EY Audit Briefing Paper

Audit & Risk Committee Meeting 2 November 2022

Background and Purpose

This paper updates the Committee on the current status of the audits of London Borough of Bromley and London Borough of Bromley Pensions Fund for 2019/20.

As part of our previous reporting we made a number of recommendations on the actions the Council needed to take to:

- Ensure that the 2019/20 audits can be completed in a timely manner; and
- Facilitate a smoother completion of the subsequent audits.

We worked with the Council to agree a plan to implement those recommendations. However, we remain concerned that the Council is still struggling to support the completion of the audit and we therefore set out below the options available to us, under the Local Audit and Accountability Act 2014 (Schedule 7), to bring those matters to the attention of the full Council and to require action in response from the Council, if the recommendations below are not actioned on a timely basis. Were we to report to Council under Schedule 7, a copy of our report would also be sent to the Secretary of State.

2019/20 Audit

During the audit we identified significant delays in resolving our audit queries. In addition, we have also seen a high turnover of key staff contacts. Recently we have seen more stability in key posts though we still remain concerned regarding the overall capacity of key staff.

The final substantive issues to be resolved on the audit are:

1) Property, Plant and Equipment (PPE);
2) Infrastructure Assets;
3) Prior Year Objections;
4) Pension Fund Audit; and
5) Going Concern.

1 – Property Plant and Equipment

The key issues in relation to PPE including details of where we have encountered and some of the reasons for those delays are set out below:

- We identified issues with the property valuations methodology applied by the external valuer, Montague Evans;
- All investment properties with the exception of one asset required revised revaluations to be completed by the external valuer;
- Car Park valuations required revised revaluations after we raised concerns regarding the approach being adopted by the external valuer. We worked with the external valuer to agree a revised approach to the valuation of car parks. That process and the subsequent time required to audit the revised valuations has added significant time to the audit;

- We identified errors in the approach to depreciation in respect of assets revalued in-year. This error is being corrected through a Prior Period Adjustment (PPA);
- We identified issues with the Council's assessment of Furniture and Fittings (F&F). The Council were assessing the value of F&F using an arbitrary percentage which, when challenged, could not be appropriately supported with documentation. This error is also being corrected through a PPA;
- We also experienced initial delays in the timeliness of responses from Council officers though a number of those individuals are no longer employed by the Council;
- We identified completeness and accuracy issues in respect of the responses received from the external valuer. In addition, we experienced delays in receiving responses. Since we previously reported this matter in November 2021 we have seen a significant increase in engagement and timeliness of responses. This has been facilitated through weekly meetings specifically on PPE chaired by the Director of Finance. These meetings are attended by key internal staff, external audit and also by the external valuer and have facilitated resolution of, and clarity, around key matters to be resolved in respect of PPE;
- As at the date of this report officers have started working on making the necessary adjustments to PPE and have indicated an 8 week turnaround. This seems an excessive amount of time and would seem to support our conclusions regarding capacity.

2 – Infrastructure Assets

During 2022 a national technical issue was raised in respect of the accounting treatment of Infrastructure Assets. The matter was escalated through CIPFA and below we set out the details of the matter and also the latest position with regards to a potential resolution of the matter.

- An issue was raised via the NAO's Local Government Technical Group as to whether local authorities should be assessing if there is any undepreciated cost remaining in the balance sheet for replaced components that need to be de-recognised when the subsequent expenditure is added. It was also determined that this may in turn lead to issues related to the reporting of gross historical cost and accumulated depreciation as elements of depreciated historical cost. This is a national issue impacting the majority of clients holding material infrastructure assets;
- CIPFA published in May 2022 its 'Temporary Proposals for the Update of the Code of Local Authority Accounting in the UK' on Infrastructure Assets. Following the CIPFA consultation, it was indicated that there may be enhance guidance, or amendments to the CIPFA Code;
- Asset registers do not tend to record Infrastructure Assets with sufficient detail to enable identification of prior cost of replaced parts/components and related accumulated depreciation. This was the case at London Borough of Bromley. Given the challenges raised as a result of the level of information available, it is not possible to identify the cost and accumulated depreciation balances that need to be de-recognised. The issues in respect of the CIPFA Code of Practice affects additions to Infrastructure Assets from 2010/11 when IFRS Accounting was adopted by the CIPFA Code of Practice;
- Infrastructure Assets have a Gross Book Value of £166 million as at 31/3/20 at Bromley and are therefore highly material;
- Officers informed us in September 2022 that the Council would not accept a Limitation of Scope qualification in respect of Infrastructure Assets on the 2019/20 Accounts. Instead, they have decided to wait for a potential statutory override which would need statutory approval before a revised and updated Code of Practice would be available. This position reflects that taken by the majority of EY audit clients on this matter;
- It is anticipated that the timetable for this legislation may now be in December 2022 which means officers will then need some time to implement the new Code and make the necessary adjustments to the accounts, which will then need to be audited.

3 – Prior Years and Matters of Objection

- Due to outstanding objections on the 2016/17 and 2017/18 audits we have previously been unable to issue our audit completion certificate for the prior year 2018/19. We have been in regular communication with the predecessor auditor in respect of this matter and they have now completed their review of the matters of objection previously reported to them. The objections raised to the predecessor auditor were in respect of 2016/17 and 2017/18. Their conclusions on the matter have now been formally reported to London Borough of Bromley. To support our assessment of the matter the predecessor auditor has shared key legal assessments supporting their assessment and we have also seen their final determination letter on the matter;
- In addition to the objections raised to the predecessor auditor we also had a matter of objection raised with us as part of the 2018/19 audit. As a number of the matters raised to us as part of the 2018/19 audit showed some consistency with matters previously raised, we have reviewed the matter in conjunction with the information shared to us by the predecessor auditor to avoid duplication of audit effort. We have performed our initial review of the matter and we have raised a number of questions with officers. We have now received responses to the questions raised and are currently working through these.

4 – Pension Fund

- We encountered significant delays throughout the audit in responding to our audit queries. The audit work is now complete with the last substantive outstanding items being the work required to update our Going Concern assessment and perform a review of subsequent events.

5 – Going Concern

- We had completed an initial assessment of Going Concern however due to the delays with the main audit we have been unable to complete our Going Concern assessment as this needs to include a forward assessment for a period of at least 12 months from the date of the audit opinion. We will therefore need to update our Going Concern assessment at the conclusion of the main audit and therefore this will be completed as soon as the outstanding items listed above have been resolved.

Recommendations

We reported in June 2021 that we expected to be reporting the conclusion and outcome of the 2019/20 audit by September 2021. However, due to the delays and issues above, the audit is not yet complete.

In order to conclude the audit and to prepare for and support the audits of the 2020/2021 and 2021/2022 accounts, we reiterate our recommendations made in November 2021, which the Council need to action to avoid us issuing Statutory Recommendations:

2019/20

1. Set out a clear timetable of when queries will be responded to and meet these deadlines. Put in place effective escalation procedures that hold officers to account for their areas of responsibility.

2. Ensure that sufficient priority is given to responding to audit queries, and that sufficient resource is available within the finance function to provide capacity to undertake audit support and “business as usual” such as budget preparation, management accounting and reporting.

2020/21 and beyond

1. Set out a clear plan of how the Council plans to address the backlog of work, including a resourcing plan and task allocation plan;

2. Ensure that the Council has a clear timetable for closing down 2020/21 and preparing the draft financial statements;

3. Develop a sustainable resourcing strategy, with appropriate skills and capacity, to address future reporting requirements such as changing business (e.g. Group reporting); and also technical reporting requirements (e.g. changes to CIPFA Codes).

Potential to issue a Schedule 7 report - Local Audit and Accountability Act of 2014

A Schedule 7 Report is where the auditor may make recommendations about actions that the auditor thinks the body should take in response to the findings of an audit.

Statutory recommendations made under a Schedule 7 must be considered by the body and responded to publicly. They can direct the body to specific shortcomings or failures, or assist in monitoring the body's progress on specific issues. The auditor must also copy a Schedule 7 to the Secretary of State.

If we decide to report under Schedule 7, our recommendations would highlight the investment required by the Council to support its financial reporting to close out the 2019/20 audit, prepare the 2020/21 accounts and support that audit, and prepare the 2021/22 accounts and support that audit, in order to address the reporting backlog by the end of 2022. We would also highlight the need for a clear timetable, accountability and consequences (e.g. performance management, escalation to Audit & Risk Committee, further auditor reporting etc) to complete the work.

Conclusion

Following our earlier reporting on the matters above we have seen some improvement in engagement and escalation at senior executive level with weekly meetings in place to facilitate quicker resolution of outstanding audit queries and we have also seen a separate specific meeting put in place and chaired by the Director of Finance to discuss specific PPE topics. In addition, we have seen the Council strengthen capacity within the finance team following our initial concerns around capacity. We have also seen greater stability in the finance team since these additional posts were created. However, we still remain concerned that the Council will be unable to address all of the issues raised above and maintain their level of response to service the future audits and recover from the backlog. We would encourage members to seek assurances from officers that the Council has a sufficiently robust timetable and plan in place to mitigate the above. Without the relevant assurances regarding a forward robust plan, a detailed timetable and a commitment to maintaining the additional capacity within the finance team we will consider issuing the Statutory recommendations detailed above.