set off against expenditure of £521k. You have informed us that the projected error across all credits to other service expenditure is £14.0m.
- e. You have informed us that your sampling of reconciling items in individual cash book reconciliations identified a high rate of error (approximately half) at 31 March 2019, where payments were deducted from the cash balance before their release, resulting in the understatement of both cash and short term creditors or included invalid entries which should be released to revenue accounts. The amount of unpresented cheques and BACS at 31 March 2019 was £8,127k, representing the maximum amount of error at each reporting date and the projected error approximately half of this amount.
- f. Detailed payroll reports for a sample of schools which had opted out of the council's corporate payroll arrangement could not be reconciled to the council's general ledger. The amounts recorded in the detailed payroll records for this sample was £184k more than the amount recorded in general ledger. You have informed us that the projected variance across all schools which had opted out of the corporate payroll arrangement was £1.4m.

We confirm our view that misstatements relating to these items, individually and in aggregate with other items summarised in the Appendix, are immaterial.

## *Information provided*

17. We have provided you with all relevant information and access as required by the Local Audit and Accountability Act 2014.
18. All transactions have been recorded and are reflected in the financial statements and the underlying accounting records.
19. We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.
20. We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
21. We are not aware of any fraud or suspected fraud that affects the entity and involves:
  - a. management;
  - b. employees who have significant roles in internal control; or
  - c. others where the fraud could have a material effect on the financial statements.
22. We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.
23. We have disclosed to you all known instances of non-compliance, or suspected non-compliance, with laws, regulations and contractual agreements whose effects should be considered when preparing financial statements
24. We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware.

# Appendix F: Draft management representation letter

25. All known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to you and accounted for and disclosed in accordance with the applicable financial reporting framework. On the basis of legal advice we have set them out in the attachment with our estimates of their potential effect. No other claims in connection with litigation have been or are expected to be received.
26. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities reflected in the financial statements.

## *Value for Money*

27. We acknowledge our responsibility for ensuring the Council has put in place arrangements for securing economy, efficiency and effectiveness in its use of resources.
28. We have disclosed to you all deficiencies of which we are aware in the Council's arrangements to secure economy, efficiency and effectiveness in its use of resources.

We confirm that the above representations are made on the basis of adequate enquiries of management and staff (and where appropriate, inspection of evidence) sufficient to satisfy ourselves that we can properly make each of the above representations to you.



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