


Non-Executive Report of the: Audit Committee Thursday, 26 January, 2023	 TOWER HAMLETS
Report of: Corporate Director, Resources	Classification: Unrestricted
Financial Accounts for 2018/19 and 2019/20	

Originating Officer(s)	Tim Harlock, Interim Head of Strategic Finance – Chief Accountant
Wards affected	All wards

Executive Summary

This report provides oversight of the 2018/19 and 2019/20 accounts, indicating the few remaining steps to complete sign-off, and provides a response to the material findings of the external auditor, Deloitte, with regard to the accounts, as presented elsewhere on this agenda.

It also tangentially considers the likely implications of the auditor’s findings for the accounts in future years, indicating that although much improvement has been made in underlying processes, the full force of these improvements will not come through until 2021/22 accounts (and in odd areas later years still).

Recommendations:

The Audit Committee is recommended to:

1. In conjunction with reviewing the findings of the external auditor, Deloitte, presented separately on the agenda, to note the Council’s consideration of matters therein.
2. To note that the Council will need to make a few further amendments to the Statements of Accounts for 2018/19 and 2019/20 since there are still a few items of ongoing discussion with the auditor.
3. To delegate authority to the Chair of Audit Committee and the s151 Officer to sign off the final versions of the Statements of Accounts upon completion of agreed amendments (with the only exception being if, subsequent to this meeting, significant and material matters arise).

4. To approve the refreshed Annual Governance Statements for 2018/19 and 2019/20, which have been inserted within the respective Statements of Accounts; these statements have been updated to ensure they are still appropriate to reflect the circumstances as at the date that the Statements of Accounts are approved.
5. To support officer efforts to ensure 100% of Members provide the appropriate information back to Finance to enable completion of the Related Parties note.
6. To request a report from officers providing update on the response to Deloitte's high priority control observations and recommendations as captured in the 2019/20 report.

1. REASONS FOR THE DECISIONS

- 1.1 Recommendations 3 and 4 are statutory requirements; recommendation 5 is so as to achieve full compliance with proper practice; recommendation 6 is to enable Members to be able to take assurance as to how well the accounts in future years are underpinned by best practice.

2. ALTERNATIVE OPTIONS

- 2.1 To defer approval of the accounts and Annual Governance Statement if there should be significant reason, but, ultimately, approval of the accounts is a statutory requirement.

3. DETAILS OF THE REPORT

Overview of the 2018/19 and 2019/20 accounts

- 3.1 This committee last received update reports in January 2022. Since that time officers have restated the accounts for both years, taking into account some of the findings produced by the external auditor that were presented at that meeting, and also incorporating further adjustments as required when significant matters have arisen in the intervening period.
- 3.2 Of great significance for Members will be the fact that the Council's useable reserves have remained constant throughout that period of twelve months, at a total of £559m as at 31 March 2020. This therefore helps to provide assurance that possibly the very most important aspect of the financial accounts, *the measure of resources available for service needs going into the future, has been unchanged for some considerable time.*

- 3.3 The restated accounts are provided in the Appendices, although it should be noted that a few further amendments will be required to disclosures in order to close out ongoing matters with the auditor.
- 3.4 Of special note is that the Annual Governance Statements have been refreshed in both years' Statements of Accounts in order to bring them up to date. They will require approval from this committee, and also signing off by the Mayor and Chief Executive at the same time as the auditors sign off the Statements of Accounts.

Consideration of the auditor's findings for the 2018/19 and 2019/20 accounts

- 3.5 The external auditor, Deloitte, present their findings to Members separately on the agenda of this meeting. At the time of writing this report, recognising that Deloitte were only able to provide their reports in time for a late despatch, and that officers haven't had time to fully digest all contents, officers will accept these findings on a provisional basis.
- 3.6 The audits for both years are nearing their conclusions, and, barring unforeseen significant matters arising, these two reports from Deloitte will be the final reports presented to this committee on these years.
- 3.7 The purpose of this section of the report is to provide an overview of findings, and to inform Members of the continuing improvements underway in order to address the wider implications of audit findings. Members should appreciate that officers have taken a risk-based approach to addressing the problems laid out in those reports, and that in some areas further improvement is still necessary and ongoing.
- 3.8 In the Key Messages section of their reports, Deloitte advise where they will issue qualified opinions; officers have been suitably advised by Deloitte on these matters. At this stage, the position on qualifications is as follows:
- The Council accepts the qualifications for failure to prepare group accounts in 2018/19 and 2019/20; group accounts are being prepared for the next version of the 2020/21 accounts.
 - The Council accepts the qualifications regarding the experience item on the net pension liability (as recorded in the 2019/20 accounts, but with probable consequences for both years); since this stems from a true-up between the actuary's annual IAS 19 report and the triennial valuation report as at 31 March 2019, this is unlikely to repeat in the following year (but thereafter may be dependent on the quality of the underlying data presented to the actuary).
 - The Council accepts the qualifications regarding related party relationships; officers are hopeful of avoiding qualification on the 2019/20 data (but understand that the 2019/20 accounts will receive a qualification due to the comparative information, ie the previous year's

disclosure). Officers are aware that for later years there is not a full set of returns from Members, and so the Council is likely to face further qualifications on this matter in 2020/21, 2021/22 and 2022/23 without remedial action.

- The Council accepts the qualifications regarding disclosure of officers' remuneration; in large part this has arisen through having a large number of schools use a third-party payroll provider. Officers have improved the quality of the data requests to this payroll provider, but there may still be some discrepancies to iron out in the capture of payroll costs on the Council's General Ledger in 2020/21.

3.9 In the Significant Audit Risks sections, Deloitte advise of areas which have been highlighted for particular attention. The Council's comments and response, which focus on what we are doing to improve in future years, are as follows:

- Valuation of Properties: officers have worked extensively to improve processes jointly with the Place Directorate, and this has been captured through the Finance Improvement Plan (FIP) under the oversight of the Finance Improvement Board (FIB) and the Corporate Leadership Team (CLT).
- Management Override of Controls: this is an ongoing area of work, since it includes the way that processes have been configured on the Agresso system. In particular, journal processes and policies have been reviewed through the oversight of the FIB, but it is unlikely that there will be significant implementation of improvements until 2022/23. Officers note the need to, and will continue to, improve the quality of working papers.
- Capitalisation of Expenditure: officers have improved the validation processes applied to expenditure captured under capital for 2020/21, and subsequently constituted an organisation-wide capitalisation guidance note to ensure the consistent and accurate treatment of qualifying expenditure; this has been discussed and the implications agreed at CLT
- Recognition of Grant Income and Expenditure: officers had made mistakes in this area as a result of (poor/inadequate) custom and practice of recent years, and also because Tower Hamlets actually has exceptional sums and complexity in some areas compared to other councils. Improvements implemented in 2020/21 include preparation of a comprehensive grants register, and embedding the learning obtained from the last two years with respect to developers' monies received (in the guise of both s106 contributions and Community Infrastructure Levy), and leaseholders' contributions to major works. There has been extensive engagement between the central finance team and the operational teams for administering developers' contributions so as to improve understanding of accounting requirements.

3.10 With regard to the Other Areas of Judgment section, this report will concentrate on 2019/20 issues, being the most relevant for current and future circumstances. The Council's comments are as follows:

- Indemnity given to Tower Hamlets Homes Limited in respect of future pension costs: the treatment adopted in the 2019/20 accounts has been deemed to be appropriate once the wider context was revealed.
- Consolidation of Schools' Balances: it has been reported previously to the Audit Committee that this area has been incorrectly accounted for in previous years at the detailed level, and officers have put great effort into ensuring that significant balances are correct. In the opinion of senior finance officers, errors such as they are in the accounts do not represent a significant financial risk to the Council. Going forwards, as part of the FIP, the process for paying schools has undergone fundamental review and revision but that change came into effect from April 2021, so will not impact until the 2021/22 Accounts. In addition, there has been a wider Schools Finance Improvement Plan, which has been implemented so as to provide greater assurance regarding processes followed.
- Preparation of Group Accounts: from a technical analysis of requirements, group accounts are required, and officers will prepare these for the 2020/21 accounts. In the meantime, for previous years, the opinion of officers is that not having presented group accounts does not constitute any financial risk to the Council and, therefore, are not planning to revise the accounts for previous years.
- NNDR Appeals Provision: officers made judgements based on the information available at the time, and in the light of resource constraints. For 2020/21 accounts a fresh approach has been adopted that takes account of more data, and should be able to estimate requirements to a better standard.
- Pension Liability Relating to the Tower Hamlets Pension Fund. There are two fundamentally different groupings of findings from Deloitte: firstly, those based on professional judgements, which includes the comments on inflation rate assumptions and the potential allowance for the effects of the Goodwin case, and officers consider these as useful reflections, but no more than that. Secondly, there is explanation of the substance of the experience item, which officers accept has probably led to an incorrect split of impacts over 2018/19 and 2019/20 taken separately. However, when these effects are taken cumulatively, they lead to the same assessment of the net pension liability on the balance sheet as at 31 March 2020; and officers are therefore of the opinion that this poses no financial risk to the Council and, therefore, are not planning to revise the accounts.

- Infrastructure Assets. This area is one that has arisen as a result of national discussion. To remediate, the Council has already adopted the provisions of the statutory instrument published in December 2022, and is now working through the very recent guidance issued by CIPFA on 11 January 2023. This is likely to complete by early February, and initial work would indicate that there will not be any impact on the balance sheet, but we will still need to amend disclosures and accounting policies in order to comply.
- Officer Remuneration. The processes followed during the preparations for 2018/19 and 2019/20 accounts did not provide sufficient assurance on the accuracy of the data from which the notes were compiled. For 2020/21, processes were improved, and for 2021/22 further improvements yet were implemented.

3.11 At the same time as auditing our financial statements, the external auditor is required to present opinion on the Council's arrangements to secure economy, efficiency and effectiveness from its use of resources. For 2018/19 Deloitte are expecting to qualify this opinion in respect of three matters, falling to two matters for the following year. The Council's comments regarding these two outstanding matters are as follows:

- Financial reporting arrangements have clearly been strained over the past two years. Although senior finance officers believe that significant improvements have been taking place, to the extent that no qualifications on the financial statements for 2020/21 might be possible, it is difficult to envisage that the timing aspect has been improved sufficiently to avoid a qualification under this section.
- Risk management and internal controls have been within the work programme of the Finance Improvement Board, and significant progress has been made; however, it should be appreciated that some of the workstreams are still ongoing.

3.12 Deloitte have made observations on controls in section 6 of their reports. This section includes recommendations, and the Council's response to the 'high priority' items outlined in the 2019/20 report is as follows:

- Preparation of Accounting Papers: officers agree that further improvement is required in preparing papers, and are seeking to embed a more comprehensive process that addresses this shortfall; however, officers do not accept that presenting detailed accounting papers to the audit committee is either necessary or helpful.
- Accounts closure resourcing and quality assurance processes: the experience of the last two years has led to many lessons learnt, and has had the engagement of CLT, and the wider organisation. The FIB was set up in order to address many of the underlying issues, though officers advise that we are still in a transitional phase of improvement,

and further reorganisation within the division of Finance, Procurement and Audit is underway.

- Reconciliation of general ledger accounts and segregation of duties: as mentioned previously, the FIB was set up to address underlying issues, and this is an area where some significant progress has been made.
- Completeness of disclosures: this is an area of ongoing improvement. Officers are responding to the findings set out in the Deloitte reports, and will continue to be alert to changing requirements in the future. Officers accept that only partial progress was made on this in the 2020/21 accounts.
- Accounting estimates: officers accept that this is an area where ongoing improvement is required.
- Classification of expenditure as capital: this has already been fully addressed, as set out in paragraph 3.9 (3rd bullet point).
- Valuation of properties: this is an area where the Council has made much progress already, within the work programme of the FIB. Officers will review the specific recommendations set out in the Deloitte report.
- Recognition of grants and contributions: processes have already improved here to a large extent as a result of lessons learnt. Officers will review the specific recommendations set out in the Deloitte report.
- Infrastructure assets: this is clearly an area where officers will need to be vigilant, and aware of the potential for changing requirements in coming years.
- Journals: this is within a wider piece of work being taken forward by the FIB; however it is unlikely to come to fruition before 2022/23.
- Other matters: these will be given due consideration by officers.

3.13 Finally, it should be noted that there is a dependency on the predecessor audit firm issuing their certificates for the 2016/17 and 2017/18 years before Deloitte can completely close off 2018/19 and 2019/20.

4. EQUALITIES IMPLICATIONS

4.1 There are no equalities implications arising from this report.

5. OTHER STATUTORY IMPLICATIONS

5.1 Approval of the accounts, once Members are satisfied, is a statutory responsibility that falls to Audit Committee.

6. COMMENTS OF THE CHIEF FINANCE OFFICER

- 6.1 This whole report presents matters that are directly concerned with fulfilment of the role and responsibilities of the s151 officer.

7. COMMENTS OF LEGAL SERVICES

- 7.1 Regulation 10 of the Accounts and Audit Regulations 2015 requires a local authority to publish their statement of accounts not later than 31 July of the financial year immediately following the end of the financial year to which the statement relates, or, for the financial year starting in 2019, not later than 30 November. These dates have not been kept.
- 7.2 Regulation 3 of the Accounts and Audit Regulations 2015 requires a local authority to have a sound system of internal control which ensures that the financial and operational management of the authority is effective.
- 7.3 Save as mentioned above, the matters set out in this report comply with the above legislation.
- 7.4 The Council's Constitution permits delegation of functions as proposed in this report.
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Linked Reports, Appendices and Background Documents

Linked Report

- There have been various updates provided to this committee since July 2019 from both Deloitte and officers, but this report, taken together with the Deloitte reports presented on this agenda, are self-contained.

Appendices

- Appendix A: 2018-19 Statement of Accounts
- Appendix B: 2019-20 Statement of Accounts

Local Government Act, 1972 Section 100D (As amended)

List of "Background Papers" used in the preparation of this report

List any background documents not already in the public domain including officer contact information.

- NONE.

Officer contact details for documents:

N/A