

<p>Non-Executive Report of the:</p> <p>Audit Committee</p> <p>23 November, 2023</p>	 <p>TOWER HAMLETS</p>
<p>Report of: Julie Lorraine, Corporate Director - Resources (Section 151 Officer)</p>	<p>Classification: Unrestricted</p>
<p>Control Observations for 2019-20, and progress in addressing these</p>	

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

Executive Summary

This report provides officer consideration of control observations as presented by the external auditor, Deloitte, in their report on the 2019/20 accounts, to this committee on 26 January 2023.

Far from being just an analysis of historical issues, the overarching purpose of this report is to ensure Members are sighted on the improvements being made to financial controls, such that at year-end the accounts can be brought together more reliably and more efficiently in future years.

Recommendations:

The Audit Committee is recommended to:

1. Note the Council's progress to date.

1. REASONS FOR THE DECISIONS

- 1.1 No decision required.

2. ALTERNATIVE OPTIONS

- 2.1 Non-applicable.

3. DETAILS OF THE REPORT

- 3.1 As well as “signing off” the Statement of Accounts, the external auditor also performs another function, that of making control observations on the framework of processes that underpin the production of the accounts. A substantial report was presented to this committee, by Deloitte, on 26 January 2023 which included a section on control observations (section 6 of the report).
- 3.2 The purpose of this officer report is to provide a response to those findings, and to inform Members of the continuing improvements underway in order to address the wider implications of audit findings.
- 3.3 Before detailed examination of those findings, the wider context of the accounts and the extended audit is worth a little consideration:
- The 2018/19 and 2019/20 accounts were required to have been published in their final, audited, version some four and three years ago respectively.
 - Financial reporting arrangements have clearly been strained over recent years. Although senior finance officers believe that significant improvements have been taking place, they acknowledge that not everything had been fixed by the time the 2020/21 accounts were compiled.
 - Interim anecdotal feedback from Deloitte is that the quality of working papers has improved during the 2020/21 audit, but still has further to go.
 - Risk management and internal controls had been within the work programme of the Finance Improvement Board (which presented its final report to this committee in June 2022), and significant progress had been made; however, it should be appreciated that officers had taken a risk-based approach to addressing the problems laid out in those reports, and that in some areas further improvement may still be necessary.
- 3.4 Dealing with the recommendations themselves now, in the following sections the Deloitte recommendation will be presented in bold, and the response of the Council will follow immediately afterwards.
- 3.5 **Recommendation 1: Preparation of accounting papers**
- **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.**
 - Officers agree that further improvement was required in preparing papers, and the Council continues to seek to embed a more comprehensive process that addresses this shortcoming (notwithstanding the improvement already noted for 2020/21); however, only significant

changes in accounting policy would be reported to the Audit Committee, it would not be necessary or beneficial to present all detailed accounting papers to the audit committee.

3.6 Recommendation 2: Accounts closure resourcing and quality assurance processes.

- **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 that will apply. We also recommend the Council considers whether there are year-end processes which can be streamlined or pulled forward to earlier in the year.**
- The experience of recent years has led to many lessons learnt, and has had the engagement of CLT, and the wider organisation. The Finance Improvement Board 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 without the benefit of a further year's completed audit to confirm progress, or confirmation that improvements have completely embedded.
- Year-end training has been provided to service management to enable better engagement with requirements, and with a wider group of staff to support more accurate capture of supplier costs and resourcing of the audit is kept under review to ensure there are no bottlenecks or capacity issues.
- Although officers have been endeavouring to improve processes, both of a wide-ranging and more detailed nature, the experience of the 2020/21 audit so far is that there are still areas where there is further work required which will be fed into future years' preparation of accounts.
- Officers pro-actively continue to learn from the 2020/21 audit process, and capture lessons learnt, which may require further training for some officers, enhanced approaches to quality assurance, and in some areas re-design of processes to ensure they are comprehensive and reliable.

3.7 Recommendation 3: Reconciliation of general ledger control accounts and segregation of duties. We recommend:

- **Responsibility for each control account is assigned to a named preparer and reviewer (with those roles allocated to different officers).**
- **The frequency and timescale for preparation and review of reconciliations is set down in written instructions to staff.**
- **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.**
- As part of the work of the Finance Improvement Plan, a dashboard of key controls and reconciliations was developed, which set out the ownership of each key control and the expected actions required. This dashboard is presented on a monthly basis to the Finance Department Leadership Team – Strategy meetings, which are chaired by the Director of Finance, Procurement and Audit. Status of reconciliations are RAG rated and areas of exception are followed up to resolve issues on a more timely basis.

- This dashboard is evolving, and is also used to highlight system changes that could improve processes.

3.8 Recommendation 4: Completeness of disclosures

- **We recommend a detailed review of the completed CIPFA disclosure checklist is carried out.**
 - For purposes of the 2020/21 accounts, the key foundation of the preparation work was to incorporate as much of the learning from the previous years as possible, thus implicitly building on the previous findings of the auditors, in the knowledge that there had been minimal significant amendments to the CIPFA Code since 2019/20.
 - For future years' accounts a check against the CIPFA checklist will be completed.

3.9 Recommendation 5: Valuation of properties

- **We recommend the Council prepares and maintains 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.**
- **We recommend the Council 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.**
- **We recommend the council 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.**
- **We recommend the Council prepare a paper to support the decision not to value particular assets prior to publishing its draft statement of accounts.**
 - As part of the work within the Finance Improvement Plan, the Council has developed a far more robust approach to valuations of properties, whereby the internal expertise of the Asset Management team is very much engaged. Within this approach, consideration is given to:
 - Categorisation of asset class (with a particular emphasis on movements out of Assets under Construction, and movements into or out of Surplus Assets).
 - Whether there has been any impairment.
 - Identifying, at draft valuation stage, whether there have been significant movements in the proposed valuation, and then following up with the valuers to either validate, or amend, the approach accordingly, including reviewing/challenging inputs and assumptions.
 - Although this engagement with the Asset Management team is considered to have brought about significant improvement in valuations over previous years, officers acknowledge that further refinement of the process may be beneficial and will examine the most efficient and effective way to achieve this.

- Standard spreadsheet controls have been applied to the fixed asset register.
- In future years, as part of the assurance process regarding adequacy of valuations, officers will prepare a comprehensive paper of which assets have not been revalued, together with the rationale behind this.

3.10 Recommendation 6: Journals

- **Re-visit which 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.**
- There has been a significant piece of work undertaken, as part of the Finance Improvement Plan, to address the efficacy and efficiency of posting journals.
- Changes have been made to the Agresso workflow such that most “bulk upload” journals require an approval (on the system) before posting; this new process has been live only since August 2023, and will require review to ensure that it is achieving objectives.

3.11 Recommendation 7: Recognition of grants and contributions. We recommend:

- **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.**
- **The decision is reflected in the type of general ledger code set-up to record the grant.**
- **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.**
- A new framework of control, the maintenance of a grants register, was implemented in 2020/21 as part of the Finance Improvement Plan.
- This management tool improved the capture of data over the previous year, but it will be necessary to undertake thorough review of implementation, as it appears that (coming out of the experience of the audit process of 2020/21) there have also been incidents of incomplete information and some inaccuracies being captured.
- Notwithstanding recognising the need for further improvement in this area, officers would, however, like to draw Members’ attention to the fact that the circumstances of Covid-19, and the welcome government response of providing numerous one-off emergency grants, made this a very challenging year for bedding in best practice with respect to grants accounting.

3.12 Recommendation 8: Classification of expenditure as capital

- **We recommend the Council implements a control to prevent revenue expenditure being erroneously treated as capital.**
- A corporate approach to capitalisation was developed through the Capital Delivery Board in time for the 2020/21 accounts.

- In the 2020/21 accounts detailed examination of the capitalisation of salary costs was conducted, and the underpinning control process is the filling out of timesheets.
- Where decisions have been made to stop a capital scheme in a more recent year (ie 2022/23), both in-year and previous years' expenditure was reviewed in accordance with the definitions and controls and written off to revenue cost centres.

3.13 Recommendation 9: Other matters, miscellaneous

- **Assets in Vehicles, Plant and Equipment and Infrastructure categories do not always contain detailed descriptions and in some cases have been aggregated by type and year of acquisition. As a result, it is not readily possible to determine whether assets remain in operational existence.**
- **Incorrect classification of non-current assets was identified in our testing including fixtures, fittings and equipment purchased as part of a larger project (for example a refurbishment) were incorrectly classified as other land and buildings and as a consequence written out when the buildings was not revalued.**
 - Officers accept the observations as presented (with the caveat that to large extent the matters noted regarding Infrastructure Assets have been largely addressed by dint of amendments to the Code and statute), and will look to review the register, taking into account the availability and timing of resources.
- **The coding structure within the council's main accounting system has codes designated for recharge income and expenditure. These were not consistently used. This complicated the year end process for eliminating internal income and expenditure amounts and incomplete elimination of such income and expenditure in the initial version of the accounts. We understand the council proposes to discontinue or limit the system of recharges going forwards. We also identified instances where internal trading between the council and schools had not been correctly eliminated.**
 - Fundamental and substantial progress has been made on this front, and officers continue to be alert to this risk; however, some errors, albeit on a far lesser scale, have been identified in the 2020/21 audit. Work to date has transformed this from being a widespread systemic error to being residual instances of one-off errors, and officers will continue to correct these instances if and when they are discovered and inform officers not to use the incorrect codes.
- **Bank reconciliations were not carried out for all corporate accounts and for others the analysis of reconciling items was presented in a way which readily showed which items represented true reconciling differences at the reporting date. The reconciliation of schools' bank accounts was complicated by the use of a single general ledger control account and reconciling items included amounts which were**

not valid reconciling items, including amounts relating to input VAT to be reclaimed and outstanding creditors.

- Corporate bank accounts are now all reconciled through a re-designed reconciliation template which provides far greater transparency and assurance.
 - Schools' bank accounts were again impossible to reconcile flawlessly in the 2020/21 financial year due to the continuation of the previously recognised inadequate framework of coding and controls; however, this was completely re-designed as a key element of the Finance Improvement Plan, and the new control framework went live at the start of 2021/22.
- **Three other observations.**
 - There were three other matters, deemed by senior finance officers to be of lesser significance, for which the relevant officers in other departments have been advised, for their consideration.

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, as noted in the report.
- 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.

Linked Reports, Appendices and Background Documents

Linked Report

- Various updates provided to this committee since July 2019 from both Deloitte and officers.

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

List of “Background Papers” used in the preparation of this report

- Deloitte Report to the Audit Committee 26 January 2023 on the audit for the year ended 31 March 2020.

Officer contact details for documents:

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