

Decision Maker: GENERAL PURPOSES AND LICENSING COMMITTEE

Date: 30th July 2020

Decision Type: Non-Urgent Non-Executive Non-Key

Title: AUDIT OF FINANCIAL STATEMENTS 2018/19

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Ward: Borough Wide

1. Reason for report

- 1.1 This report sets out the Council's 2018/19 statutory accounts for approval by Members in accordance with the requirements of the Accounts and Audit Regulations 2015. The report also details the conclusions and significant issues arising from the work carried out in relation to the audit of the 2018/19 accounts.
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2. **RECOMMENDATION(S)**

2.1 **The Committee is requested to:**

- (a) **Approve the Council's statutory accounts and Annual Governance Statement for 2018/19 (Appendix 1)**
- (b) **Authorise the Chairman to sign and date the Statement of Accounts [on page 1] as a formal record of the Committee's approval**
- (c) **Consider the external auditor's Audit Results Report (Appendix 2)**
- (d) **Note the status of the auditor's conclusion on Value for Money (paragraph 3.13)**
- (e) **Confirm agreement with the auditor's conclusion on their independence and objectivity (paragraph 3.14)**
- (f) **Note the objections to the accounts (paragraphs 3.17 to 3.19)**
- (g) **Authorise the Chairman of this Committee to sign the letter of representation for 2018/19 on behalf of the Council (Appendix 3 and supporting schedule at Appendix 4)**

Impact on Vulnerable Adults and Children

1. Summary of Impact: None arising directly from this report
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Corporate Policy

1. Policy Status: Existing Policy
 2. BBB Priority: Excellent Council
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Financial

1. Cost of proposal: Not Applicable
 2. Ongoing costs: Not Applicable
 3. Budget head/performance centre: Council wide
 4. Total current budget for this head: £150.6m 2018/19 budget (excluding GLA precept)
 5. Source of funding: N/A
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Personnel

1. Number of staff (current and additional): 2,038 FTE posts (per 2018/19 Budget) which includes 504 for budgets delegated to schools
 2. If from existing staff resources, number of staff hours: N/A
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Legal

1. Legal Requirement: Statutory Requirement: The statutory duties relating to financial reporting are covered within the Local Government Act 1972, the Local Government Finance Act 1998, the Local Government Act 2000, the Local Government Act 2002 and the Accounts and Audit Regulations 2015.
 2. Call-in: Not Applicable
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Procurement

1. Summary of Procurement Implications: None arising directly from this report
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Customer Impact

1. Estimated number of users/beneficiaries (current and projected): The 2018/19 final accounts reflect the financial impact of the Council's strategies and service plans which impact on all of the Council's customers, including council tax payers and users of our services.
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Ward Councillor Views

1. Have Ward Councillors been asked for comments? Not Applicable
2. Summary of Ward Councillors comments: Council Wide

3. COMMENTARY

- 3.1 The Accounts and Audit Regulations 2015 require the Statement of Accounts to be considered and approved by resolution of a Committee or Full Council. Following approval, the Statement of Accounts must be signed and dated by the person presiding at the meeting at which that approval was given.
- 3.2 Before the Committee is able to approve, the Director of Finance must re-confirm on behalf of the authority that he is satisfied that the Statement of Accounts presents a true and fair view of the financial position of the authority at the end of the financial year and of the authority's income and expenditure for that year.
- 3.3 2018/19 was the first year that the audit has been undertaken by Ernst & Young LLP (EY) who was appointed as Bromley's external auditor from 1st April 2018. Public Sector Audit Appointments (PSAA) is responsible for appointing an auditor for the five-year period to 2022/23 to relevant authorities that have chosen to opt into its national auditor appointment arrangements. In August 2017 PSAA wrote to the Council to formally consult on the appointment of EY as Bromley's external auditor for 5 years from 2018/19. The appointment was confirmed in December 2017.
- 3.4 The Accounts and Audit Regulations 2015 required financial statements for this period to be approved and published no later than 31st July 2019. However, as previously reported to Committee, completion of the audit has been substantially delayed owing to issues in relation to the valuation of fixed assets.
- 3.5 At its meeting on 28th November 2019 the Committee received a report from the Council's external auditor EY entitled 'Audit of Financial Statements 2018/19' and was informed that EY had not yet been able to conclude its audit of the Council's main accounts due to issues relating to asset valuations. In all other respects the audit was substantially complete. EY's report stated that *'we have substantially completed our audit of the Council for the year ended 31st March 2019, subject to auditing adjustments made to the financial statements to correct current and prior year valuation of the Council's long term physical assets, which have resulted in delays to the audit process. We consider this issue further in the detailed report. We will not be able to fully conclude until these adjustments are made'*.
- 3.6 The Council's valuations in relation to 2018/19 were carried out by Cushman and Wakefield (C&W) under the responsibility of the Assistant Director – Strategic Property. As set out in EY's initial report, their work identified pervasive and material errors in the external valuation of the Council's land and buildings. These errors covered both the accuracy of base data used to inform the valuations (e.g. floor areas) and the key assumptions made by the valuer (e.g. estimates of asset yield). As a result of material variations between the original and revised valuations, combined with a lack of consistency in the type of error, it was not possible to argue that the errors were isolated to the assets reviewed or that the results of the revised valuations could be extrapolated. It has therefore been necessary for the Council to produce and account for the impact on our financial statements, effectively re-stating both the 2017/18 and 2018/19 accounts (prior period adjustment). Further detail was provided in the report to this Committee on 28th November 2019.
- 3.7 Significant work has been undertaken, initially requiring C&W and in-house LBB valuers to undertake a full revaluation exercise (100% of the Council's assets) as at 31st March 2019. Backward indexation was then applied to determine values as at 31st March 2018 and 1st April 2017. Assets that were disposed of during this period, or those that transferred between asset classes, required additional valuations to be undertaken. Following detailed reconciliations between the C&W 'master file' and the Council's Fixed Asset Register, accounting entries for 2017/18 and 2018/19 have been re-worked and the accounts have been re-stated. A

summary of the impact on prior year accounts is set out in Note 6B of the updated financial statements.

- 3.8 The draft 2018/19 (pre-audited) accounts were approved by the Director of Finance on 31st May 2019 and were published on the Council's website. A summary of the key changes that have been required to be made to these draft accounts includes:
- (i) Revaluation restatements: the impact on prior year accounts is shown in Note 6B of the updated financial statements. The impact on the 2018/19 balance sheet is a £42.8m reduction in the carrying value of fixed assets matched by a corresponding reduction in unusable reserves. Information for 2018/19 in the other core statements (Comprehensive Income and Expenditure Statement, Movement in Reserves Statement and Cash Flow Statement) and all relevant disclosure notes have also been restated.
 - (ii) McCloud judgement: relating to a legal case regarding age discrimination within the Judicial and Fire Pension Schemes. In June 2019 the Supreme Court denied the Government's request for an appeal and it has since been confirmed that the difference in treatment will need to be remedied across all public service pension schemes, including the LGPS. As a result, employers in the LGPS have been required to re-state their 2018/19 accounts to reflect the estimated impact on IAS19 and IAS26 calculations as an adjusting post balance sheet event (see Note 6A). The impact on the 2018/19 balance sheet is an increase of £23.7m in long term liabilities and a corresponding reduction in unusable reserves. Information for 2018/19 in the other core statements (Comprehensive Income and Expenditure Statement, Movement in Reserves Statement and Cash Flow Statement) and all relevant disclosure notes has also been restated.
 - (iii) Covid-19: Since the 2018/19 audit was incomplete and the accounts had not been issued at the time at which the pandemic started impacting the UK, a non-adjusting post balance sheet event has been disclosed (see Note 6A). As this is a non-adjusting event, no amendments are required to the 2018/19 accounts. Additionally, commentary on Covid-19 has been added to the narrative report to explain the financial impact in more detail. Similarly, within the Accounting Policies disclosure (see Note 1) the Council has reaffirmed that the accounts have been prepared on a 'Going Concern' basis and provided details on its underlying financial resilience and governance, in light of the challenges posed by Covid-19.
- 3.9 EY has now issued its final Audit Results Report on the main financial statements and accounts for 2018/19. A copy of this report is attached at Appendix 2 and includes the findings from the interim and final audits and recommendations for improvement. At the time of writing, the auditors anticipate issuing an unqualified audit opinion on the financial statements.
- 3.10 In accordance with ISA260, the external auditor is required to report all uncorrected audit differences, other than those that it believes are clearly trivial, to those charged with governance. It is also required to report any material misstatements which have been corrected and which it believes should be communicated to the Committee to assist in fulfilling governance responsibilities. A number of amendments have been required to correct for the material errors in the valuation of the Council's long term physical assets in both the current and previous year accounts. A number of other amendments have been made to the financial statements as a result of the audit work which the auditor does not consider to be sufficiently significant to bring to the Committee's attention. A small number of minor presentational changes were agreed and the financial statements have been updated accordingly. None of

these matters have an impact on the Council's revenue accounts or general fund balance. EY has highlighted two unadjusted differences in its report; these are judgemental differences relating to the GMP pension liability (£1.98m) and an initial error of £14k in relation to assets which has been extrapolated to a value of £596k. EY states in its report that '*Both items [above] are estimates calculated based on audit findings and as such we would not be expected to be amended in the financial statements due to their nature. They are calculated to provide an indication of whether additional work is required to establish whether there is a risk of material misstatement. Given that the estimates are not material, no further work is indicated*'. Appendix 4 provides further details on these matters.

- 3.11 As required by ISA 260 and other ISAs specifying communication requirements, the auditor is required to inform the Committee of any significant findings from the audit and other matters if they are significant to the oversight of the Council's financial reporting process. There are no matters that the auditors wish to draw to the attention of the Committee other than those highlighted in the auditor's findings report.
- 3.12 The auditor's report also reviews accounting systems and systems of internal control as part of an assessment of the control environment. It is required to report to this Committee any significant deficiencies in internal control. It has not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in the financial statements. EY has, however, identified six areas where internal control should be improved and these are included with corresponding recommendations in Appendix 2.
- 3.13 The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the Authority 'has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources'. For 2018/19 this is based on the overall evaluation criterion 'in all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people'. Owing to the outstanding objections (see paragraphs 3.17 to 3.19) EY has indicated that it is not able to issue a VfM conclusion at the present time.
- 3.14 The auditor's report details the requirement for annual disclosure of all relationships between EY and the Council that may reasonably be thought to bear on its integrity or objectivity, including those that could compromise independence. In conclusion EY has confirmed that, in its professional judgement, EY is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements. It has also confirmed that there are no relationships from 31st March 2018 to the date of their report which it considers may reasonably be thought to have a bearing on independence and objectivity. This Committee is requested to consider the matters detailed in the external audit report and confirm agreement with their conclusion on independence and objectivity.
- 3.15 In accordance with the Accounts and Audit Regulations 2015 the Director of Finance, as responsible financial officer, has authenticated and signed the amended accounts and the authorised for issue date has been updated to 30th July 2020. The Statement of Accounts, accompanied by the Annual Governance Statement, is attached at Appendix 1.
- 3.16 The Council's Accounts and related records were made available for public inspection for 30 working days between 3rd June 2019 and 12th July 2019. This is a requirement of the Regulations and must take place prior to the completion of the audit.
- 3.17 A local elector has raised an objection to the 2018/19 accounts. There are a range of matters set out in the objection which primarily relate to waste management and waste collection

services but also include grounds maintenance contract, street cleansing contract and civic centre empty offices. These are similar issues to those raised in previous objections but have been extended to include matters relating to the tendering and letting of the new environmental services contract. The objection was submitted on 6th July 2019 and EY has indicated that it will consider the objections raised matter once KPMG has concluded its work on the related objections in relation to 2016/17 and 2017/18

- 3.18 Members will be aware of the objections made in relation to the 2016/17 and 2017/18 accounts relating to the Council's waste management and waste collection services, and the on-going management of the waste management and street cleansing contracts. The 2017/18 objection also includes areas relating to the grounds maintenance contract as well as civic centre empty offices. As KPMG was the Council's external auditor during 2016/17 and 2017/18, it has responsibility for reviewing these matters. At the time of writing these objections have not yet been concluded.
- 3.19 The objections to the 2016/17, 2017/18 and 2018/19 accounts are from the same elector. As a result of these objections remaining unresolved, the audit for these years cannot be formally concluded and an audit certificate issued.
- 3.20 The Council has very little discretion over the format of its Accounts as they must be presented in the form prescribed in the Code of Practice on Local Authority Accounting (the Code). The Code is published by the Chartered Institute of Public Finance and Accountancy (CIPFA) under the oversight of the Financial Reporting Advisory Board. The Code requires authorities to produce accounts based on International Financial Reporting Standards (IFRS) while at the same time recognising the particular position of local government where legislative requirements override accounting principles in some areas.
- 3.21 The Statement of Accounts reflects the 2018/19 outturn position for both capital and revenue in the required statutory format. The overall outturn position for 2018/19 was reported to the Executive on 21st May 2019 with more detailed information being reported to individual PDS Committees. This report identified the key cost variations compared with the 2018/19 budget. Details of variations relating to the 2018/19 capital programme outturn were also reported to the Executive in May 2019 and there was no requirement to use General Fund balances to support the capital programme.
- 3.22 The sections that follow provide a brief commentary on the main points to note in the Accounts.
- 3.23 The Comprehensive Income and Expenditure Statement (CI&E Statement)
- 3.23.1 This statement reports on how the authority performed during the year and whether its operations resulted in a surplus or deficit. Specifically, it brings together all of the functions of the Council and reports on the Council's income and expenditure in accordance with International Financial Reporting Standards (IFRS) rather than just the amount to be funded from local taxes, rents and government grants. This difference is accounted for by a series of adjustments made in accordance with regulations.
- 3.23.2 Any surplus or deficit reflected on the CI&E Statement is offset by the movement shown in the MIRS, as detailed within note 8 of the Accounts and section 3.24 below. These two statements should be considered together and the overall position is summarised on page 16 of the accounts. The result is an overall increase in the Council's general fund balance and earmarked reserves of £23.6m.

3.24 Movement in Reserves Statement (MIRS)

- 3.24.1 This statement shows the movement from the start of the year to the end on the different reserves held by the authority (as shown in the bottom half of the Balance Sheet), analysed into 'usable reserves' (i.e. those that can currently be used to fund expenditure or reduce local taxation) and other 'unusable' reserves (those that an Authority is unable to utilise to provide services).
- 3.24.2 The crucial line in the MIRS is the one containing adjustments between the accounting basis and funding basis under regulations. The Comprehensive Income and Expenditure Statement (CI&E Statement) is prepared wholly in accordance with accounting standards but local authorities are subject to specific rules and statutory requirements which, in significant instances, differ substantially from proper accounting practices particularly in relation to capital accounting and retirement benefits. This line reconciles the surplus or deficit on the provision of services as detailed in the CI&E Statement with the statutory amounts required to be charged to the general fund balance for council tax setting purposes.
- 3.24.3 Usable reserves showed an overall increase of £24.9m in 2018/19 which was due to an increase in earmarked reserves of £23.6m and a net increase in capital grants unapplied and capital receipts of £1.3m.
- 3.24.4 Unusable reserves decreased by £21.3m which was mainly due to the Pension Reserve (£14.8m), Capital Adjustment Account (£3.7m) and other net variations of £2.8m. The movement on the Pension Reserve was due to an increase in the net liability from £68.0m to £82.8m mainly due to the estimated impact of the McCloud judgement on past service costs and interest on liabilities being higher than interest on plan assets. The reduction to the Capital Adjustment Account was the result of a number of accounting entries relating to depreciation and impairment of non-current assets and the write-off of asset values on disposal or sale offset by capital grants and other sources of capital financing.

3.25 Balance Sheet

- 3.25.1 The balance sheet provides a snapshot of the Council's financial position, its assets and liabilities, at 31st March 2019. Compared to the position in 2018 (restated), Property Plant & Equipment asset values increased by £1m, Investment Properties decreased by £5.4m and Assets Held for Sale decreased by £1.8m (overall net reduction of £6.2m). The Council's assets are valued on different bases depending on the type of asset, as described in the Accounting Policies Note.
- 3.25.2 Other significant variations between the 2018 and 2019 Balance Sheet dates include an increase of £80.8m in the value of short term investments (1 year or less to maturity) offset by a reduction of £44.4m in long term investments (1 year or more to maturity) whilst cash and cash equivalents (instant or easy access) has reduced by £7.6m.
- 3.25.3 The net Pension Fund liability has increased by £14.8m, mainly due to the estimated impact of the McCloud judgement on past service costs and interest on liabilities being higher than interest on plan assets. Proper accounting practice requires that the actuarially calculated fund deficit, in relation to Bromley's employees and pensioners, is disclosed on the face of the Council's Balance Sheet. The net liability of £82.8m represents the difference between the bid value of assets and the value of liabilities based on a valuation carried out by the Actuary as at 31st March 2019 in accordance with the requirements of IAS19. This is different from the Actuary's triennial valuation that determines the contribution rate to the Pension Fund. Although the liability has a significant negative effect on the net worth of the Authority, the

contribution payments agreed as a result of the 2016 triennial valuation include arrangements to clear the deficit over a 12 year period from 1st April 2017.

3.26 Cash Flow Statement

3.26.1 The Cash Flow Statement shows the changes in cash and cash equivalents of the authority during the reporting period. The statement shows how the authority generates and uses cash and cash equivalents by classifying cash flows as operating, investing and financing activities.

3.27 Notes to the Main Statements

3.27.1 The notes to the Accounts are grouped together at the end of the main statements rather than following each statement individually. They provide information that supports the main financial statements and the disclosure of additional information required by the Code.

3.28 Pension Fund Accounts

3.28.1 These are the accounts of the London Borough of Bromley pension fund that provides pension benefits for staff, excluding Teachers and staff in the NHS pension scheme. The accounts relate to the whole fund including the assets and liabilities of the scheduled and admitted bodies.

3.28.2 During 2018/19 the net assets of the Fund increased by £72m, mainly as a result of investment performance (net return of £81m) offset by other net cash outflows of £9m.

3.28.3 The Fund actuary values the fund every three years and a full valuation was carried out during 2016/17 on the position at 31st March 2016. The actuary found a solvency level of 91%, an increase of 9% compared to the position at the 31st March 2013. The most recent full valuation (as at 31st March 2019) was reported to Pensions Investment Sub-Committee on 30th January 2020 and to this Committee on 11th February 2020. This has determined an overall funding level of 110% and set employer contribution rates for the three years 2020/21, 2021/22 and 2022/23. Although an overall surplus is identified there remain individual employers in the fund for whom a past deficit still exists. Where a past deficit exists for individual employers a recovery period of 12 years has been assumed. The Actuarial report refers to 'on the basis that there is still an investment risk and uncertainties around the McCloud judgement we have assumed that the surplus will be retained to act as a margin against the investment risk and other potential adverse experience over 2020/23'.

3.28.4 The Accounts also include disclosures in relation to the Bromley part of the Fund, which are based on the assumptions used in the 2016 valuation. Note 44 explains the IAS19 valuation basis used to prepare the Authority's accounts, which uses different assumptions from those used in the triennial valuation.

3.29 Annual Governance Statement (AGS)

3.29.1 The Council has a responsibility for conducting, at least annually, a review of the effectiveness of the system of internal control. Regulation 6 (2) of the Regulations requires that the AGS should be considered and approved by a Committee or Full Council. The statement must accompany the Statement of Accounts.

3.29.2 A draft AGS was approved by Audit Sub Committee on 4th June 2019. There has been one change relating issues identified on the valuation of fixed assets and this has been added as a governance issue. An updated AGS was circulated to Members of Audit Sub-Committee and was approved by this Committee on 28th November 2019. No further changes have been made and this Committee is requested to formally approve the audited AGS (see Appendix 1) which will be published alongside the Statement of Accounts.

4. FINANCIAL IMPLICATIONS

- 4.1 The final revenue and capital outturns for 2018/19 were reported to the Executive on 21st May 2019. Members are referred to these reports for detailed information on variations from approved budgets.
- 4.2 In line with accounting Regulations, changes arising from the revised asset valuations have been posted through revenue accounts and reversed through the Movement in Reserves Statement (MIRS) into unusable capital reserves (revaluation reserve and capital adjustment account).
- 4.3 The Council is seeking to recover the additional costs incurred in undertaking the revaluations and amending the accounts. The outcome of this process will be reported to Members in due course.
- 4.4 Information in relation to the external audit fees is set out on page 42 of Appendix 2. Whilst the planned fee is £91,689, a further amount will be payable due to the additional audit work required work on asset revaluations and required restatements relating to the McCloud judgement. The final fee is subject to discussions between officers and EY. Additionally, is not yet possible to provide an accurate estimate for the fees relating to objections to the 2016/17, 2017/18 and 2018/19 accounts.
- 4.5 This report refers to matters reflected in the auditor's report. There are no adjustments to the accounts that have an impact on the Council's revenue outturn position and general fund balance for 2018/19. Accordingly, there is no impact on the level of reserves previously reported to the Executive in the Provisional Final Accounts report on 21st May 2019.

5. LEGAL IMPLICATIONS

- 5.1 The Accounts and Audit Regulations 2015 require the Statement of Accounts to be signed and dated by the responsible financial officer by 31st May immediately following the end of the financial year and subsequently to be considered and approved by a Committee of the Council, or by the Council meeting as a whole, before 31st July. The responsible financial officer must firstly re-confirm that the accounts present a true and fair view of the financial position of the authority at the end of the financial year to which it relates and the authority's income and expenditure for that financial year. Regulation 10(1) requires the publication of the accounts and other prescribed information.
- 5.2 Regulation 10(2) sets out the provisions that apply where an audit of accounts has not been concluded before 31st July in that the authority must publish a notice stating that it has not been able to publish the Statement of Accounts and its reasons for this under Regulation 10(2)(a). Regulation 10(2)(b) requires compliance with Regulation 10(1) but substitutes the date of 31st July with a requirement to publish "as soon as reasonably practicable after the receipt of any report from the auditor which contains the auditor's final findings from the audit which is issued before the conclusion of the audit".

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| Non-Applicable Sections: | Impact on Vulnerable Adults and Children Policy, Personnel, Procurement Implications. |
| Background Documents: (Access via Contact Officer) | Provisional Final Accounts – Executive 21 st May 2019; Capital Programme Outturn – Executive 21 st May 2019; Code of Practice on Local Authority Accounting in the United Kingdom 2018/19; Service Reporting Code of Practice 2018/19; The Accounts and Audit Regulations 2015; Final accounts supporting papers are held by the Technical and Control (Accountancy) Team. |