Middlesbrough
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Legal and Governance

CORPORATE AFFAIRS AND AUDIT COMMITTEE

Date: **Monday 5th December, 2022**
Time: **3.30 pm**
Venue: **Mandela Room**

AGENDA

1.	Welcome and Evacuation Procedure	
2.	Apologies for Absence	
3.	Declarations of Interest To receive any declarations of interest.	
4.	Minutes - Corporate Affairs and Audit Committee - 23 and 29 September 2022	3 - 14
5.	Teesside Pension Fund Audit Results report 2020/21 Verbal Update	
6.	External Audit - Value for Money Governance Update	15 - 30
7.	Annual Governance Statement 2021/22	31 - 62
8.	Council Audit Planning Report 2021/22	63 - 106
9.	Teesside Pension Fund Planning Report 2021/22	107 - 144
10.	Internal Audit and Counter Fraud Progress Report 2022/23	145 - 172

11. Capital Strategy 2022/23 - Mid Year Update 173 - 202

12. Any other urgent items which in the opinion of the Chair, may be considered

Charlotte Benjamin
Director of Legal and Governance Services

Town Hall
Middlesbrough
Friday 25 November 2022

MEMBERSHIP

Councillors B Hubbard (Chair), J Platt (Vice-Chair), T Higgins, C Hobson, T Mawston, D Rooney and C Wright

Assistance in accessing information

Should you have any queries on accessing the Agenda and associated information please contact Susan Lightwing, 01642 729712, susan_lightwing@middlesbrough.gov.uk

CORPORATE AFFAIRS AND AUDIT COMMITTEE

A meeting of the Corporate Affairs and Audit Committee was held on Friday 23 September 2022.

PRESENT: Councillors B Hubbard (Chair), T Higgins, T Mawston, M Saunders (substitute for J Platt) and M Storey (substitute for D Rooney)

ALSO IN ATTENDANCE: Councillors D Coupe (Executive Member for Adult Health and Public Protection and Digital inclusion) and J Thompson
M Rutter, EY

OFFICERS: C Benjamin, G Cooper, S Lightwing, S Gilmore, R Horniman, A Hoy, A Johnstone, S Lightwing and J Weston

APOLOGIES FOR ABSENCE: were submitted on behalf of Councillors J Platt, C Hobson, D Rooney and C Wright

22/19 WELCOME AND EVACUATION PROCEDURE

The Chair welcomed all present to the meeting and read out the Building Evacuation Procedure.

22/20 DECLARATIONS OF INTEREST

Name of Member	Type of Interest	Item/Nature of Interest
Councillor Higgins	Non pecuniary	Member of Teesside Pension Fund
Councillor Hubbard	Non pecuniary	Member of Teesside Pension Fund

22/21 MINUTES - CORPORATE AFFAIRS AND AUDIT COMMITTEE - 22 JULY 2022

The minutes of the Corporate Affairs meeting held on 22 July 2022 were submitted and approved as a correct record.

22/22 ANNUAL GOVERNANCE STATEMENT 2020/2021

A joint report of the Chief Executive, Director of Legal and Governance Services and the Director of Finance was presented. The purpose of the report was to present the finalised Annual Governance Statement (AGS) 2020/21 which had been agreed by the Mayor, Chief Executive and Section 151 Officer. A copy of the AGS was included in the submitted report.

As set out to the Committee in July 2022, the Council's Auditor, EY, identified serious and pervasive governance and culture concerns with the operation of the Council, in their Value for Money judgement. As a result of work required to ensure the scale and seriousness of that challenge were accurately reflected within the AGS, it was not able to be finalised in July when the audited Statement of Accounts 2020/21 were submitted for decision at Committee.

The Mayor, Chief Executive and the Section 151 Officer had worked together, alongside other senior members and the Monitoring Officer to agree the AGS. It was explained that the Chief Executive's previous concern was that the AGS did not fully articulate the risks that were associated with the current position. Extensive discussions had taken place to ensure that the wording accurately reflected the scale of the situation and the challenge that existed.

A Member highlighted that the AGS had been signed on 6 September 2022 and raised concerns regarding a motion passed at a Council meeting held on 7 September 2022 in relation to a Standards Committee recommendation. It was confirmed that when the Audit Opinion was signed by the External Auditor, and the Audit was closed, the AGS would need to be resigned. Therefore there would be an opportunity for additional information to be added or reflected in the AGS, if appropriate.

In relation to the implementation of actions from the 2019/2020 AGS, the action to implement a case management tool for those Councillors who wished to use it was marked as completed. It was noted that following completion of training on the new tool, no Councillor was willing to progress and therefore a new system was not introduced and the action was marked as completed. It was suggested that this action should be revisited and an Officer confirmed that it could be brought forward in the 2021/2022 AGS. It was also anticipated that CIPFA might do this also.

A query was also raised in relation to an action to establish an approach to reviewing delivery models to identify changes required to delivery models. The Officer stated that this was in relation to operational models and agreed to forward further clarification via email following the meeting.

It was highlighted that as a result of the issues identified within the AGS and the range and varied nature of them, the Council would launch a Corporate Governance Improvement Plan (CGIP). The CGIP would be overseen by a multi-disciplinary Officer Board using the Council's Project Management Framework, with robust scrutiny of action delivery and reporting to Corporate Affairs and Audit Committee, Overview and Scrutiny Board and Executive on a regular basis to demonstrate delivery of actions and also to assess the impact of those actions. This would provide assurance to Members on action being taken and ensure that if control weaknesses continued to exist even after action, further actions could be identified to address those. It would also include engagement with Internal and External Audit to provide assurance around delivery. It was suggested that the milestones, timescales, actions and outcomes needed to be included in detail. An Officer commented that this would be developed with Members.

AGREED that the Corporate Affairs and Audit Committee noted that the Annual Governance Statement 2020/2021 had been finalised and agreed by the Mayor, Chief Executive and the Section 151 Officer.

22/23 SUSPENSION OF COUNCIL PROCEDURE RULE NO. 5 - ORDER OF BUSINESS

In accordance with Council Procedure Rule No. 5, the Committee agreed to vary the order of business to deal with the items in the following order: Agenda Item 8, Agenda Item 6, Agenda Item 7, and Agenda Item 9.

22/24 MAYORAL DEVELOPMENT CORPORATION (MDC)

A report of the Director of Regeneration was presented to provide the Committee with an overview of the governance process for the proposed Mayoral Development Corporation and the next steps in the process.

The Tees Valley Mayor and Middlesbrough Mayor had announced an ambition for a Mayoral Development Corporation (MDC). The aim of a MDC was to accelerate major regeneration initiatives, in a defined area/scope, by dedicating specialist capacity, securing additional investment and streamlining processes.

The establishment of a Mayoral Development Corporation was a power available to devolved, city-region authorities under the Localism Act 2011, albeit a case must be made to the relevant Secretary of State and formal approval must be granted.

To commence the process for a Mayoral Development Corporation was a unilateral decision available to the Tees Valley Mayor - Members of Middlesbrough Council were not able to determine whether a MDC could be established or not. However, as the Host Authority, Middlesbrough Council was a principal statutory stakeholder and would have great influence on how the MDC's Constitution was shaped and to what extent any assets could be pooled/transferred.

The initial stages of the process to create a Mayoral Development Corporation had commenced but this amounted to an initial expression of interest/formal letter to the Secretary of State, to commence the process. This was informed by a provisional consultation held over June/July 2022. This only established the ambition to establish an MDC and the proposed area (red line boundary) within which the MDC's powers/influence would apply.

Upon receipt of the request, the Secretary of State would commence a detailed statutory consultation exercise to involve major stakeholders. Middlesbrough Council, as host authority, would be the principal statutory consultee in this exercise. This would provide the opportunity to express any governance, democratic, accountability and financial concerns to inform the establishment of an agreed Constitution for any MDC structure.

The process would involve detailed discussion and engagement with Elected Members. It was important to stress that the process was in the very early stages and many of the logistical factors and required financial appraisals could only be detailed once the scope of the Secretary of State's consultation was known. This was not to obfuscate the process, or material concerns of Elected Members, rather it was recognition that this was the start of a collaborative process and any potential impacts could only be assessed as details of any framework, came forward.

Middlesbrough Council's initial thinking was based on the fundamental requirements that:

a) should any financial assets be proposed to be pooled within an MDC, this could not prejudice Middlesbrough Council's financial position and would need to be protected/compensated accordingly.

b) the Constitution of the MDC and any proposed transfer of powers, should properly reflect/protect the democratic mandate of Middlesbrough's Elected Members and the primacy of local powers, strategic objectives and adopted plans.

Details of specific proposals, development sites, investments were not known in any detail at this stage. When specifics were known, each factor would be assessed for implications and offered for Member consideration. This was likely to inform the conditions, protections, and covenants which the Council would highlight as a response to the next stage (Secretary of State – Statutory Consultation). However, some frequently asked questions and responses were included at paragraphs 11 to 20 of the submitted report.

A Member raised concern in relation to the removal of planning powers from the Council. Reference was also made to information obtained through Freedom of Information requests (FOIs) in relation to planning and the benefits of having an MDC. The Officer explained that whilst the MDC could take control of planning powers, it could also delegate back to the Local Authority, as many of those powers as it wanted to. However, it was emphasised that as there was no proposal as yet, the implications were not clear. Officers had been informed however, that the MDC would be bound by the same planning legislation as the Council. Whilst the Officer could not comment on the FOIs, it was clarified that the Council had not agreed to transfer any assets at this point in time. An MDC would enable the Council to conclude deals and investments that it did not have the financial capacity to deliver.

It was highlighted that Middlesbrough Council had a good working relationship with the Tees Valley Combined Authority (TVCA) which had enabled several economic development priorities, such as Tees Advanced Manufacturing Park (TAMP), the dock bridge, Boho and Centre Square to be completed, without the need for an MDC. The Officer explained that the Council was probably close to exhausting opportunities to be able to develop such projects as finances were now much tighter.

With regard to any possible financial detriment to the Council, the issue of business rates income was raised. Currently, the Government received 50% and Middlesbrough Council received 50% of business rates income. However, under the MDC, the Government's 50% could potentially be reinvested locally so the Council would ultimately benefit. Negotiations around asset transfer would be complex and as yet there was no clarity.

Concern was also raised regarding accountability and ensuring that local people were represented on the MDC Board. The Officers agreed that this issue had been articulated by Elected Members in several different forums and had been noted. This point would be raised as part of the consultation feedback.

The Chair thanked the Officers for attending and for sharing the information available at the current time.

AGREED that the information provided was received and noted.

22/25 HIGHWAYS INFRASTRUCTURE ASSETS - UPDATE

A report of the Director of Finance was presented, the purpose of which was to update Members on the Highways Infrastructure Assets position for 2020/21 following the Chartered Institute of Public Finance and Accountancy's review on this subject earlier in the year.

A way forward on this issue, which was acceptable to both the Council and to the external auditors, would allow EY to issue their opinion on the financial statements and to close the audit process for that financial year. This would be useful given the length of the current audit and the need to move on with the audit of the 2021/22 accounts for the Council which had been prepared.

At a meeting on 22 July, the Committee approved the audited statement of accounts subject to; the annual governance statement being finalised and agreed by the Mayor, the Chief Executive and the Director of Finance, and the Highways Infrastructure Assets issue, which had been raised during the audit being resolved. A signed annual governance statement for 2020/21 was included within the agenda papers for this meeting. In order for EY to issue their audit opinion for the financial year, a resolution on the position on highways assets was required.

It was explained that in an audit, a limitation of scope was a situation where auditors could not obtain sufficient appropriate evidence to make a conclusion on certain account balances, transactions or events. This was the position with highways assets where local authorities held some data but the accounting records did not generally record and adjust for de-recognitions (or disposals) in sufficient detail. The normal approach to this was for the auditors to modify their opinion on the financial statements as a result.

The limitation of scope approach would allow the audit process for 2020/21 to be completed with a view from EY that the financial statements give a true and fair view in all regards and for all key balances, except for Highways Infrastructure Assets. This would allow the Council to publish their audited Statement of Accounts for 2020/21 and EY to move on with their audit of the 2021/22 accounts.

Although Middlesbrough's highways service maintained an information management system (Symology) and some of the information that was required for the accounting process was recorded within this system. Officers were not confident that this was sufficient to restate the balances needed back to 2011, when international financial reporting standards were first introduced. Although further work could be done to extract the information and to use local knowledge to fill in the gaps, this work could take several months. The current accountancy fixed asset register also did not provide the level of detail required in relation to new additions and derecognitions to be able to account for those assets in a reasonable way.

Officers were more confident that Symology could be used to capture the correct level of data going forwards and that this work could be linked with the Council's fixed asset register to produce the correct capital accounting entries going forwards.

As a result, the view of the Director of Finance (as responsible financial officer) was that the limitation of scope option to close the external audit for 2020/21 brought more benefits than disadvantages and that the Council should pursue this option with EY. It was also sensible given the circumstances, as it allowed the maximum certainty on the Council's financial position and to stakeholders.

The External Auditor confirmed that EY were supportive of the limitation of scope approach and commented that the Government and CIPFA were taking forward an action plan to amend the Code and the legislation to remove some of the disclosure requirements.

The Council finance team would continue to work with the Highways Service to see what information was needed/available to resolve this issue, both retrospectively and going forward. Officers would monitor the position on future CIPFA guidance and changes to the accounting code of practice and update the Committee on an interim basis.

AGREED as follows that:
1. the contents of the report and the position on the audit process for 2020/21 were noted.
2. the Committee concurred with the Director of Finance's advice to accept a limitation of

scope option in relation to Highways Infrastructure assets for the year in question.

22/26 TEESSIDE PENSION FUND PROVISIONAL AUDIT RESULTS REPORT - YEAR ENDED 31 MARCH 2021

The External Auditor presented a report which summarised EY's preliminary audit conclusion in relation to the audit of Teesside Pension Fund for 2020/21.

EY's audit of Teesside Pension Fund ('the Fund') for the year ended 31 March 2021 was nearing completion. Subject to concluding the outstanding matters listed in the report, the External Auditor confirmed that EY expected to issue an unqualified audit opinion on the financial statements.

In the Audit Committee Planning Report, EY communicated that the audit procedures would be performed using a materiality of £34.2m and the threshold for reporting misstatements would be £2.3m. At year end EY updated this assessment and confirmed that these levels remained appropriate.

The Audit Plan identified a number of key areas of focus for the audit of the financial report of Teesside Pension Fund and the report set out EY's observations in relation to these areas, including views on areas which might be conservative and areas where there was potential risk and exposure. Consideration of these matters and others identified during the period were summarised within the Areas of Audit Focus section of the report.

The External Auditor drew attention to following:

- Misstatements due to fraud or error – no misstatements were identified.

- Valuation of unquoted pooled investment vehicles - included within the initial draft accounts presented to EY for audit was the quarter three valuations rolled forward to produce a year end valuation. Upon receipt of the year end confirmations it was apparent that the valuations were higher than the amounts included in the accounts, which resulted in a net understatement of investments by £26.4m. Management chose not to adjust for this valuation movement due to it being immaterial. No further misstatements were identified.

- Valuation of directly held property – EY's Real Estate Team reviewed a sample of properties and concluded that all valuations were within an acceptable range. No misstatements were identified.

A number of audit differences had been adjusted for by management. Details of these are included in Section 4 of the report.

There was one audit difference which was unadjusted. EY identified a total net understatement of investments by £26.4m. This was primarily due to timing differences - the valuation reports used by the Pension Fund when preparing the accounts contained reports as at December 2021, whereas the year end valuation provided by Fund Managers as part of the confirmations process were as at March 2021. Management chose not to adjust for this error due to it being immaterial.

The 2021/2022 audit work was almost completed and a matter around recording of income had been identified. This had the potential to reach back into 2020/2021 and management were looking into this issue as a priority.

The External Auditor was required to review the Pension Fund Annual Report and issue an opinion on the consistency of the report with the audited Pension Fund financial statements included within the Middlesbrough Council Statement of Accounts. EY had identified some consistency issues within the Annual Report which management were going to adjust for. Once the updates had been made EY would be in a position to issue their consistency opinion.

The External Auditor extended EY's thanks to the Officers for their assistance with the Audit.

It was highlighted that the latest valuation of the Fund was £5.1 billion.

AGREED that the Teesside Pension Fund Provisional Audit Results Report - Year ended 31 March 2021 was received and noted.

22/27 **ANY OTHER URGENT ITEMS WHICH IN THE OPINION OF THE CHAIR, MAY BE CONSIDERED**

None.

CORPORATE AFFAIRS AND AUDIT COMMITTEE

A meeting of the Corporate Affairs and Audit Committee was held on Thursday 29 September 2022.

PRESENT:	Councillors B Hubbard (Chair), J Platt (Vice-Chair) and T Higgins
ALSO IN ATTENDANCE:	P Jeffrey (Internal Auditor) (Veritau) and J Dodsworth (Veritau)
OFFICERS:	S Lightwing, C Benjamin, G Cooper, A Johnstone, C Walker, J Weston and M Rutter
APOLOGIES FOR ABSENCE:	Councillors C Hobson, T Mawston, D Rooney and C Wright

22/27 WELCOME AND EVACUATION PROCEDURE

The Chair welcomed all present to the meeting and read out the Building Evacuation Procedure.

22/28 DECLARATIONS OF INTEREST

There were no declarations of interest received at this point in the meeting.

22/29 PROCUREMENT OVERVIEW 2021/2022

A report of the Director of Finance was presented to provide the Corporate Affairs and Audit Committee with the annual overview of procurement activity undertaken for the financial year 2021/2022.

The Council had Contract Procedure Rules in place as part of the Council’s Constitution and these provided the governance in respect of procurement practices.

Public Procurement Notice (PNN) 10/21 – Threshold & Inclusion of VAT was published on 6 December 2021, which notified all Contracting Authorities of the uplift to thresholds and the inclusion of VAT on contract value from 1 January 2022. The inclusion of VAT is due to Brexit and aligned the UK to all non-members. The table at paragraph 5 of the submitted report showed the thresholds as at 1 April 2021 to 31 March 2022, which all procurement was required to adhere to.

During 1st April 2021 to 31st March 2022 the Procurement Team had been involved and supported service areas with 273 procurement activities that equated to a total of £62 million worth of contracts being awarded in the year. It was confirmed some contracts might be 1 to 2 years in length and others could be longer or have options for extension. A breakdown of activity was shown at paragraph 7 of the submitted report.

There were currently 467 active contracts recorded on the contract register, which was publically available. Work was being undertaken to ascertain how many of the contracts were with local suppliers and this information would be provided to the Committee when completed.

A report was presented to Corporate Affairs and Audit Committee on 9 June 2022, which provided a full overview of exemption activity for 2021/22 and a copy was attached to the submitted report at Appendix A for reference.

The Procurement Team continued to gate keep via Business World for any orders raised over £5k up to £100k which further strengthened understanding of the Council’s spend.

The Procurement Team supported service areas with procurement queries
and the Specialist Commissioning and Procurement Manager was currently working with the digital and organisational development colleagues in order to review and update the intranet and internet pages and develop some training for the Middlesbrough Learns site. It was anticipated that this work would be completed by the end of the year and with training going live from 1 April 2023.

During 2021/22 the Council spent £8,149,948 via purchasing cards which was 30,446 transactions. The majority of spend was low value with 19,785 (65%) being below £99, 9,875 (32%) was £100 to £1,000 and 787 (3%) was over £1,000. A review of purchasing cards' function in the Council would be undertaken led by the Specialist Commissioning and Procurement Manager.

Rebates for the cards were paid annually each year and were based on spend activity between 1 December to 30 November the previous year. In February 2022 the Council received a rebate of £60,651.27.

It was highlighted that the Council had employed an officer specifically to work on VAT and also stabilise the banking functions. Some more detailed work would take place around VAT over the next 3 to 6 months and this information would be provided to a future meeting of the Committee.

In line with the purchasing card policy staff were responsible for reviewing all spend on cards monthly, which included providing the receipt, detail of expenditure, cost centre and GL codes. Managers with staff who had cards were also responsible for monitoring spend and the team shared monthly reporting and management of cardholders in line with the Council's policies.

Executive approval was given on 7 September 2021 to award and implement the Supplier Incentive Programme (SIP) with Oxygen Finance calling off the North East Procurement Organisation (NEPO) Framework in order to pay suppliers as early as possible in return for a rebate payment.

The SIP programme has now been implemented following a mobilisation period that involved a number of stakeholders from across the Council, including the Finance Accounts Payable (AP) Team, Business World Support Team and the Procurement Team. Some internal practices had been identified that would be improved to ensure that the Council realised the benefits from SIP. In order to understand actions that could assist Middlesbrough, Officers had met with South Tyneside Council who had had SIP in place for nearly 7 years and were seeing rebates over £400k and aiming for this to grow further.

PowerBI was used to produce quarterly reports on local spend which had been really useful. Further work was needed in order to further increase reporting on spend and the Specialist Commissioning and Procurement Manager would be working with the data team over the next year to develop this. A summary of the percentage performance of local spend during 2021/22 was detailed at paragraph 31 of the submitted report.

AGREED that the information provided was received and noted.

22/30 ANNUAL ASSURANCE REPORT ON PARTNERSHIP GOVERNANCE

A report of the Director of Legal and Governance Services was presented to outline the Council's Partnership Governance Policy and set out information on the current levels of compliance with that policy.

The Partnership Governance Policy had been in place since it was approved by Executive in February 2020 and had not been reviewed until now. Lead Officers had completed a self-assessment for each of the 16 significant partnerships that existed during 2021/22 and the outcomes were shown at paragraph 7 of the submitted report.

While partnerships were assessed as being generally in a sound state by the Lead Officers who self-assessed compliance with governance standards, some marked performance as amber, where outcomes were less able to be articulated or because performance was below target or below national average. The position in relation to each of the partnerships identified as amber for performance and planned actions to address that status were set out in the submitted report at paragraph 8.

In relation to those partnerships that had previously had no Key Performance Indicators (KPIs) in place to measure delivery, it was clarified that these had been identified and added although it would take some time for them to embed.

A minimum standard was to be developed as part of the supporting policy. During 2022/23 this would be completed, and the next annual assessment would include an assessment against that, as well as an overall governance assessment of the health of partnerships.

As part of the completion of the annual assessment it was identified that there was a requirement to develop a complementary governance structure to assess wholly or partly owned Council companies that would provide a framework to consider:

- When a part or wholly owned company should be considered for establishment.
- The required content of any business case to establish one, for example: clear evidence that the required business to be conducted could not be completed as effectively within the Council.
- The minimum standard any company that is established should comply with for the purposes of demonstrating its effectiveness back to the Council.

During 2022/23 a governance framework and supporting minimum standard will be developed for the Executive's consideration. An action to deliver this had been included in the draft 2021/22 Annual Governance Statement.

AGREED as follows that the:
1. current position of the Council in relation to compliance with the Partnership Governance policy was noted.
2. planned inclusion of an assessment against the minimum standard for partnerships in the next annual assessment was noted.
3. planned actions to strengthen governance in relation to performance Management were noted.
4. proposal to create a governance framework to assess wholly and partly owned arm's length local authority companies was endorsed.

22/31 2021/2022 DRAFT STATEMENT OF ACCOUNTS

A report of the Director of Finance (Section 151 Officer) was presented for Members of the Corporate Affairs and Audit Committee to note and review the draft Statement of Accounts (SOA) for the 2021/22 financial year.

The report presented the draft SOA for the 2021/22 financial year, commented on the main movements in the organisation's financial position during the year and set out the legal processes that underpinned the SOA process and the responsibilities that needed to be undertaken.

This report was presented two months behind last year's draft SOA and four months later than in financial years pre-Covid-19. The Committee were aware of the reasons for delay on the audit process (from previous reports in 2019/20 and 2020/21).

The draft SOA was a highly technical and complex document and the main form of external financial reporting provided by local authorities. Its format and content was prescribed by the CIPFA Accounting Code of Practice with the aim of giving a high level of visibility and transparency over the Council's financial affairs.

The SOA comprised:

- A narrative report from the Director of Finance that provided an explanation on the financial position of the Council and described the key activities/highlights for the Council during the year. The report also contained performance-based information that illustrated what had been achieved by the use of these funds during the financial year.

- The Council's financial statements. These were the core elements of the SOA and included the movement in reserves statement, the income and expenditure statement, the balance sheet and the cash flow statement for 2021/22.

- Notes to the accounts which included detailed narrative and figures that supported the key totals within the financial statements and other issues that were of interest to local authority stakeholders.

- The Collection Fund, covering Council tax and business rates activities and the accounts of the Teesside Pension Fund for which Middlesbrough Council was the administering authority. For the first time this year, the Council had produced a set of group accounts (financial statements and notes) which consolidated the wholly owned subsidiary, Middlesbrough Development Company, into the Council's own accounts. This was due to the size of assets and liabilities associated with the company exceeding the Council's materiality threshold during the financial year.

- The Annual Governance Statement that set out how the Council had complied with best practice governance arrangements and any key issues that had arisen from it. Due to the governance issues identified by Ernst & Young (EY) during the audit of the 2020/21 accounts, this document was not finalised at present. It would be added into the draft SOA once the Statement had been considered by Members at a subsequent meeting.

The timetable for the approval of the SOA was set out at paragraph 13 of the submitted report and it was highlighted that the timescale for the audit and approval of accounts was outside of this statutory timeframe. This was not uncommon in recent years and a CIPFA survey showed that only 9% of local authorities had their 2020/2021 Accounts audited by the legal date of 30 September 2021. It was also highlighted that the target date of 2 March 2023 for the Committee's approval of the audited accounts was based on there being no significant delays or issues. The period available for inspection of the Accounts had been extended by one day due to the recent additional public holiday for Queen Elizabeth II's funeral.

The balance sheet for the Council had improved significantly during the financial year from a negative net worth of £44.9m to a positive position of £64.5m. An improvement of £109.4m. This predominantly related to the net pensions liability and the position in relation to International Accounting Standard (IAS) 19. Further analysis of this movement was contained within Note 39 to the accounts. This change was also reflected in the movement in reserves statement as part of unusable reserves and in the income and expenditure statement as an actuarial gain.

Members' attention was drawn to other areas of interest outside of the Core Financial Statements including:

- The narrative report.
- The going concern disclosures for the Council in Note 1 to the accounts.
- Note 7 on Earmarked Reserves.
- Note 12 on Grant Income.
- Note 14 on Officers' Remuneration.
- The various notes on non-current assets (notes 21-28).
- The various notes on Financial Instruments (notes 29-31).
- The new section on Group accounts.

A query was raised in relation to the increase in audit fees from 2021 to 2022. It was clarified that issues around Children's Services and governance had taken more audit time. It was also noted that the figures for both years were the Finance Team's assessments and not the actual fees. The External Auditor would report the final fees through the audit report once the audit was completed.

Discussion took place regarding the provision of additional training for Committee Members in relation to the Accounts which would provisionally take place before the December meeting.

AGREED that the draft Statement of Accounts for the 2021/22 financial year, published by the Director of Finance on 8 August 2022, representing a true and fair view of the Council's financial position as at 31 March 2022, was received and noted.

22/32 INTERNAL AUDIT AND COUNTER FRAUD PROGRESS REPORT

A report of the Head of Internal Audit, Veritau, was presented to provide Members with an update on progress with the delivery of internal audit and counter fraud work and on reports issued and other work completed since the last update report to the Corporate Affairs and Audit Committee.

A copy of the Internal Audit progress report was contained at Appendix 1 to the submitted report. It reported on progress against the internal audit work programme and included a summary of current work in progress, internal audit priorities for the year, completed work, and follow-up of previously agreed audit actions.

In relation audit reports with Priority 2 recommendations, the Chair highlighted the P2 definition which was: "A significant system weakness, whose impact or frequency presents risks to the system objectives, which needs to be addressed by management." Responding to a request, the Internal Auditor suggested that any Audits with Priority 2 recommendations could be added at Appendix 3 to the update report and provided to the Committee Members if required.

The Counter Fraud progress report was attached at Appendix 2 to the submitted report. It reported on progress against the counter fraud work programme. A range of work was detailed including activity to promote awareness of fraud, work with external agencies, and information on the level of fraud reported to date.

The Committee's attention was drawn to the following:

- The Counter Fraud Team raised awareness of whistleblowing on World Whistleblowers' Day in June. It was important that workers were aware that they should raise concerns that were in the public interest and that there were protections in place if they did so. It was equally important that managers responded to whistleblowing concerns in the correct way.

- Counter fraud training was delivered to the Council's finance team to address a form of cybercrime that had been increasing in terms of sophistication, frequency, and success over the past 12 months. This crime was mandate fraud, which was also known as payment diversion fraud. The training provided an update on the latest tactics and tools used by criminals to commit this type of fraud.

- The National Fraud Initiative (NFI) was a large-scale data matching exercise that involved all councils and other public sector bodies in the UK. The work of the NFI was overseen by the Cabinet Office. The 2020/21 exercise had now concluded and there was ongoing work in preparation for the 2022/23 exercise. Data would be securely gathered from council systems at the end of September, processed, and then securely sent to the NFI in October.

AGREED that the reports on progress of internal audit and counter fraud work in 2022/23 were received and noted.

22/33 COUNTER FRAUD FRAMEWORK REPORT

A report of the Head of Internal Audit, Veritau, was presented to update Members on the impact of fraud nationally and in particular on local authorities. The Council's Counter Fraud Policy Framework had been reviewed and the Counter Fraud Strategy Action Plan and the Fraud Risk Assessment had been updated for 2022/23.

The UK was currently experiencing a cost of living crisis and early indications were that fraud would rise and affect more local authorities. Cybercrime was 95% human error – so whilst robust procedures and processes might be in place, if systems were not followed fraud could occur. Internal Audit would continue to raise awareness and had set out objectives the action plan attached to the submitted report.

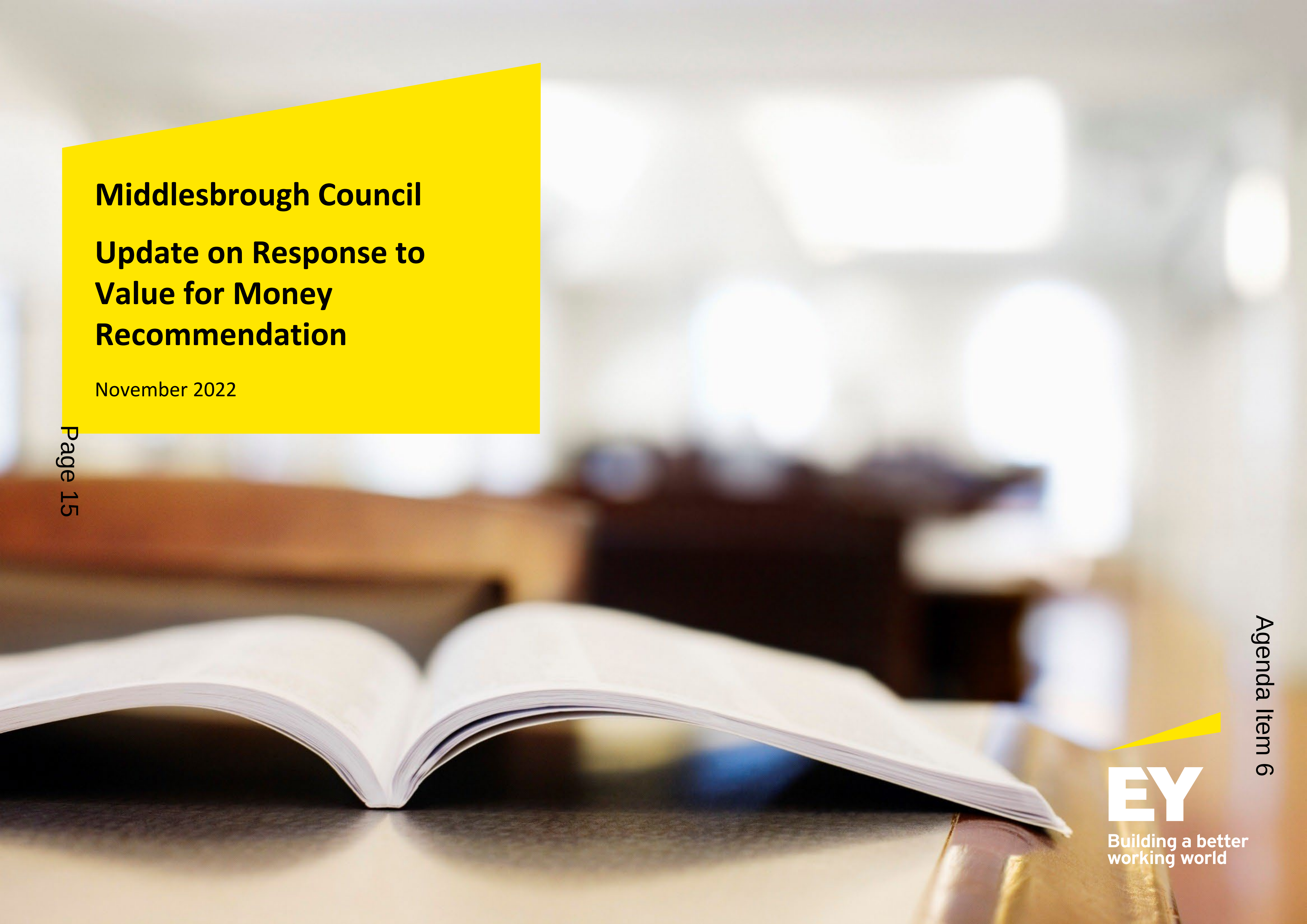
The review had identified that the Council's Anti-Fraud, Bribery, and Corruption Policy required updating to reflect changes in legislation. The Police, Crime, Sentencing and Courts Act 2022 had removed Councils' ability to offer simple cautions as an alternative to prosecution. A new process was proposed which could be used to offer offenders a formal written warning when it was not in the public interest to prosecute. The policy had also been revised to make it more readable and up to date.

AGREED that the updated Counter Fraud Strategy Action Plan, Fraud Risk Assessment and Anti-Fraud, Bribery, and Corruption Policy were received and noted.

22/34 **ANY OTHER URGENT ITEMS WHICH IN THE OPINION OF THE CHAIR, MAY BE CONSIDERED**

Teesside Pension Fund Provisional Audit Results Report – Year Ended 31 March 2021

At the Corporate Affairs and Audit Committee meeting held on 23 September 2022, the External Auditor had informed Members that the 2021/2022 audit work was almost completed and a matter around recording of income had been identified. This had the potential to reach back into 2020/2021 and management were looking into this issue as a priority. The External Auditor confirmed that this issue had now been resolved.



Middlesbrough Council

Update on Response to Value for Money Recommendation

November 2022

Building a better working world

Private and Confidential

November 2022

Corporate Affairs and Audit Committee
Middlesbrough Council
Civic Centre
Middlesbrough
TS1 9GA

Dear Corporate Affairs and Audit Committee Members

In our Draft Audit Results Report presented to the Corporate Affairs and Audit Committee in July 2022 we reported that we had observed evidence which led us to conclude that the culture and governance arrangements at the Council had not been operating as expected, and that this was undermining the effectiveness of the Council's governance framework.

At the same time, we made recommendations to the Council to address our observations and emphasised that the Council needed to address our primary recommendation as an immediate action. Within our value for money commentary, we highlighted that we would follow-up on the Council's response to this recommendation over the following six months. This report provides our assessment of the Council's initial response to our recommendation.

This report is intended solely for the use of the Corporate Affairs and Committee, other members of the Council, and senior management. It should not be used for any other purpose or given to any other party without obtaining our written consent.

We would like to thank your staff for their help during our work on this matter.

We welcome the opportunity to discuss the contents of this report with you at the next meeting of the Corporate Affairs and Audit Committee on 5 December 2022.

Yours faithfully

Stephen Reid

Partner

For and on behalf of Ernst & Young LLP

Value for Money

The Council's responsibilities for value for money

The Council is required to maintain an effective system of internal control that supports the achievement of its policies, aims and objectives while safeguarding and securing value for money from the public funds and other resources at its disposal.

As part of the material published with its financial statements, the Council is required to bring together commentary on its governance framework and how this has operated during the period in a governance statement. In preparing its governance statement, the Council tailors the content to reflect its own individual circumstances, consistent with the requirements set out in the CIPFA code of practice on local authority accounting. This includes a requirement to provide commentary on its arrangements for securing value for money from their use of resources.

Our observations

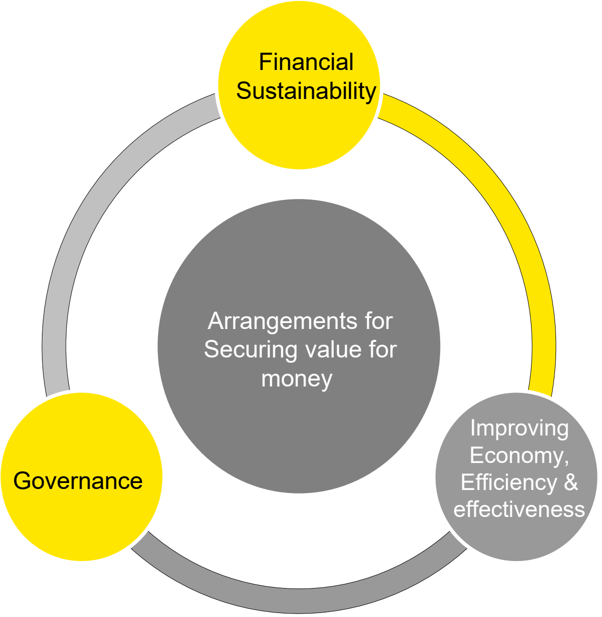
In our Draft Audit Results Report we reported that we had observed evidence which led us to conclude that the culture and governance arrangements at the Council had not been operating as expected, and that this was undermining the effectiveness of the Council's governance framework.

During the year ended 31 March 2021, we identified multiple instances where significant decisions were taken by the Council without following the Council's established policies and procedures and contrary to the boundaries of the respective roles and responsibilities of officers and members. These included, but were not limited to:

- Significant changes to the design of the Council's largest capital project, Boho X, occurring outside of the Council's Programme and Project Management Framework.
- Purchase of Covid-19 tests, which were not authorised for use in the United Kingdom, outside of the Council's normal procurement processes.
- Engagement of an external individual to provide mayoral assistance activities which are required by The Local Authorities (Elected Mayor and Mayor's Assistant) (England) Regulations 2002 to be performed by an employee of the Authority.

In addition, we reported our observation that there is a pervasive lack of trust within the Council between officers and elected members, and between elected members, which is having a significant impact on the governance of the Council and was a contributing factor to the respective roles and responsibilities of officers and members not being adhered to.

Further details of our observations were set out in our auditor's commentary on the Council's value for money arrangements, a copy of which may be found at Appendix A.



Financial Sustainability

Arrangements for Securing value for money

Governance

Improving Economy, Efficiency & effectiveness

Value for Money

Our recommendation and management's response

What was the recommendation?	What was management's response?	What was the timescale?
We recommend that the Council develop a comprehensive Improvement Plan to address the cultural and relationship issues which exist within the Council as a matter of urgency. In our view it is the responsibility of all elected members and officers to work together to address these serious matters. This will require the involvement of external specialists as, in our view, the relationships within the Council have deteriorated to a point which the Council will not be able to remedy on its own.	The Council has proposed, within the draft Annual Governance Statement, that a Corporate Governance Improvement journey is commenced. It is intended that this will be informed by the views of external specialists, CIPFA, who have been commissioned to undertake an independent diagnostic piece of work, engaging with all stakeholders over the summer. This will inform the proposed content of a Corporate Governance Improvement Plan which will be submitted to Full Council for consideration. In order for this to be successfully delivered, it will require full buy in from all stakeholders in this process. There is a significant risk that this action cannot be achieved if this is not gained. This is reflected within the Annual Governance Statement and has been highlighted to EY.	October 2022

Management's actions

Alongside our Draft Audit Results Report, the July 2022 meeting of the Corporate Affairs and Audit Committee was presented with a joint paper from the Council's Chief Executive, Section 151 Officer and Monitoring Officer entitled 'Commencing a Corporate Governance Improvement Journey' which sought endorsement from the committee to appoint the Chartered Institute of Public Finance and Accountancy (CIPFA) to undertake an initial diagnostic piece of work to better understand the cultural and governance issues which exist within the Council and propose further steps to address these. The committee provided the requested endorsement and the CIPFA review commenced in late July 2022.

Following interviews with over 40 individuals from across the Council, including members of the Executive, political group leaders and senior officers, and a review of other documentation, CIPFA issued the results of their review in September 2022. The review further highlighted the significance of the cultural and governance issues at the Council, concluding:

> *"It is clear from what we have seen that the issues facing the Council are significant. They are having a negative impact on the culture of the Council and, as identified by the External Auditor, affecting the Council's ability to deliver good governance. In the context of what will be a very difficult 2023/24 budget settlement, and a cost-of-living crisis that is affecting the lives of the citizens of Middlesbrough, the issues identified in this report have the potential to increase the risk that the Council will not be able to deliver its priorities.*
>
> *The Council has an opportunity to make considerable improvements, but not without acceptance that the issues contained in this report are real, serious and need resolution."*

Alongside their observations, CIPFA recommended the development of an action plan to address the issues raised and the use of cross-party working groups to involve members in this process. The CIPFA report and recommendations, alongside management's proposal for an Improvement Board to oversee the action plan was presented to, and approved by, a meeting of the full council in October 2022.

Value for Money

Management's actions (continued)

The Improvement Board will have an independent chair from the Local Government Association, and membership which includes the Council's Mayor, the Executive Member for Finance and Governance, the Chief Executive, the Monitoring Officer, political group leaders and a representative from CIPFA. It will be supported by four task and finish sub-groups focusing on roles and responsibilities within the Council, training and development, the Council's Constitution and the culture and communications within the Council.

The first meeting of the Improvement Board took place on 2 November 2022, at which the Board approved its terms of reference and an action plan based around 30-, 60- and 90- day milestones.

The Annual Governance Statement

Also alongside our Draft Audit Results Report and the 'Commencing a Corporate Governance Improvement Journey' management paper, the July 2022 meeting of the Corporate Affairs and Audit Committee received an update from the Council's Chief Executive and Section 151 Officer which articulated that, at that time, they did not feel able to sign the Council's Annual Governance Statement for the year ended 31 March 2021 on the grounds that the statement did not fully reflect the size and scale of the cultural change required at the Council.

An updated version of the Annual Governance Statement was produced in September 2022 which includes additional narrative highlighting further deterioration in relationships at the Council since 31 March 2021, concerns that that there is insufficient acceptance of the significance of the cultural issues at the Council and their impact on the Council's governance processes and, consequently, that there are significant risks to the Council being able to deliver the necessary improvement.

Similar concerns regarding the acceptance of the scale of issues at the Council and the Council's ability to deliver improvement have also been raised to us by multiple members of the Council.

Our assessment

The Council has taken positive actions to respond to our recommendation, including the commissioning of external work by CIPFA to assist in identifying the root causes of relationship issues at the Council and an action plan to address them, implementation of an Improvement Board with an external chair and strong representation from elected members and senior officers, and reporting of these actions through full council.

These steps are in-line with those we expected to see from the Council in responding to our recommendation and the future actions identified to date appear to be appropriate steps towards addressing both the depth and breadth of cultural and governance issues at the Council.

It is however clear that there is significant concern amongst a number of stakeholders over the ability of the Council to deliver on these actions, characterised by expressions of a lack of confidence in the acceptance by individuals of the significance of the governance issues identified at the Council and the commitment of all necessary stakeholders towards meaningful change. It will take all of the Council's elected members and senior officers working together to address the issues faced by the Council, however it remains unclear whether this can be achieved.

In addition, the Improvement Plan prepared by the Council focuses on actions to be completed over the next 90 days. Whilst these are positive first steps, the Council will not be able to enact the necessary cultural changes within the Council which are required within this timescale, and concerted effort over a much longer period of time will be required.

Value for Money

Our conclusion

It is clear that significant barriers to implementation of the Improvement Plan exist, however the actions taken to date have been appropriate and given sufficient prominence amongst elected members and senior officers. On this basis, we do not consider that it is either necessary or would be beneficial to escalate our recommendation through the exercise of additional auditor reporting powers (inc. a statutory recommendations) at this time. The Council is currently taking appropriate steps and should be given time to demonstrate whether those steps can have the necessary impact on the Council's culture and governance.

We will however continue to monitor the progress of the Council against the Improvement Plan as part of our value for money assessment, where we have recognised the Council's governance as a risk of significant weakness, and report on the Council's progress through our value for money commentary. Should this assessment provide evidence that the Council is not making satisfactory progress against the Improvement Plan or the actions taken are not having the necessary effect on the Council's culture, we will reconsider whether a statutory recommendation or exercise of other auditor reporting powers may be appropriate.

Commentary on value for money arrangements

We include below a copy of our commentary on the Council’s arrangements for securing value for money from its use of resources which was presented to the July 2022 meeting of the Corporate Affairs and Audit Committee within our Draft Audit Results Report.

Commentary of value for money arrangements

Scope and risks

We have complied with the NAO’s 2020 Code (2020 Code) and the NAO’s Auditor Guidance Notes in respect of VFM. We presented our VFM risk assessment to the 5 August 2021 Corporate Affairs and Audit Committee meeting which was based on a combination of our cumulative audit knowledge and experience, our review of minutes from the Council’s committees and Section 151 Officer and evaluation of associated documentation through our regular engagement with Council management and the finance team. We reported that we had identified one risk of significant weaknesses in the Council’s VFM arrangements for the year ended 31 March 2021.

Provision of Children’s Services

We qualified our VFM opinion for the year ended 31 March 2020 in respect of the Council’s provision of children’s social care services following an assessment by Ofsted in December 2019 that services were inadequate. Following the Ofsted inspection, the Council put in place an Improvement Plan and subsequent reports by the appointed Commissioner for Children’s Services in Middlesbrough and Ofsted supported that the Council has put in place appropriate governance structures to respond to the Ofsted findings.

Nevertheless, there remained a risk that the Council did not have proper arrangements in place to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people within its children’s social care services during the year ended 31 March 2021.

We responded to this risk by making enquiries of management to understand the progress being made against the Improvement Plan and reviewing the findings of subsequent external assessments of the Council’s Children’s Services as third party evidence of the progress being made by the Council. Based on the insight gained from these procedures, we formed an assessment of whether a significant weakness in the Council’s arrangements existed during the year to 31 March 2021. We concluded that no significant weakness existed. Further details of our assessment are provided within the ‘How the body evaluates the services it provides to assess performance and identify areas for improvement’ section below.

During the course of our audit, additional matters came to our attention which indicated a further risk of significant weaknesses in the Council’s VFM arrangements for the year ended 31 March 2021. We therefore recognised a further significant risk of significant weaknesses in the Council’s VFM arrangements for the year ended 31 March 2021.

Member and Senior Officer Relationships

During the course of our audit a number of matters were brought to our attention by management, internal audit, elected members and external parties which indicated potential weaknesses in the Council’s governance arrangements and its ability to ensure Council policies and procedures were adhered to. We noted that a common theme to the matters brought to our attention were observations and concerns about strained relationships between the Council’s senior officers and elected members, and between elected members, and the impact of those on the effectiveness of the Council’s governance processes. Based on identification of these matters and in accordance with the proper arrangements criteria set out in the 2020 Code, we recognised a risk that the Council did not “have proper arrangements in place to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people”.

We responded to this risk by following up on each of the individual matters brought to our attention through enquiries of management and the Council’s internal auditor, review of reports and other documentation, including reports commissioned by management to investigate the more serious concerns raised and consideration of the consistency of the information obtained in the course of these enquiries with other information obtained during the course of our audit. Based on the insight gained from these procedures, we formed our assessment of whether a significant weakness in the Council’s arrangements existed during the year to 31 March 2021. We concluded that significant weaknesses did exist, and provide further details of these in the sections below.

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

Reporting

We completed our VFM arrangements work in *[TBC]* and identified a significant weakness in the Council's VFM arrangements in relation to member and senior officer relationships and the impact of these on the Council's governance processes. We reported this matter by exception in the audit report on the financial statements and provided further details in the Audit Results Report. We include within the VFM commentary below the associated recommendation(s) we have agreed with the Council.

VFM Commentary

In accordance with the NAO's 2020 Code, we are required to report a commentary against three specified reporting criteria:

- Governance

  How the Council ensures that it makes informed decisions and properly manages its risks;

- Improving economy, efficiency and effectiveness

  How the Council uses information about its costs and performance to improve the way it manages and delivers its services; and

- Financial sustainability

  How the Council plans and manages its resources to ensure it can continue to deliver its services.

Introduction and Context

The 2020 Code confirms that the focus of our work should be on the arrangements that the audited body is expected to have in place, based on the relevant governance framework for the type of public sector body being audited, together with any other relevant guidance or requirements. Audited bodies are required to maintain a system of internal control that secures value for money from the funds available to them whilst supporting the achievement of their policies, aims and objectives. They are required to comment on the operation of their governance framework during the reporting period, including arrangements for securing value for money from their use of resources, in a governance statement.

We have previously reported the VFM work we have undertaken during the year including our risk assessment. The commentary below aims to provide a clear narrative that explains our judgements in relation to our findings and any associated local context.

For 2020/21, the significant impact that the Covid-19 pandemic had on the Council has shaped decisions made, how services have been delivered and financial plans have necessarily had to be reconsidered and revised.

We have reflected these national and local contexts in our VFM commentary.

Governance

How the body ensures it makes properly informed decisions, supported by appropriate evidence and allowing for challenge and transparency. This includes arrangements for effective challenge from those charged with governance/audit committee.

The Council has a number of Executive and other committees, operating at both Council-wide and service level, which are responsible for approving key decisions. Committee discussions are informed by a standard reporting template which sets out the background to the decision, available alternatives to the proposed decision, the advantages and disadvantages of available options and any financial or legal implications for the Council of the proposed action.

The Council also has an Overview and Scrutiny Board whose role is to scrutinise the performance of Council functions and the decisions taken by Executive committees. The Overview and Scrutiny Board is supported by 7 Scrutiny Panels and a joint committee with Redcar and Cleveland Council, with each able to refer decisions back to the Executive for further consideration.

The Corporate Affairs and Audit Committee receives reports on the Council's internal control environment from internal and external audit and monitors the implementation of recommendations to address identified weaknesses.

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

The Council's largest project during the year was the development of a specialist digital office space known as Boho X. The Council's Executive originally approved a 60,000 square foot design for this project in March 2019, before approving a revised 20-floor 100,000 square foot design in March 2020. Between March 2020 and August 2020, the design of Boho X changed again from the 100,000 square foot design to a revised 6-floor 60,000 square foot design. We have not sought to assess the merits of each Boho X design nor the strength of the evidence base informing them.

Under the Council's Constitution, elected members have no role in the delivery of projects, however changes in design were recorded by the external contractor as being approved by the Council's Mayor and followed meetings between the contractor and the Mayor which were held without Council officers being present. The changes in design were not submitted through the formal project change control process, as required by the Council's Programme and Project Management Framework (PPMF), and no meetings of the Internal Project Board were held during the period when changes occurred. The impact of the Covid-19 pandemic was cited by the Council as the reason for the change in design during public consultation and approval by the Executive of the revised design, however there is no documentation of the reasons for the change to support this assertion and the decision-making process remains unclear. Whilst the Council's Mayor understood that he had been authorised to discuss changes to the design with the external contractor by a senior officer, in our view the communication on which this was based did not explicitly provide such authority and such approval would in any event have been contrary to the Council's Constitution and the PPMF. It is therefore our assessment that there have been significant weaknesses in the Council's management of the Boho X project which undermine the Council's ability to demonstrate that the project represents value for money for taxpayers.

In addition to the changes in design for the Boho X project, we have identified several other transactions entered into by the Council during the year where Council policies and procedures were not followed and where a lack of adherence to the respective roles of officers and members was a key factor. These included the purchase of Covid-19 antibody tests which were not approved for use by the Medicines and Healthcare Products Regulatory Authority and therefore could not be used as the Council had intended, and the provision of political and administrative support to the Mayor by an outside party. In both cases, concerns about the proposed transactions were raised by senior officers prior to the transactions being entered into however both subsequently proceeded without following the Council's proper procurement processes. Whilst the monetary value of these transactions was not significant in the context of the financial statements, they demonstrate that the weaknesses identified in the Boho X project were not a one-off and that there are wider weaknesses in the Council's arrangements in particular where reliant on appropriate working between officers and elected members.

We have also noted multiple further examples of difficult relationships between officers and members, and between members, across a number of areas in the course of performing our audit work. As part of our reporting on the Council's audit for the year ended 31 March 2018, we reported that:

> *"We have observed that the relationship between some Councillors and senior officers is strained. This appears to be due to a mutual level of mistrust. Officers consider that the level of challenge provided by some Councillors is excessive. Officers have also noted that they are required to spend disproportionate amounts of time on issues that, in their opinion, have been previously addressed. We note that concerns about the style of communication between members and officers have also been expressed that have resulted in Standards Committee action.*
>
> *In contrast, some members consider that the information provided by officers, in relation to their challenge, is in some cases not adequate or is deliberately withheld, and as a result they are unable to make informed decisions. This has also led to members sharing concerns directly with internal and external audit regarding ongoing matters as a way to address their concerns, rather than being confident to address matters with the responsible statutory officers and ultimately the head of paid service."*

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

Since 2018 there have been a number of changes to both the senior officers of the Council and to elected members. Despite these changes, our observations during the year ended 31 March 2021 are that a lack of trust is still pervasive within the organisation and is undermining the effectiveness of the Council's governance arrangements. In our view these are serious matters indicative of deep rooted cultural and relationship issues which require urgent action. This lack of trust extends beyond the relationships between officers and members to the relationships between members, in particular between the Council's Executive and other members. This in turn hinders efforts to improve the relationships between officers and all members, as officers feel they are regarded by members as 'taking sides' in areas of disagreement between members.

1. We therefore recommend that the Council develop a comprehensive Improvement Plan to address the cultural and relationship issues which exist within the Council as a matter of urgency. In our view it is the responsibility of all elected members and officers to work together to address these serious matters. This will require the involvement of external specialists as, in our view, the relationships within the Council have deteriorated to a point which the Council will not be able to remedy on its own.

We consider that the Council needs to take this step as an immediate action and we will be following up on the Council's response to our recommendation over the next 6 months. Where we remain unsatisfied with the Council's progress, we will consider exercising our further powers by making formal statutory recommendations. This would require a formal public response from the Council and be notified to the Secretary of State.

How the body monitors and ensures appropriate standards, such as meeting legislative/regulatory requirements and standards in terms of officer or member behaviour (such as gifts and hospitality or declarations/conflicts of interests)

The Council's Overview and Scrutiny Board monitors the performance of the Council's services and has the power to invite expert witnesses, such as professionals or service users, to advise the Board. The Council's Constitution includes Codes of Conduct for both elected members and employed officers which set out the expected behaviour of individuals, including the management of conflicts of interest. Failure to adhere to the Codes of Conduct may result in disciplinary proceedings under the Council's HR policies.

Elected members are required to complete annual declarations of any potential conflict of interest, which are maintained on a register by the Council. A gifts and hospitality register is also maintained and available for public inspection.

Like many organisations, the Council is reliant on self-reporting by elected members and officers of any conflicts of interest, however we have identified a small number of instances where declarations made by elected members were either incomplete or inconsistent with previous declarations. We have also observed that there is a lack of trust between elected members that relevant interests are declared at decision making meetings, which contributes to a lack of confidence from some elected members in decisions being taken.

2. We therefore recommend that refresher training be provided to all of the Council's elected members on the requirements of the Council's Code of Conduct for Members, including the disclosure of pecuniary interests and the Seven Principles of Public Life (also known as the 'Nolan Principles'), as set in the Council's Constitution.

3. Whilst we recognise that the responsibility to declare actual or potential conflicts of interest sits with members under both statute and the Council's Code of Conduct, given our observations we also recommend that management implement additional assurance checks over elected member declarations of interest, for example by cross-referencing to Companies House records or declarations made by elected members to other public bodies, to provide additional comfort over their completeness.

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

As a local authority with a mayoral model, the Council is entitled to utilise its resources to appoint a mayoral political assistant. A mayoral political assistant is a local government employee who undertakes research and provides administrative support to the Mayor. The mayoral political assistant post is a politically restricted post, and there are strict rules set out within The Local Authorities (Elected Mayor and Mayor's Assistant) (England) Regulations 2002 which govern appointments to this post. These include that the role must be performed by an employee of the Council. The Council's mayoral assistant post has remained vacant since September 2019.

Between October 2019 and November 2020, the Council engaged an external advisor through a local publicity company, at a cost of £32,000, to work directly with the Council's Mayor. The Council has been unable to explain the exact nature of services provided by this external advisor, however it has accepted that they likely included activities which fall within the scope of the role of the mayoral political assistant. This arrangement was terminated in November 2020 after it was assessed by the Council to be unlawful under The Local Authorities (Elected Mayor and Mayor's Assistant) (England) Regulations 2002. The payments made to the publicity company under this arrangement were therefore also unlawful, however we note they were not material to our opinion on the Council's financial statements.

The arrangement was entered into by the Council without following either the Council's recruitment policies, which would have applied to a permanent employee of the Council, or the Council's procurement policies, which would have applied to an external supplier. Payments to the publicity company were directly approved by the Council's Chief Executive despite the Council not being able to explain the nature of services received. Notwithstanding the lawfulness of the arrangement, by making payments to a supplier without understanding the nature of services being received in exchange for those payments the Council is unable to demonstrate that the payments represented value for money for taxpayers.

4. We therefore recommend that management undertake a review to establish whether there are any other arrangements at the Council which may have been entered into without following proper Council processes and, if so, review those arrangements to ensure that they are appropriate and represent value for money for the Council.

How the body monitors and assesses risk and how the body gains assurance over the effective operation of internal controls, including arrangements to prevent and detect fraud

The Council maintains a Strategic Risk Register which is used to record and monitor the most significant risks, both financial and non-financial, identified by the Council. Beneath the Strategic Risk Register, each directorate maintains its own risk register and can escalate risks up to the Strategic Risk Register when sufficiently significant.

The strategic and directorate risk registers are reviewed monthly by the Leadership Management Team and directorate management teams, respectively. The Strategic Risk Register is also reviewed quarterly by the Executive and the Overview and Scrutiny Board.

Internal audit undertake an annual programme of work to provide assurance over the operation of the Council's internal controls. Risks identified and recorded on the Council's risk registers are used to inform the annual internal audit plan. Internal audit also provide a programme of counter-fraud activity to the Council.

A number of the matters which have been brought to our attention during the course of our audit were also reported to senior officers and the Council commissioned several reviews by internal audit to respond to the matters raised. These included reports on the management of the Boho X project, the purchase of the Covid-19 tests and the completeness of member declarations of interest. In our view, the scope of this work was not always sufficient to provide assurance to management on the full extent of issues or the wider risks posed to the Council as the work was narrowly defined and it was not always evident that there was follow-up on findings which indicated areas where additional risks may exist beyond the initial scope of work. Budget limitations were cited as a reason for this, however the reports produced did not highlight these areas for consideration of follow-up work by officers or the Corporate Affairs and Audit Committee. Significant reliance was also placed by internal audit on verbal evidence from individuals relating to events which occurred sometime previous, and there appeared to be a lack of documented challenge by internal audit to assertions received from those subject to enquiry.

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

5. We recommend that management consider whether further assurance is required to establish whether the risks identified by the Council to date are complete and the actions taken to respond to those risks sufficient.

6. We also recommend that management work with internal audit to ensure that where future pieces of work identify evidence of wider risks which are not immediately followed-up on, these are reported so that the Council's officers and the Corporate Affairs and Audit Committee can decide whether further investigation is appropriate.

How the body approaches and carries out its annual budget setting process

The Council maintains a Strategic Plan which sets out the key priorities for the Council, including those of the Mayor, over a multi-year period. The Strategic Plan forms the basis for the Council's budget setting exercise, along with forecasts from individual directorates for existing plans and services. These are collated with assumptions for cost pressures and future funding levels to produce a draft budget.

The draft budget is reviewed and stress tested for different scenarios by the Council's Leadership Management Team and Executive, before being issued to key stakeholders for consultation.

Management review the responses received from stakeholder consultations and make any necessary amendments to the draft budget, before submitting the finalised budget to meeting of the full Council for approval.

How the body ensures effective processes and systems are in place to ensure budgetary control; to communicate relevant, accurate and timely management information (including non-financial information where appropriate); supports its statutory financial reporting requirements; and ensures corrective action is taken where needed

The Council delegates budgets to individual cost centre managers, who are responsible for ensuring delivery within the delegated budget. Financial training is provided to all budget holders, who meet regularly with finance business partners to monitor financial performance.

Financial performance against budget and updated forecasts for the remainder of the year are presented to the Council's Leadership Management Team and Executive on a quarterly basis, along with proposals for corrective actions where required.

Improving economy, efficiency and effectiveness

How financial and performance information has been used to assess performance to identify areas for improvement

Financial performance is monitored via management accounts and presented to the Executive and Corporate Affairs and Audit Committee on a quarterly basis. Reporting includes comparison of both performance to date and full-year forecasts against budgets, with explanations provided for significant variances. Comparison is also made to the position in previous reporting to monitor whether improvement actions have had the desired impact.

Beneath the Council's high-level reporting, budgets and performance are monitored at service line and budget holder levels, with individual budget holders responsible for ensuring delivery against delegated budgets and the accurate forecasting of future performance.

How the body evaluates the services it provides to assess performance and identify areas for improvement

Business intelligence dashboards are used by both Council leadership and service line management to monitor key performance indicators across the Council's services and track the implementation of previously agreed actions.

In January 2020, the Council's provision of childrens social care services was rated inadequate by the Office for Standards in Education, Children's Services and Skills (Ofsted), who noted that 'leaders have not sufficiently focused on the significant areas of weakness to ensure that the needs of children and care leavers are properly met'. Our value for money opinion in 2019/20, issued in accordance with the 2015 Code of Audit Practice extant at the time, was qualified in respect of this matter.

In response to the Ofsted findings, the Council implemented a Children's Services Improvement Plan. Delivery against this plan is overseen by a Multi-Agency Strategic Board, supported by a Multi-Agency Operational Board.

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

The appointed Commissioner for Children’s Services in Middlesbrough issued a 12-month review of the Council’s progress against the Improvement Plan in July 2021, covering the period to May 2021. This review noted that “considerable progress has been made and there is evidence of real impact” and recommended that the Council be allowed to retain control of its Children’s Services. The report did however note that the Council’s Improvement Plan remains a multi-year exercise and, whilst good progress is being made, the Council has more to do before its Children’s Services can be considered as adequate in all regards.

Whilst we note that the Council’s Children’s Services are not yet consistently delivering the expected levels of performance, this reflects the status of the service at the start of the 2020/21 financial year. The Council’s actions during the year to 31 March 2021, as assessed by the Commissioner for Children’s Services in Middlesbrough, demonstrate that the Council had appropriate arrangements in place during 2020/21 to deliver against the Improvement Plan. We do not therefore report a significant weakness in the Council’s arrangements during the year ended 31 March 2021 in respect of the provision of Children’s Services, however we will continue to monitor the Council’s progress against the Improvement Plan.

The provision of childrens social care is a key financial pressure for the Council. Whilst the Council has invested additional resources in the delivery of the Childrens Services Improvement Plan, it is management's expectation over the medium term that the improvements in service delivery will ultimately decrease costs by more effectively meeting the needs of service users during the earlier, lower cost, stages of care.

How the body ensures it delivers its role within significant partnerships, engages with stakeholders it has identified, monitors performance against expectations, and ensures action is taken where necessary to improve

The Council has a Partnership Governance Policy which governs how the Council develops and manages its partnerships. All new partnership arrangements are considered to be projects and subject to the approval processes of the Council's Programme and Project Management Policy.

Each partnership arrangement has a dedicated lead manager who is responsible for managing the partnership's performance and governance. A register is maintained of all Council partnerships and the performance of significant partnerships is included in quarterly performance reporting to the Executive and Overview and Scrutiny Board.

A number of the Council's elected members also hold positions in local and regional partner organisations to promote effective cross-working between partnership members.

Through the Multi-Agency Strategic Board and Multi-Agency Operational Board, the Council has worked particularly closely during 2020-21 with the Department for Education (DfE) and the DfE appointed Commissioner for Children's Services in Middlesbrough on the delivery of the Council's Childrens Services Improvement Plan.

Where the body commissions or procures services, how the body ensures that this is done in accordance with relevant legislation, professional standards and internal policies, and how the body assesses whether it is realising the expected benefits

The Council uses the North East Procurement Organisation (NEPO), a regional procurement hub for North East local government authorities, for all of its tendered procurements. NEPO also maintain a public contracts register which lists all of the Council's current contracts. The Council also has a central procurement unit, which provides support to individuals within the Council overseeing procurement activity through NEPO.

The Council has a Strategic Procurement Strategy and Contract Management Framework which are used to provide a framework for the commissioning of services and evaluation of the services received under awarded contracts.

The monitoring of the performance received from suppliers is integrated into the Council's overall processes for monitoring the delivery of its services to service users, as detailed above.

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

Financial sustainability

How the body ensures that it identifies all the significant financial pressures that are relevant to its short and medium-term plans and builds these into them

The Council undertakes an annual exercise to set its annual budget for the following financial year and to update its Medium Term Financial Plan (MTFP), which covers the following three years. Key inputs to this exercise include forecasts for pay and non-pay inflation, changes in the level of demand for the Council's services and changes in funding received from central government. The MTFP for 2021-24 also included consideration of additional costs and funding relating to the Covid-19 pandemic.

The Council's finance team work with the heads of individual directorates to identify cost pressures, including due to changes in demand for services, and model the impacts of different scenarios on the Council's finances. Significant changes are discussed by the Leadership Management Team and Council Executive prior to being implemented in the MTFP.

Performance against the current year's budget is monitored on a quarterly basis during the year and used to identify cost pressures which require reflecting in subsequent MTFPs.

How the body plans to bridge its funding gaps and identifies achievable savings

As part of the annual budget setting exercise, the Council identifies the level of savings required to match the anticipated net cost of services to the levels of available funding. For the 2021-22 budget, a budget gap of £1.626 million was identified.

Individual directorates are required to identify potential savings within their service area, which may arise from reductions to expenditure or increases to income. Savings may also be identified through the Council's finance team, as they are not always directly related to service delivery. Where proposed savings may have a significant impact on service delivery, the Council holds a public consultation prior to incorporating the saving into financial plans.

The level of savings identified and incorporated into the Council's budget exceeds the required level of savings to provide additional buffer against the non-achievement of planned savings. For the 2021/22 budget, identified savings exceeded required savings by £0.695 million.

How the body plans finances to support the sustainable delivery of services in accordance with strategic and statutory priorities

The impact of changes to the Council's financial plans are modelled through a minimum of 3 years as part of the MTFP and any resulting budget gap over that period quantified and incorporated into the following budgeting cycle.

The Council aims to meet the costs of its day-to-day activities from available funding, but borrows for capital investment purposes. The impact of planned borrowing (i.e. interest charges) is incorporated into the Council's revenue budget and MTFP.

During 2020/21, management undertook a self-assessment against the CIPFA Financial Management Code, which promotes the financial sustainability of local authority capital expenditure and associated borrowing. Several actions were identified to strengthen the Council's processes, however no major weaknesses were noted.

Under the Council’s constitution there is a clear delineation between the responsibility for setting the Council’s strategic objectives, which sits with members and the Executive, and the responsibility for delivery of the operational activities which underpin the strategic objectives, which sits with officers. We have however identified multiple instances, as detailed above, where the involvement of members strayed into operational matters. We also note that where this occurred, it was often known to officers and insufficient challenge was provided to members on the boundaries of members’ and officers’ respective responsibilities. A lack of adherence to the delineation between strategic and operational responsibilities increases the risk that operational decisions are taken which are not optimal for the Council or the Council is unable to demonstrate represent value for money. Examples of this noted above include the Boho X project and the purchase of Covid tests.

Commentary on value for money arrangements (continued)

Commentary on value for money arrangements (continued)

7. We therefore recommend that the Council provides additional training to members and officers on the boundaries of respective responsibilities under the Council's Constitution. The Council should also seek to ensure that a culture of challenge, where these boundaries are not being adhered to, is understood by and expected from all parties as part of the wider Improvement Plan to address the cultural and relationship issues which exist within the Council.

How the body ensures that its financial plan is consistent with other plans such as workforce, capital, investment, and other operational planning which may include working with other local public bodies as part of a wider system

The Council develops its Capital Strategy and Investment Strategy alongside the MTFP and incorporates the revenue impact of planned capital expenditure and borrowing into the MTFP.

The Council operates a finance business partner model to facilitate regular communication between finance staff and the Council's directorates to ensure that other plans being prepared by the Council are consistent with the Council's financial planning.

The Council also requires that all decisions which are deemed significant enough to warrant approval by the senior management team or elected members are approved by the Council's Director of Finance to ensure that the financial implications of significant decisions are considered and reflected in the Council's financial planning.

How the body identifies and manages risks to financial resilience, e.g. unplanned changes in demand, including challenge of the assumptions underlying its plans

The Council maintains a number of earmarked reserves, which represent amounts set aside from the Council's General Fund to be used for specified purposes in the future. Management use earmarked reserves to allow for known or potential future cost pressures. During 2020-21, management released a previously held Investment Fund Reserve to offset the impact of the Covid-19 pandemic on the Council's finances.

In addition, the Council sets a minimum level for its General Fund in order to ensure that the Council does not fully deplete its reserves through normal activities. During 2020/21, the Council increased this minimum level from £9.4 million to £11 million, effective from 2021/22, to reflect higher uncertainty in the Council's financial projections, including the ongoing impact of the Covid-19 pandemic. At 31 March 2021, the Council's General Fund balance was above the £9.4 million minimum level in effect for 2020/21 at £10.5 million and is forecast to increase to the revised minimum level of £11 million during 2021/22.

The Council's MTFP produced during 2020/21 included a balanced budget for 2021/22 and indicative budgets for 2022/23 and 2023/24. The MTFP forecast a budget deficit of £0.6 million in 2022/23, which the Council intends to finance from reserves, and a budget deficit of £3.1 million for 2023/24 which the Council will need to address in future MTFPs.

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Annual Governance Statement 2021/22

Summary

This Annual Governance Statement (AGS) sets out the Council's position at the end of the 202/22 financial year in relation to compliance with the Local Code of Corporate Governance (LCCG) which sets out the standards to be achieved across the corporate governance framework.

The AGS comprises the following sections:

- an overview of the Council's governance arrangements;
- progress made on governance during 2021/22;
- Internal Audit activity and governance concerns arising from that in 2021/22
- Member involvement in corporate governance
- issues that have arisen during 2021/22;
- a position statement against the Code of Corporate Governance; and
- conclusion, summary of the key issues to be addressed and resulting governance priorities for 2022/23.

It sets out:

- how well the Council has delivered previous commitments to strengthen its corporate governance arrangements, providing an update on actions committed to in the 2020/21 Annual Governance Statement
- governance concerns arising from Internal Audit activity during 2021/22
- specific events during 2021/22 that relate to corporate governance arrangements and their impact on compliance with the LCCG.

In summary, across the different sections of the document, the following key issues and themes have been set out:

- During 2021/22 there were a series of statements of concern made in relation to Mayoral conduct that required investigation which identified weaknesses and incidents of non-compliance with procurement, financial governance and project management.
- Member to member and member to officer relationships have deteriorated further in the 2021/22 financial year resulting in a more dysfunctional culture than that evident in 2020/21, detail of which was referenced in the 2020/21 AGS. During 2022/23 positive action has begun to address this and has resulted in the commissioning of external support, development of a Corporate Governance Improvement Plan, comprising equal Member / Officer membership to oversee delivery and in recognition of the need to further develop and strengthen officer / Member working relationships
- Actions set out for delivery in 2022/23 may need to be adjusted to align with the model for Corporate Governance Improvement agreed by Council in October 2022. As well as progress, any required changes will be reported to the Corporate Governance Improvement Board (CGIB) and to full Council
- Significant concerns in two internal audits resulted in seven Priority One recommendations in relation to CCTV and the governance of the BOHO X project. As a result of this and other issues reported in the body of the AGS, the overall opinion of the Head of Internal Audit on the framework of governance, risk

management and control operating at the Council is that it provides **Limited Assurance**.

- Although outside the scope of the reporting period, inflation and the cost of living have had a significant impact on the Council's budget position and on the financial resilience of the town.

In order to ensure there is a continued high profile focus on this corporate governance activity, content of this statement has been cross referenced with the Corporate Governance Improvement Plan and progress against the detailed activities set out within this AGS will be reported by Exception to the Corporate Governance Improvement Board (CGIB) established in November 2022, comprised of Group Leaders, the Mayor, Senior Officers, CIPFA representatives and the Local Government Association (Chair). this replaces the previously established officer led Corporate Governance Board, reflected in the 2021/22 governance structure diagram.

Introduction

1. Middlesbrough Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards. The Council has in place a Code of Corporate Governance, which sets out its corporate governance framework and is reviewed annually. This framework comprises the culture, values, systems and processes of the Council, which together ensure that it does the right things, at the right time and in the right way. As set out in the 2020/21 Statement of Accounts, the Council is currently experiencing challenges in meeting these standards though is working to address areas of weakness or non-compliance.

2. This statement will set out that Member to Member and Member to officer relationships have deteriorated further in the 2021/22 financial year, resulting in a more dysfunctional culture than that evident in 2020/21. It will also set out joint plans to address this as both members and officers have the responsibility for this in terms of the result of further dysfunctionality and in terms of repairing this situation. The seriousness of this situation has been recognised by the Council's external auditors, Ernst & Young (EY), who have indicated that if insufficient progress is made in tackling the weaknesses that exist in our Value for Money arrangements by February 2023, EY will consider exercising its powers by making formal statutory recommendations. In December 2022 EY will submit a report to the Corporate Affairs and Audit Committee to state it does not intend to exercise further reporting powers at this time.

3. Please note, as a result of delays in the ratification of the recently agreed 2020/21 Annual Governance Statement, this draft statement contains repetition between that document. Progress made during the coming months will be reflected in the finalised version of this statement.

4. The Code of Corporate Governance aligns with the latest CIPFA / Solace guidance, which sets out the following principles of good governance:

   - behaving with integrity, demonstrating strong commitment to ethical values, and respecting the rule of law;
   - ensuring openness and comprehensive stakeholder engagement;
   - defining outcomes in terms of sustainable economic, social and environmental benefits;
   - determining the interventions necessary to optimise the achievement of the intended outcomes;
   - developing the entity's capacity, including the capability of its leadership and the individuals within it;
   - managing risks and performance through robust internal control and strong public financial management; and
   - implementing good practices in transparency, reporting, and audit to deliver effective accountability.

5. The purpose of the Annual Governance Statement (AGS) is to assess the extent to which the Council complies with its Code of Corporate Governance, how it has monitored and improved the effectiveness of its governance arrangements in the past year and identify actions to strengthen these arrangements going forward.

6. The AGS forms part of the Statement of Accounts that the Council must produce on an annual basis and as such must be approved by the Mayor of Middlesbrough and the Council's Chief Executive and Section 151 Officer.

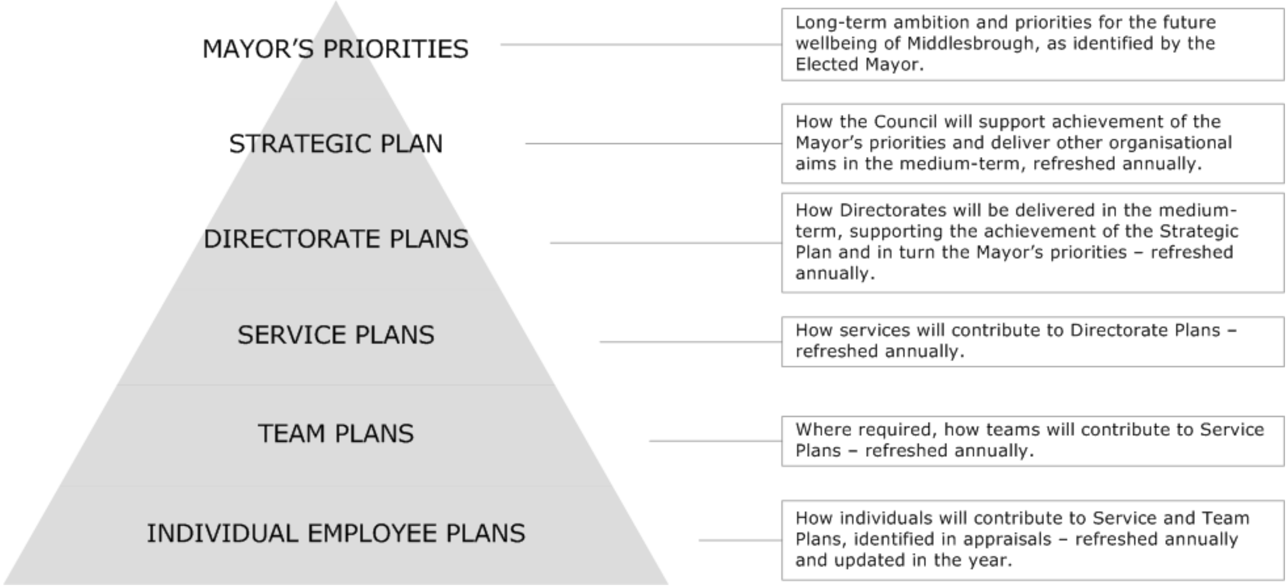
7. The development of the AGS was coordinated by the Strategy, Information and Governance service, in conjunction with statutory officers and other officers with responsibility for corporate governance processes, and with input from Internal Audit.

The Council's governance arrangements during 2021/22

8. The Committee structure in place within the Council during 2021/22 is set out Appendix 2. The terms of reference of all committees are published on the Council's committee papers site and open data site.

9. Committees take decisions in line with the Council's approved strategies and policies. The Strategic Plan is the Council's overarching business plan for the medium-term and is typically refreshed on an annual basis. The plan was last refreshed in February 2021 to reflect the impact of COVID-19 and UK's exit from the European Union on Middlesbrough and on the Council's strategic priorities. However in April 2022 the underpinning work programme was refreshed by Council to cover the period up until 2024.

10. There is a 'golden thread' which runs from this document and throughout of the Council's governance and policy frameworks.



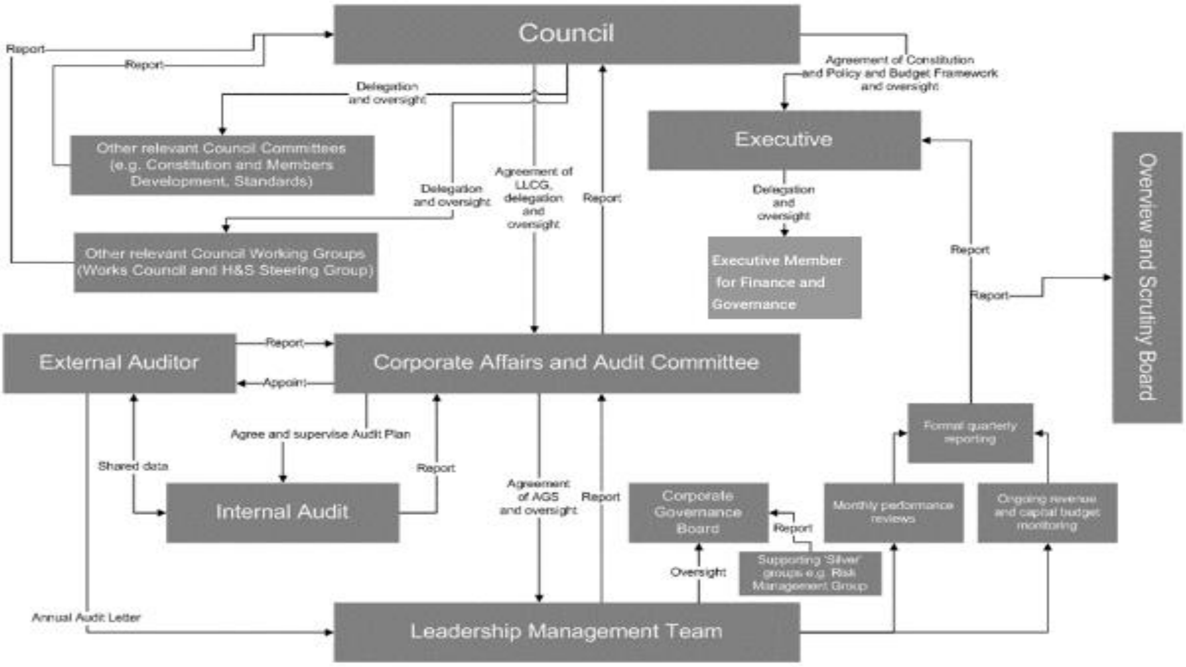
MAYOR'S PRIORITIES	Long-term ambition and priorities for the future wellbeing of Middlesbrough, as identified by the Elected Mayor.
STRATEGIC PLAN	How the Council will support achievement of the Mayor's priorities and deliver other organisational aims in the medium-term, refreshed annually.
DIRECTORATE PLANS	How Directorates will be delivered in the medium-term, supporting the achievement of the Strategic Plan and in turn the Mayor's priorities – refreshed annually.
SERVICE PLANS	How services will contribute to Directorate Plans – refreshed annually.
TEAM PLANS	Where required, how teams will contribute to Service Plans – refreshed annually.
INDIVIDUAL EMPLOYEE PLANS	How individuals will contribute to Service and Team Plans, identified in appraisals – refreshed annually and updated in the year.

11. In making decisions, the Mayor and councillors are supported by a senior management structure that is designed to support effective compliance with the Council's legal and governance responsibilities, led by the three statutory officers (Head of Paid Service, Section 151 Officer and Monitoring Officer). Some decisions are delegated to senior officers. All delegations are required to be published on the Council's website.

12. The Council's Constitution defines the respective roles of councillors and officers, outlines expected standards and behaviours and provides a framework to enable effective working relationships across the Council. The Constitution also provides

direction on the various roles in place to ensure effective corporate governance within the Council.

13. Member and officer groups work together with the Council's auditors within the following structure which was in place during 2021/22 to ensure compliance with the LCGG and its supporting policies and procedures (as set out in Appendix 3) and promote continuous improvement in governance, maximising its potential to deliver its priorities and value for money.



Progress made during 2021/22

Implementing actions from the 2020/21 AGS

14. This section would normally set out progress made against the previous year's Annual Governance Statement which had been considered 12 months before this statement. Delays in the signing off of the 2020/21 AGS mean that document has only recently been approved and it therefore contains little movement between the table set out in the 2020/21 AGS and this document, at this stage. Actions due to be delivered in October in relation to delivery of officer training in relation to understanding governance and delivery of advice and challenge have been completed.

15. One action in relation to delivery of a refreshed training approach to ensure senior officer training encompasses the full suite of corporate governance training has been reprofiled to February 2023 in order to allow the shape of that to be influenced by the Training and Development working group which commenced work in November 2022 as part of the Corporate Governance Improvement journey.

16. As set out in the summary of this statement, in order to ensure there is a continued high profile focus on this corporate governance activity, content of this statement has been cross referenced with the Corporate Governance Improvement Plan and progress against the detailed activities set out in both the 2020/21 AGS and this AGS will be

reported by Exception to the Corporate Governance Improvement Board (CGIB) established in November 2022, comprised of Group Leaders, the Mayor, Senior Officers, CIPFA representatives and the Local Government Association (Chair). this replaces the previously established officer led Corporate Governance Board, reflected in the 2021/22 governance structure diagram. 12 actions we completed, one is ongoing and six will be delivered during 2022/23. Appendix 2 sets out the detail of those actions.

Internal Audit during 2021/22

17. During 2021/22 Internal Audit undertook and finalised 20 audits during the year which are set out at Appendix 1.

Corporate Affairs and Audit Committee during 2021/22

18. Corporate Affairs and Audit Committee reviews the Council's arrangements for corporate governance and makes recommendations as appropriate to ensure good governance and continuous improvement.

19. The committee met seven times during 2021/22, and considered the following corporate governance related items:

- Annual Report of the Senior Information Risk Owner (SIRO)
- Update on the Ofsted improvement journey
- Annual Audit letter 2019/20
- Annual assurance report on HR – Health and Wellbeing
- Annual Report of the Head of Internal Audit
- Counter Fraud reports
- 2020-21 EY planning report
- Draft Statement of accounts 2020/21
- Lessons learnt – Best Value Inspection of Liverpool City Council
- Annual Assurance report on Procurement
- Subject Access Requests – Compliance Update
- Complaints and lessons learned report
- Annual Review of the Local Code of Corporate Governance
- Health and Safety Annual Assurance Report
- Community Governance review
- Corporate Debt Write Off policy
- Capital Strategy
- Appointment of External Auditors
- Lessons Learned – Governance on Leasing our Commercial Assets.

Overview and Scrutiny during 2021/22

20. Overview and Scrutiny Board (OSB), supported by a range of topic-specific panels, scrutinises Executive decisions and the performance of Council services. During 2021/22, scrutiny considered the following items that are relevant to corporate governance:

- quarterly reports on delivery of the Strategic Plan and compliance with key corporate governance disciplines;
- quarterly reports on budget outturns for the quarter;
- the Executive Forward Work Programme;
- Terms of Reference for the Middlesbrough Council COVID-19 Recovery group and the subsequent plan;
- COVID-19 Update: Health, Adult Social Care and Public Health;
- Middlesbrough Council COVID-19 – Response and Test, Track and Trace;
- Children's Services update on finance and performance
- COVID-19 updates; and
- governance updates from the Chief Executive.

21. There were no scrutiny call-ins during 2021/22 of any Executive decision.

Other governance related events during 2021/22

COVID-19

22. The During the period covered by this statement, the pandemic continued to impact on the Council and the public, affecting the way services were delivered, although during 2021/22 the delivery of the vaccine programme enabled government to remove all domestic legal restrictions in February 2022. Throughout the year staff continued to work flexibly to ensure services continued to be delivered.

23. During 2021/22 the Council administered and issued over £9m in business grants on behalf of the Government in response to the pandemic, and approximately £2.5m of support to households, providing assistance to hundreds of businesses and over 30,000 residents in some form.

Governance allegations

24. In May 2021, several former Members of the Council's Executive made statements of concern on alleged Mayoral conduct in relation to activity conducted during 2020/21 and concerns that there had been failings of governance across a number of areas. Pre-formal fact finding has been conducted by Internal Audit as a precursor to any matters being conducted under the standards regime. This was commissioned by the Monitoring Officer, following consultation with the 151 Officer and the Head of Paid Service. This has identified weaknesses and incidents of non-compliance, by officers and Members, in relation to governance controls for procurement, financial governance and project management. Actions to address these weaknesses are reflected in the action plan for this statement. This work has been shared with the External Auditors and used to inform their Value for Money assessment.

Resignation of Executive Members

25. Following the submission of the governance allegations referenced above, five Executive members resigned from the Executive on the 11 May 2021, leaving the Council with an Elected Mayor and one Executive Member. The Localism Act 2011 sets out that the Executive minimum composition is a Mayor plus two other members and therefore the Executive was not lawfully constituted and unable to make decisions.

26. The Monitoring Officer immediately set out to senior managers the contingency measure contained in the Council's constitution that could be put in place to enable decision making, however it was not necessary to implement this as the Mayor appointed two new members to the Executive within the following two days.

Organisational culture and Member officer relationships

27. As set out in the 2020/21 AGS, Member to Member and Member to officer relationships have deteriorated further in the 2021/22 financial year resulting in a more dysfunctional culture than that evident in 2020/21. It is the responsibility of both officers and Members to address this proactively to ensure that the culture of the organisation improves. The Chartered Institute of Public Finance and Accountancy (CIPFA) were commissioned to undertake an independent diagnostic of the issues to assist the Council in a way forward. This was reported to Council in the autumn.

28. In addition, positive discussions have been held between senior officers and senior members as part of the finalisation of the 2020/21 AGS which will be built on going forward. External support has also been provided from the Local Government Association (LGA). An extraordinary meeting of the Council was also called to discuss the findings of the External Auditor.

Although out of time scope, significant progress has been made to date in 2022/23 to secure external support, develop an improvement plan and establish an officer / member governance structure to oversee delivery, assess impact to drive forward improvement at a pace. The first meeting of the Corporate Governance Improvement Board and associated Task and Finish working groups to agree the detailed improvement plan commenced in November 2022. Progress against delivery will be measured at 30 / 60 / 90 days. Task and finish groups have been organised around the following themes:

- Roles and Responsibilities
- Training and Development
- Constitution
- Culture and Communities.

29. Some of the key outcomes this work aims to achieve are:

- a refreshed constitution that is easier to follow and reflects the procedures, behaviours and standards that should be adhered to
- improved Officer and Member and Member to Member relationships
- an approach to Member and Officer training that better equips them to deliver their roles in full while adhering to the Council's values and in Members case, the Nolan Principles of Public Life
- A better understanding of, and respect for, the differing roles and responsibilities undertaken by various officers and Members across the organisation.

BOHO X Internal Audit

30. An internal audit of the project management of the BOHO X project was undertaken during 2020/21. The findings of this audit identified five Priority One internal audit actions. The Section 151 Officer and the Chief Executive provided an overview of the detailed findings of this audit to the Corporate Affairs and Audit Committee in April

2022 in order to provide assurance to the Committee that officers recognised the seriousness of the findings and give assurance to committee that these issues were being tackled by also setting out the governance actions to address them. These actions were embedded within the 2020/21 Annual Governance Statement improvement plan. All five priority actions have now been delivered.

CCTV

31. Although completed as part of the 2020/21 internal audit programme of work, an audit of CCTV governance arrangements was not finalised until July 2021. As reported in the 2020/21 AGS, that audit found that there was no central register available that identifies the location of all CCTV camera equipment across the Council. Therefore, the Council was unable to confirm that all CCTV schemes are compliant with the Surveillance Camera Code of Practice and the relevant legislation.

Post-OFSTED improvement journey

32. In December 2019 OFSTED completed an inspection of the Council's compliance with the Inspection of Local Authority Children's Services (ILACS) framework. The outcome of that inspection was a judgement across four categories:

Judgement	Grade
The impact of leaders on social work practice with children and families	Inadequate
The experiences and progress of children who need help and protection	Inadequate
The experiences and progress of children in care and care leavers	Inadequate
Overall effectiveness	Inadequate

33. In 2020/21 a three-year plan was developed to deliver sustained improvement and change in Children's Services, monitored by a monthly Multi-Agency Strategic Improvement Board with a highly-experienced independent chair. The board receives progress reports on delivery of the improvement plan, has oversight of key performance metrics to track impact and considers themed reports on key practice issues. These three elements give the board a comprehensive overview of the delivery and impact of improvement work. The strategic board is supported by an operational board and weekly meetings with senior managers within Children's Services.

34. The Council continued to deliver against this plan during 2021/22 and continues to engage with Ofsted and the Department of Education on its improvement journey. A monitoring visit conducted in March 2022 identified that the Council has:

    1. 'delivered a sustained programme of improvements to ensure there is a systemic focus on children'
    2. 'Senior managers know their service well and have an improved management grip'
    3. 'there has been a substantial improvement in permanence planning for children in case'.

32\. A further visit was held in July 2022 which found that:

- the corporate leadership team has continued to develop and improve services at the front door

- there are stronger and wider partnerships in the Multi-Agency Children's Hub (MACH)
- there are challenges around workforce stability which are impacting on caseloads and quality of practice.

Inflation and cost of living

35. Although the larger impacts are out of the time scope for this statement, the ongoing and cost of living inflationary pressures facing the town and its residents have had and will continue to have a significant impact on the Council's budget position. This is because not only are the costs of delivering services continuing to rise but demand for services has and will continue to increase as more and more households are affected by this issue. As Middlesbrough is one of the most deprived local authorities in England, it is likely to also be one of the most adversely affected areas. An effective Council-wide response to this will be a key challenge for Middlesbrough in 2022/23.

Middlesbrough Development Company activity during 2021/22

36. Middlesbrough Development Company (MDC) is a local authority trading wholly-owned company limited by shares, with the Council as the sole shareholder.

37. During 2021/22 MDC Board met 11 times, with key decisions taken by the company published at www.middlesbroughdevelopmentcompany.co.uk.

38. Internal Audit are currently undertaking an assessment of the company using Local Partnerships and CIPFA best practice guidance on local authority trading companies. While the Council is awaiting feedback and the outcome of their work, the Council is considering the future role of the company and its contribution it makes to delivering council strategic objectives notwithstanding any possible recommendations and changes to strengthen governance arrangements.

Position statement against the Council's Code of Corporate Governance

Self-assessment

39. The Council has completed a position statement against its Code of Corporate Governance for the 2021/22 year, informed by:

    - The information identified in the 2020/21 Annual Governance Statement which has been significantly delayed in its finalisation and therefore updated throughout 2021/22
    - the professional opinion of statutory and other officers with responsibility for the development and maintenance of the Council's internal control environment;
    - reports from Overview and Scrutiny, and Corporate Affairs and Audit Committee's examinations of governance processes; and
    - findings from Internal Audit's review programme and other work completed by Internal Audit, and engagement with the Council's external auditor.

40. The detailed position statement is at Appendix 3 and is reflective of governance risk levels as outlined in the Council's strategic and directorate risk registers.

41. In summary, while the Council can demonstrate that governance processes are in place for the most part, the control weaknesses that were identified in the recently published 2020/21 Annual Governance Statement continue to exist. The Council commissioned CIPFA during 2022 to complete an independent review of its governance arrangements which has informed a Corporate Governance Improvement Plan, along with establishment of an appropriate governance structure which includes a multi-disciplinary Member and officer board that aligns with the Council's Project Management Framework. Progress will be reported to Council on a regular basis to demonstrate delivery of actions and also to assess the impact of those actions.

42. This will provide assurance to members on action being taken and ensure that if control weaknesses continue to exist even after action, further actions can be identified to address those. This will also include engagement with Internal and External Audit to provide assurance around delivery.

Internal Audit opinion

43. The overall opinion of the Head of Internal Audit on the framework of governance, risk management and control operating at the Council is that it provides **Limited Assurance**. No reliance was placed on the work of other assurance providers in reaching this opinion.

44. In giving this opinion, Internal Audit drew attention to the following significant control weaknesses which are considered relevant to the preparation of the 2021/22 Annual Governance Statement.

45. An audit on the project management of Boho X found significant weaknesses in governance and decision making. It found that the project was not always managed in line with the Council's Constitution and the Council's project management framework. In addition, the Council's elected Mayor held undocumented meetings with external contractors without officers present, following agreement by a senior officer.

46. The audit has now been finalised and actions have been agreed with management and delivered.

47. During the year a further audit work was carried out on a number of allegations made by former Executive members. This work was fact-finding in nature and intended to provide management with information on the allegations enabling them to make a decision on the next steps to be taken.

48. Whilst Internal Audit's work on this is not yet complete, the findings have largely been agreed with officers. The work found issues related to those for the Boho X audit including governance weaknesses, a lack of challenge or advice from officers, and examples of the Mayor holding undocumented meetings with external contractors.

49. These findings lead Internal Audit to conclude that the concerns identified are not limited to one area or audit and are indicative of wider issues around relationships between councillors and officers and a lack of clear separation of their respective roles, in practice.

50. Actions agreed for the issues identified from the Boho X audit will be followed-up during 2022/23 and further updates will be brought to the Corporate Affairs and Audit Committee.

51. The overall opinion given is based on work that has been undertaken directly by Internal Audit, and on the cumulative knowledge gained through their ongoing liaison and planning with officers. In giving the opinion, Internal Audit note that the Covid-19 pandemic has continued to affect the Council over the last year, with a consequential impact on business operations and controls. The work of Internal Audit has been directed to the areas considered most at risk, or that offer the most value for the authority overall. However, not all the areas affected by the Covid-19 pandemic will have been reviewed.

External Audit opinion

52. The opinion of the Council's External Auditor will be provided to Corporate Audit and Affairs Committee alongside the final version of this document.

Conclusion

53. As was the case in the 2020/21 Annual Governance Statement, the Council continues to demonstrate that while there are governance processes in place for the most part, it is clear that control weaknesses have continued to exist and need to be addressed if the Council is to improve adherence to processes.

54. During the financial year 2021/22 Member to member and member to officer relationships deteriorated further. Both members and officers have the responsibility for this in terms of the result of further dysfunctionality and in terms of repairing this situation. This was reflected in the diagnostic work completed by CIPFA and reported to Council in October 2022. All members at that meeting voted to accept those findings in full and to work together, with officers to address them. The Chief Executive has also stated that senior officers fully accept the findings of that work.

55. The scale of the culture change required is significant and cannot be underestimated. The Council's External Auditors have made clear that they view this matter with the utmost seriousness, as do the senior officers and senior members who have contributed towards the development of this statement.

56. During 2022/23, the upmost governance priority of the organisation will therefore be ensuring that it responds positively to the issues identified within both the 2020/21 AGS and through ongoing discourse through 2021/22 and into 2022/23. The Mayor is committed to leading this change with the support of the Chief Executive and senior managers.

57. As set out in this AGS, the diagnostic work undertaken by CIPFA during the second quarter of 2022/23 provided an evidence base to inform the planned governance improvements actions required to ensure the culture of this organisation is improved. A detailed improvement plan has been developed in partnership with officers and members to maximise the likelihood of them being successfully delivered.

Signed on behalf of Middlesbrough Council (to be completed upon finalisation)

Andy Preston
Elected Mayor of Middlesbrough
Xx/xx/xx

Tony Parkinson
Chief Executive
Xx/xx/xx

Helen Seechurn
Director of Finance
(Section 151 Officer)
Xx/xx/xx

Appendix 1 Internal Audits completed during 2021/22

Audited System / Service	Assurance Opinion	Priority Actions		
		P1	P2	P3
Use of CCTV	Limited Assurance	2	5	1
Officer and Member decision making	Reasonable Assurance	0	0	6
Schools themed audit – pupil premium	Reasonable Assurance	0	0	4
Teesside Pension Fund – investments	Substantial Assurance	0	0	1
Teesside Pension Fund – Administration	Substantial Assurance	0	1	2
Governance arrangements	Substantial Assurance	0	0	2
Main accounting system	Reasonable Assurance	0	0	3
Cyber security awareness	Substantial Assurance	0	0	1
Social Care and emergency payments	Substantial Assurance	0	0	0
Council Tax and NNDR	Substantial Assurance	0	0	0
Council Tax Support and Housing Benefits	Reasonable Assurance	0	2	0
Youth Employment Initiative	Substantial Assurance	0	0	0
Project management – Boho X	Limited Assurance	5	6	1

Audited System / Service	Assurance Opinion	Priority Actions		
		P1	P2	P3
Asset maintenance	Substantial Assurance	0	0	0
Teesside Pension Fund – Overpayments	Substantial Assurance	0	0	0
Schools themed audit – purchasing cards & asset management	Reasonable Assurance	0	6	9
ICT change management	Substantial Assurance	0	0	1
Home working	Substantial Assurance	0	1	2
Future High Street Fund Governance	Substantial Assurance	0	1	1
Benefits – overpayments	Substantial Assurance	0	0	0
Burial grounds	Draft report issued			
Children’s commissioning & contract management	In progress			
Middlesbrough Development Company	In progress			
	Total:	**7**	**22**	**34**

58. The opinions used by Internal Audit during 2021/22 are explained below:

- Substantial Assurance – A sound system of governance, risk management and control exists, with internal controls operating effectively and being consistently applied to support the achievement of objectives in the area audited.
- Reasonable Assurance – There is a generally sound system of governance, risk management and control in place. Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of objectives in the area audited.

- Limited Assurance – Significant gaps, weaknesses or non-compliance were identified. Improvement is required to the system of governance, risk management and control to effectively manage risks to the achievement of objectives in the area audited.
- No Assurance – Immediate action is required to address fundamental gaps, weaknesses or non-compliance identified. The system of governance, risk management and control is inadequate to effectively manage risks to the achievement of objectives in the area audited.

59. The following categories of opinion are also applied to individual recommendations agreed with management:

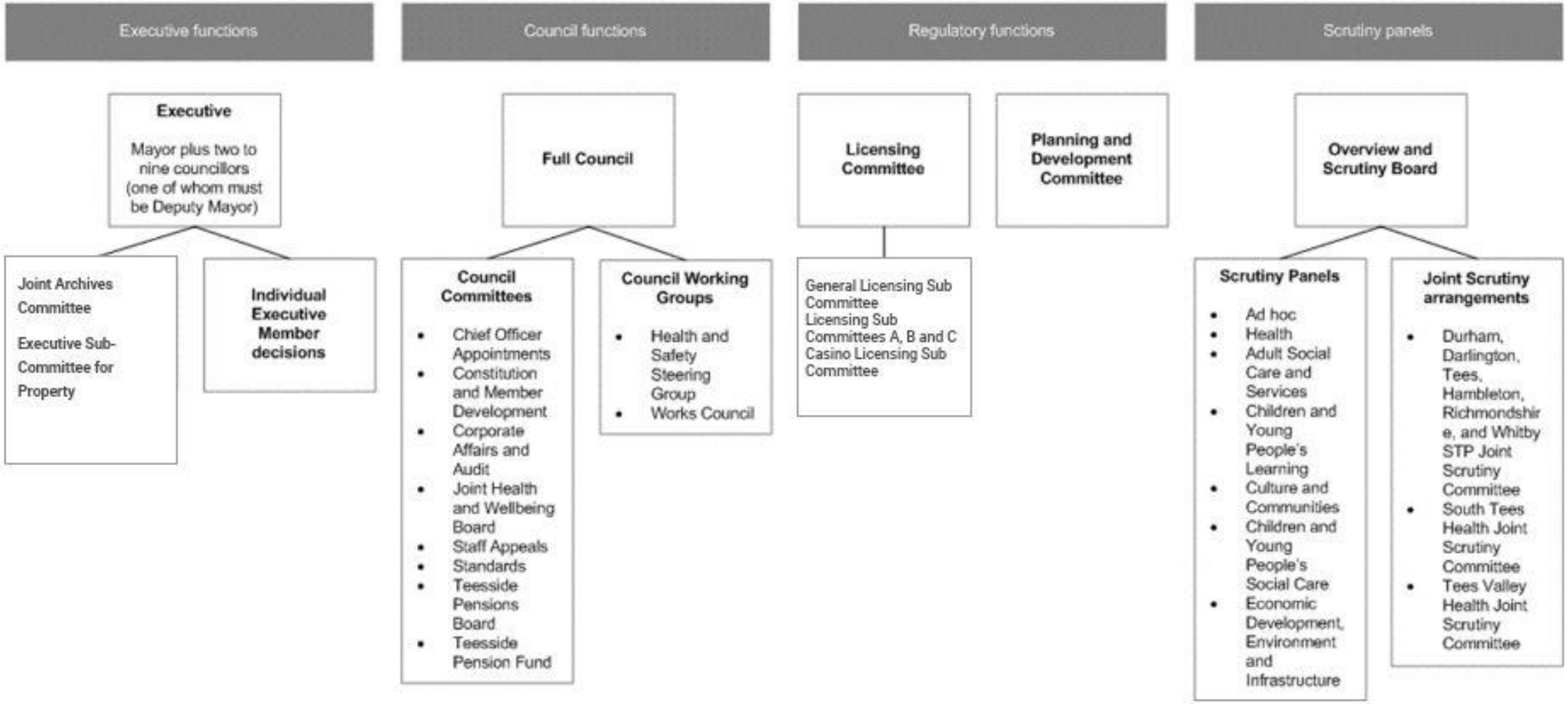
- Priority 1 (P1) – A fundamental system weakness, which presents unacceptable risk to the system objectives and requires urgent attention by management.
- Priority 2 (P2) – A significant system weakness, whose impact or frequency presents risks to the system objectives, which needs to be addressed by management.
- Priority 3 (P3) – The system objectives are not exposed to significant risk, but the issue merits attention by management.

Appendix 2 – 2020/21 Annual Governance Statement actions

Action	Lead Officer(s)	Status / deadline
Revise members' code of conduct and deliver training on it to all members, including ethics.	Head of Democratic Services	Complete
Raise awareness of the role of the Monitoring officer, in particular giving advice and guidance to officers on governance.	Monitoring Officer	Complete
Delivery of training to all Members on roles and responsibilities in relation to Programme and Project Management	Strategic Delivery Manager	Complete
Launch the revised Management Framework, to ensure managers understand how they are expected to act to be in line with the refreshed corporate values.	Head of Human Resources	Complete
Refresh training materials on the Council's Organisational Development system to align training with compliance with the values	Head of Human Resources	Complete
Refresher senior leadership development work programme delivered by the LGA to ensure officer and member roles continue to be understood and adhered to.	Monitoring Officer	Complete
Launch an expanded 360 project to cover a wider cohort of managers.	Head of Human Resources	Complete
Member refresher training on the code of conduct will include information on hospitality requirements and registers of interests.	Head of Democratic Services	Complete
Constitution and Member Development committee to consider amendments to the constitution to strengthen and clarify the actions that can be taken in response to councillors failing to complete mandatory training.	Head of Democratic Services	Complete
Deliver training to members on use of social media.	Head of Democratic Services	Complete
Continue to deliver the OFSTED Improvement plan, in particular those actions that have been identified to strengthen leadership within Children's Safeguarding Services.	Executive Director of Children's Services	Ongoing
Refreshed and strengthened training to officers delivering projects to ensure project and wider Council decision making governance is understood and adhered to.	Strategic Delivery Manager	Complete
Delivery of training for Senior Officers on the officer code of conduct and the provision of effective advice and challenge	Monitoring Officer	Complete
Refreshed training approach to ensure senior officers training encompasses the full suite of corporate governance training.	Head of Human Resources and the Monitoring Officer	February 2023
Transition to OPEN, the NEPO e-procurement system that is being put in place for the North East, replacing the current contract management framework with an end to end product once fully rollout.	Head of Commissioning and Procurement	March 2023

Refresh training on the Equality Act and the impact assessment process, ensuring it is mandatory for key officers.	Head of Strategy, Information and Governance	March 2023
Complete mandatory refresher training on the officer and member protocol within Middlesbrough Council’s constitution for all members and senior officers.	Monitoring Officer	March 2023
Continue to implement a scheme of sub-delegations where appropriate to further improve governance around officer delegated decisions.	Director of Legal and Governance Services	March 2023
Refresh the Joint strategic Needs Assessment (JSNA) for children and young people this year and complete the Adults and Older persons JSNA.	Director of Public Health with support from the Interim Head of Strategy, Information and Governance	March 2023

Appendix 3: Middlesbrough Council Committee Structure 2021/22



Appendix 4: Position statement against the Council's Code of Corporate Governance

Local Code of Corporate Governance		Self-assessment	
Principle / supporting principles	**To meet these requirements, the Council will:**	**Evidence of compliance with this principle**	**Areas for improvement**
Behaving with integrity, demonstrating strong commitment to ethical values and respecting the rule of law. • Behaving with integrity • Demonstrating strong commitment to ethical values • Respecting the rule of law	• Work diligently and with integrity to achieve the Elected Mayor's Priorities for Middlesbrough. • Clearly document expected behaviours, and decision-making processes, for members and officers, and regularly review these. • Effectively communicate expected behaviours to members and officers, and provide appropriate training on ethical behaviour. • Ensure members, statutory officers, other key post holders are able and supported to fulfil their duties and meet their responsibilities. • Ensure compliance by maintaining effective audit committee, internal audit and scrutiny functions, and standards and disciplinary processes.	• Constitution and supporting documentation clearly set out expected behaviours and decision-making processes, including member and officer relationships, codes of conduct, financial procedure rules and schemes of delegation. Constitution updated during 2020 to reflect COVID impacts to ensure meetings continued to be conducted effectively and in line with best practice. Additional guidance was issued to support this. • Corporate values (one of which is integrity) in place and embedded within employee recruitment and selection, induction, appraisal and development. They were refreshed during 2020/21. • Comprehensive member induction process and member development programme was delivered for the first year of the current term of office (19/20). • Member and officer declarations of interests registers in place, and requested to be updated annually but there is a requirement that Members notify the Monitoring Officer electronically of any changes through the Council's committee management system, Modern.gov. • Training for members on the code of conduct in place with a high level of compliance, and with all members individually signed up to the code. The action to deliver refreshed training in 20/21 has been slipped to 2021/22 as a result of COVID and its impact on capacity to deliver. • Comprehensive member handbook in place to provide guidance and signpost support, and members' enquiries service in place to assist with casework and data requests. • Statutory officers clearly identified and appropriately supported. The Council	• A robust officer scheme of delegations and sub-delegations is required to ensure effective, appropriate and timely taking of decisions that can be taken by officers. (20/21 action) • Refresher training on ethics has been identified as prudent in light of increased standards complaints and the misconduct in public office conviction. (20/21 action) • Action required to ensure understanding of the Equality Act and the impact assessment process, supplementing mandatory equality and inclusion training with refresher impact assessment training for key officers. (20/21 action) • Increased awareness of the role of the Monitoring officer, to ensure officers are aware that they can seek advice and guidance on governance matters as well as escalation to line managers or use of HR or whistleblowing processes. (20/21 action)

		complies with the CIPFA statement on the role of the Chief Financial Officer (2016). • Effective Corporate Affairs and Audit Committee, internal audit and scrutiny arrangements in place, with members trained appropriately. • Policies in place for counter-fraud, bribery and corruption; complaints; procurement; and whistleblowing, and regularly reviewed. • Member standards arrangements and employee disciplinary procedures in place and updated regularly. • Proactive approach to equality and inclusion in place, engaging staff, acting on intelligence and reporting progress. The Council has engaged staff online (and offline for staff with no ICT access) during Covid using a variety of methods to support maintenance of a positive, inclusive culture.	

Local Code of Corporate Governance		Self-assessment	
Principle / supporting principles	**To meet these requirements, the Council will:**	**Evidence of compliance with this principle**	**Areas for improvement**
Ensuring openness and comprehensive stakeholder engagement. • Openness • Engaging comprehensively with institutional stakeholders • Engaging with individual citizens and service users effectively	• Document and operate a culture of openness and transparency within the organisation. • Maintain a culture of accountability, so that members and officers understand what they are accountable for and to whom they are accountable. • Consult appropriately with stakeholders on the development of its budget, key plans and service development. • Maintain effective decision making processes, ensuring that reports to decision makers clearly set out stakeholder views where relevant. • Publish all Executive and Committee reports and decision papers, unless there is a legitimate need to preserve confidentialities on the basis of the statutory tests. • Publish on its website information on the Council's strategies, plans and finances as well as on outcomes, achievements and challenges.	• Stated commitments to transparency within the Strategic Plan and supporting strategies such as the Information Strategy and annual SIRO Report. • Constitution and supporting documentation clearly set outs accountabilities and delegated authorities. • Consultation on Strategic Plan priorities; and annual budget consultation in place. • Corporate consultation and impact assessment policy in place (refreshed during 2020/21), ensuring that stakeholders (including third party providers) are engaged appropriately and views considered in decision making. • Committee diary planner published on an annual basis, approved by members and accessible via the Council's website. • Executive Forward Work Programme in place, setting out planned decisions in the coming four months on the online committee system. • All public Executive and Committee agendas, papers and minutes are published via the Council's website. Officer-delegated decisions are also published. • Virtual meeting solutions in place for Councillor meetings while Covid-19 restrictions are in force to ensure transparency around decision-making. • Key strategies and plans are clearly published on the Council's website / open data site, and regularly updated. • Information on performance and expenditure sent to all households annually as part of Council Tax billing. • The Council complies with Open Data requirements, publishing statutorily required and other datasets such as the Freedom of Information Act publication scheme on its open data site. The Council proactively seeks to publish information for which there is a demand.	• A robust officer scheme of delegations and sub-delegations is required to ensure effective, appropriate and timely taking of decisions that can be taken by officers.(20/21 action) • Action required to ensure understanding of the Equality Act and the impact assessment process, supplementing mandatory equality and inclusion training with refresher impact assessment training for key officers. (20/21 action) • Key Performance Indicators with targets will strengthen the Council's Strategic plan and increase transparency around the impact of actions on the achievement of aims within it. (21/22 action) • Work during 2021/22 has identified weaknesses in understanding across elements of the corporate governance framework. Refreshed training will ensure senior officers training encompasses the full suite of corporate governance disciplines. (20/21 action). • Work was undertaken to improve compliance with Freedom of Information and Subject Access Requests during 2021/22 to improve compliance. This continues to be monitored on a monthly basis by the Council's Leadership Management Team. • Completion of a review of the Constitution as part of the Council's Corporate Governance improvement journey.

		- Plans with the digital and marketing and communications strategies to advance in the current approach.	

Local Code of Corporate Governance		Self-assessment	
Principle / supporting principles	**To meet these requirements, the Council will:**	**Evidence of compliance with this principle**	**Areas for improvement**
Defining outcomes in terms of sustainable economic, social and environmental benefits. • Defining outcomes • Sustainable economic, social and environmental benefits	• Clearly set out its contribution to delivery of the Mayor's priorities for Middlesbrough, and use this as the basis for its overall strategy, planning and other decisions. • Define outcomes through robust consideration of appropriate evidence bases, such as the Joint Strategic Needs Assessment. • Ensure that it delivers defined outcomes on a sustainable basis within available resources. • Effectively identify and manage risks to the achievement of targeted outcomes. • Manage customer expectations effectively when determining priorities to make best use of resources, and ensure fair access to services.	• Strategic Plan and Directorate Priorities Plans in place which outline how the Council plans to deliver the Council's priorities for Middlesbrough, • Strategic Plan is part of the Council's policy framework – reports to decision makers set out how recommendations would impact on strategic objectives if approved. • Consultation on Strategic Plan priorities; and annual budget consultation in place. • Joint Strategic Needs Assessment and supporting assessments in place for children and young people – the children and young people's assessment was refreshed during 2017/18. Market position statements use needs assessments to inform commissioning priorities. • Corporate planning cycle considers targeted outcomes and annual budgeting over the medium-term within the context of the Council's Medium-Term Financial Plan and Capital Investment Strategy. • Performance, Risk and Programme and Project Management frameworks provide for regularly tracking of progress and addressing issues and risks, with reporting to members and senior managers as appropriate. • Customer Strategy and Charter in place, identifying what customers can expect from the Council, alongside specific service eligibility criteria.	• Key Performance Indicators with targets will strengthen the Council's Strategic plan and increase transparency around the impact of actions on the achievement of aims within it. (21/22 action) • Refresh the Joint strategic Needs Assessment (JSNA) for children and young people this year and complete the Adults and Older persons JSNA. (20/21 action) • Recent guidance on the conduct of local authority owned arm's length companies has been issued that Middlesbrough Development Company should be assessed against to ensure it is operating in line with it. (21/22 action)

Local Code of Corporate Governance		Self-assessment	
Principle / supporting principles	**To meet these requirements, the Council will:**	**Evidence of compliance with this principle**	**Areas for improvement**
Determining the interventions necessary to optimise the achievement of the intended outcomes. • Determining interventions • Planning interventions • Optimising achievement of intended outcomes	• Ensure reports to decision makers on services are fair, balanced, and analyse options and the risks associated with those options, to ensure Best Value is achieved. • Ensure that external and internal stakeholders are engaged with when the Council is determining how services should be planned and delivered, and the outcome of consultations is considered when decisions are made. • Ensure achievement of social value through service planning and commissioning. • Ensure that it has clear and robust planning and control cycles for its strategic and operational plans, priorities and targets. • Determine appropriate KPIs to demonstrate service and project performance, and provide members and senior managers with timely updates on these. • Ensure medium and long term resource planning is realistic, sustainable and inclusive. • Prepare budgets that are aligned to the strategic objectives of the organisation and its MTFP.	• Reports to decision makers developed using a standard format to ensure effective, fair, and evidence-based decision making. • Corporate consultation and impact assessment policy in place, ensuring that stakeholders engaged appropriately and views considered in decision making. • Guide to social value in procurement and commissioning in place. • Strategic Procurement Strategy in place. Contract management framework now also in place. • 'How to do Business with Middlesbrough Council' guidance for providers in place. • Annual reports to Corporate Affairs and Audit committee on disposals on the grounds of social value provided where appropriate. • Corporate planning cycle considers targeted outcomes and annual budgeting over the medium-term within the context of the Council's Medium-Term Financial Plan and capital Investment Strategy. • Performance, Risk and Programme and Project Management frameworks provide for regularly tracking of progress and addressing issues and risks, with reporting to members and senior managers as appropriate.	• A robust officer scheme of delegations and sub-delegations is required to ensure effective, appropriate, and timely taking of decisions that can be taken by officers. (20/21 action) • Transition to OPEN, the NEPO e-procurement system that is being put in place for the North East, replacing the current contract management framework with an end to end product once fully rollout. (20/21 action) • Recent guidance on the conduct of local authority owned arm's length companies has been issued that Middlesbrough Development Company should be assessed against to ensure it is operating in line with it. (21/22 action) • Key Performance Indicators with targets will strengthen the Council's Strategic plan and increase transparency around the impact of actions on the achievement of aims within it. (21/22 action)

Local Code of Corporate Governance		Self-assessment	
Principle / supporting principles	**To meet these requirements, the Council will:**	**Evidence of compliance with this principle**	**Areas for improvement**
Developing the Council's capacity, including the capability of its leadership and the individuals within it. • Developing the Council's capacity • Developing the capability of the Council's leadership and other individuals	• Regularly review operations to ensure that it is continuing to deliver services that are effective, including the use of benchmarking and sectoral research. • Work collaboratively and in partnerships where added value can be achieved. • Maintain an effective approach to organisational development to ensure continued capacity and capability to deliver. • Clearly define roles, responsibilities and terms of engagement for members and employees. • Maintain and regularly review its schemes of delegations that outline the types of decisions that are delegated and those that are reserved for collective decision-making. • Develop the capabilities of members and senior management to achieve effective shared leadership. • Ensure there are appropriate structures in place to encourage public participation. • Ensure that systems are in place to ensure that members and staff can be both held to account for performance, and supported as appropriate.	• Performance Management Policy set out how corporate performance will be managed. • Directorates review performance internally. Business intelligence dashboards are have been implemented to facilitate this. • Range of benchmarking and other tools are used within Directorates to contextual performance and drive improvement. • Wider Leadership Management Team in place to enable broader consideration of key policy issues. • Key strategic partnerships in place, such as the South Tees Health and Wellbeing Board. • The organisational development ambitions of the Council are embedded within the Strategic Plan which clearly outlines corporate approach to organisational development. • Constitution and supporting documentation clearly set out member and officer role profiles, relationship protocol and schemes of delegation. • Corporate consultation policy and online consultation portal in place. • Plans with the digital and marketing and communications strategies to advance in the current approach. • Processes in place for public involvement in determining scrutiny priorities, for the public to petition Council and to register questions to be considered by full Council. • Clear employee appraisal and development process and member development programme in place.	• A robust officer scheme of delegations and sub-delegations is required to ensure effective, appropriate and timely taking of decisions that can be taken by officers. (20/21 action) • The Council must continue on its improvement journey to address issues raised by OFSTED in relation to its safeguarding services for children to ensure all children are safe receive consistently good care that results in sustained improvement to their lives and their families lives. (20/21 action)

Local Code of Corporate Governance		Self-assessment	
Principle / supporting principles	**To meet these requirements, the Council will:**	**Evidence of compliance with this principle**	**Areas for improvement**
Managing risks and performance through robust internal control and strong public financial management. • Managing risk • Managing performance • Robust internal control • Managing data • Strong public financial management	• Embed a proportionate approach to risk management within all activities, ensure that progress is reviewed regularly and that risk is considered as part of decision making. • Ensure effective performance management of service delivery and provide members and senior managers with timely updates on service performance and progress towards outcomes. • Ensure reports to decision makers on services are fair, balanced, and analyse options and the risks associated with those options, to ensure Best Value is achieved. • Ensure effective, member-led scrutiny is in place that provides constructive challenge and debate on objectives and policies before, during and after decisions are taken. • Ensure an effective, risk-led Internal Audit service is in place to provide assurance on the overall adequacy and effectiveness of the Council's governance arrangements. • Ensure effective counter fraud and anti-corruption policies and arrangements are in place. • Ensure effective internal control arrangements exist for sound financial management. • Maintain an effective audit committee function. • Ensure effective arrangements are in place to collect, store, use and share data, including processes to safeguard personal data. • Put in place arrangements to ensure that data used to support decision-making is accurate and clear. • Ensure financial management arrangements support both long term outcome delivery and day-to-day operations.	• Performance Management; Risk and Opportunity Management; and Programme and Project Management policies provide for regularly tracking of progress and addressing issues and risks, with reporting to members and senior managers as appropriate. Risk is a standard section in reports to decision makers. • Reports to decision makers developed using a standard format to ensure effective, fair, and evidence-based decision making. • Wide-ranging annual scrutiny programme in place, examining policy and performance. • Urgent decision process and records in place and reported to Council annually. • Effective internal audit arrangement in place, utilising the Council's plans and risk registers to identify priorities. • Policy in place for counter-fraud, bribery and corruption; complaints; procurement; and whistleblowing, and regularly reviewed. Money Laundering Policy. • Effective Corporate Affairs and Audit committee in place clear terms of reference and a full and trained membership. • Information Strategy in place to provide systematic approach to information governance, including data protection and data quality. • Robust financial management procedures in place relating to medium-term financial planning, budget setting, procurement and contract management.	• A robust officer scheme of delegations and sub-delegations is required to ensure effective, appropriate and timely taking of decisions that can be taken by officers. (20/21 action) • Action required to ensure understanding of, and compliance with, procurement processes of the organisation. (21/22 action) • Assess and embed compliance with the Partnerships Governance policy. (21/22 action) • Limited assurance judgement from Internal Audit which will be addressed by the Corporate Governance Improvement Plan.

Local Code of Corporate Governance		**Self-assessment**	
Principle / supporting principles	**To meet these requirements, the Council will:**	**Evidence of compliance with this principle**	**Areas for improvement**
Implementing good practices in transparency, reporting, and audit to deliver effective accountability. • Implementing good practice in transparency • Implementing good practices in reporting • Assurance and effective accountability	• Provide reports in plain English wherever possible, ensuring that they are easy to access and interrogate and balancing transparency requirements with clarity. • Report regularly on performance, delivery of value for money and stewardship of resources. • Report on compliance with good governance principles within its Annual Governance Statement, including an action plan for continued improvement. • Ensure compliance with good governance principles extends to its partnership arrangements. • Ensure that recommendations made by external audit are addressed. • Ensure that the internal audit service has direct access to members to enable it to provide assurance with regard to governance arrangements. • Welcome and positively engage with peer challenges, reviews and inspections of its services.	• Standard template for reports to decision makers designed to advance proposition logically and simply, and reduce duplication of information. Training for report writers ongoing, including expectations around use of plain English. • Quarterly results reports to Executive and scrutiny covering performance, financial and risk updates. • Annual Governance Statement complying with the standard set out in the Local Code of Corporate Governance. • Governance arrangements in place for key strategic partnerships, such as the South Tees Health and Wellbeing Board, with improvement activity underway. • Recommendations made by external audit are addressed as a matter of priority through the most appropriate route. • Internal audit reports its plans, progress and findings regularly to the audit committee. Agreed actions from internal audit are tracked by DMTs until completion. • Council proactively seeks peer challenge, publishing findings and responses and commissioning follow-ups. There are positive relationships with statutory inspectorates and regulators.	• Assess and embed compliance with the Partnerships Governance policy. (21/22 action) • Action required to ensure understanding of the Equality Act and the impact assessment process, supplementing mandatory equality and inclusion training with refresher impact assessment training for key officers (20/21 action) • Key Performance Indicators with targets will strengthen the Council’s Strategic plan and increase transparency around the impact of actions on the achievement of aims within it. (21/22 action) • Provision of an independent Technical Advisor to the Corporate Affairs and Audit Committee to support challenge

Appendix 5: Corporate governance priorities for 2022/23

2020/21 AGS actions to be still delivered

Action	Lead officer	Deadline
Refreshed training approach to ensure senior officers training encompasses the full suite of corporate governance training.	Head of Human Resources and the Monitoring Officer	February 2023
Transition to OPEN, the NEPO e-procurement system that is being put in place for the North East, replacing the current contract management framework with an end to end product once fully rollout.	Head of Commissioning and Procurement	March 2023
Refresh training on the Equality Act and the impact assessment process, ensuring it is mandatory for key officers.	Head of Strategy, Information and Governance	March 2023
Complete mandatory refresher training on the officer and member protocol within Middlesbrough Council's constitution for all members and senior officers.	Monitoring Officer	March 2023
Continue to implement a scheme of sub-delegations where appropriate to further improve governance around officer delegated decisions.	Director of Legal and Governance Services	March 2023
Refresh the Joint strategic Needs Assessment (JSNA) for children and young people this year and complete the Adults and Older persons JSNA.	Director of Public Health with support from the Interim Head of Strategy, Information and Governance	March 2023

Actions identified within this 21/22 AGS for delivery in 2022/23

Issue	Action	Lead officer	Deadline
The 2020/21 AGS identified that while there were governance processes in place for the most part, there were control weaknesses that needed to be addressed. In particular that process identified there were concerns about Member to Member and Member to Officer relationships that needed to be addressed as a matter of urgency. The Council's External Auditors stated in its 2020/21 Value for Money judgement that the Council should 'develop a comprehensive Improvement Plan to address the cultural and relationship issues which exist within the Council as a matter of urgency. In our view it is the responsibility of all elected members and officers to work together to address these serious matters. This will require the involvement of external specialists as, in our view, the relationships within the Council have	Develop a Governance Improvement plan for noting by full Council during 2022/23 that identifies actions to improve the culture of the organisation and reflect detail of that plan within the final version of this document.	Chief Executive	Complete

Issue	Action	Lead officer	Deadline
deteriorated to a point which the Council will not be able to remedy on its own.'			
The 2020/21 Audit results report of the council's External auditors identified concern in relation to accurate declarations of interest. It stated 'Whilst we recognise that the responsibility to declare actual or potential conflicts of interest sits with members under both statute and the Council's Code of Conduct, given our observations we also recommend that management implement additional assurance checks over elected member declarations of interest, for example by cross-referencing to Companies House records or declarations made by elected members to other public bodies, to provide additional comfort over their completeness.'	The Council will undertake periodic spot checks on a risk-based basis at least three times a year of one or more Members' declarations during 2022/23 to assess whether there are ongoing compliance issues	Head of Democratic Services	March 2023
Within the 2020/21 Audit reports report External Auditors also recommended that Management should work with internal audit to ensure that where future pieces of work identify evidence of wider risks which are not immediately followed-up on, these are reported so that the Council's officers and the Corporate Affairs and Audit Committee can decide whether further investigation is appropriate	Management will work with Veritau to build the highlighting of identified wider risks into the audit reporting process. The reporting of these risks will then be built into regular Internal Audit updates to Corporate Affairs and Audit Committee	Section 151 Officer	The initial action has been completed but there is ongoing monitoring this as part of our monthly liaison meetings and Veritau will be addressing this action within their regular reports to Committee.
Within the 2020/21 audit results report it was identified that the Council's procurement processes required strengthening.	Updated e-learning training guides on procurement practice will be developed along with improved links through business partner relations with service directorates. Enhanced detail will be recorded on exemption forms following approvals. Procurement will also introduce a Best Value process to facilitate a smarter	Head of Commissioning and Procurement	March 2023

Issue	Action	Lead officer	Deadline
	procurement process for lower value procurement of goods and services		
Weaknesses in relation to the Council's recording of leasehold interests was identified by the Council's External Auditors as part of its assessment of the Council's control environment.	All leasehold interests are now recorded on the TF system with quarterly reviews matched against Delegated Approvals (DA) for any changes. A revised DA notification system is currently in development and will go live by end August 2022	Head of Commissioning and Procurement	Complete
It was identified during the development of the Partnership Governance Register that there were entities that would benefit from an appropriate governance framework.	Develop and implement a governance framework for wholly or partly owned Council companies that aligns with best practice guidance.	Interim Head of Strategy, Information and Governance	March 2023
Following completion of the first register and annual assurance report, it would be prudent to assess continued impact within the next annual review.	Assess and embed compliance with the Partnerships Governance policy.	Interim Head of Strategy, Information and Governance	September 2023
Whole Council response required to ensure that it responds effectively to the cost of living crisis impact on its budget position and its ability to meet increased demand for services	Complete a refresh of the Medium Term Financial Plan position to provide assurance to the organisation that there is good financial governance in place.	Chief Executive and Section 151 officer	February 2023
There are areas for improvement within the next refresh of the Council's Strategic Plan to ensure that it is better able to differentiate between actions the Council can deliver and actions to be delivered in partnership. Strengthened measures within the plan will also enable improved assessment of impact.	Ensure Key Performance Indicators with targets are embedded within the Council's Strategic plan when next refreshed. (21/22 action)	Interim Head of Strategy, Information and Governance Strategic Delivery Manager	September 2023

Middlesbrough Council

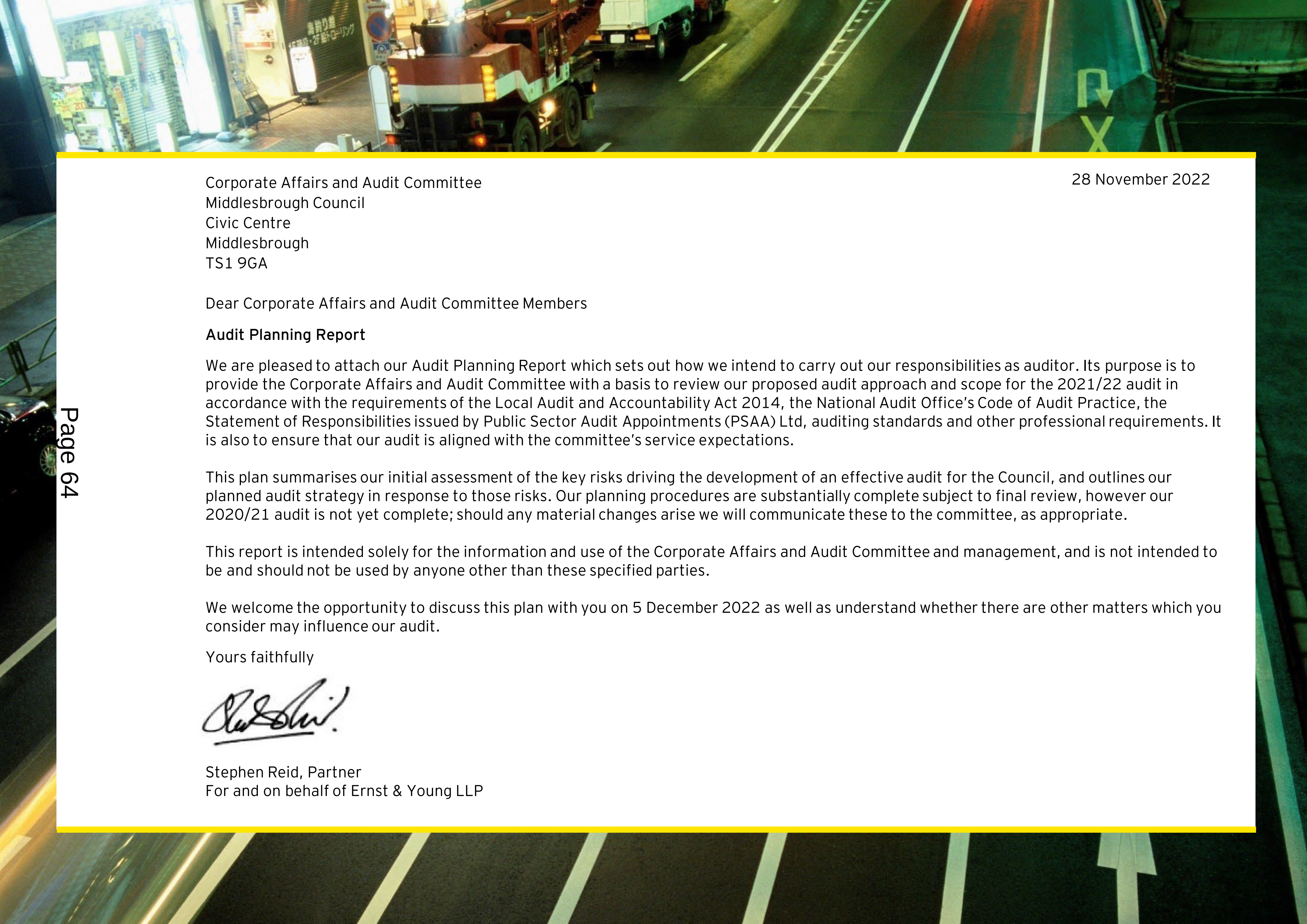
Audit Planning Report

Year ended 31 March 2022

November 2022

Agenda Item 8

Building a better working world



28 November 2022

Corporate Affairs and Audit Committee
Middlesbrough Council
Civic Centre
Middlesbrough
TS1 9GA

Dear Corporate Affairs and Audit Committee Members

Audit Planning Report

We are pleased to attach our Audit Planning Report which sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the Corporate Affairs and Audit Committee with a basis to review our proposed audit approach and scope for the 2021/22 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the committee's service expectations.

This plan summarises our initial assessment of the key risks driving the development of an effective audit for the Council, and outlines our planned audit strategy in response to those risks. Our planning procedures are substantially complete subject to final review, however our 2020/21 audit is not yet complete; should any material changes arise we will communicate these to the committee, as appropriate.

This report is intended solely for the information and use of the Corporate Affairs and Audit Committee and management, and is not intended to be and should not be used by anyone other than these specified parties.

We welcome the opportunity to discuss this plan with you on 5 December 2022 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Stephen Reid, Partner
For and on behalf of Ernst & Young LLP

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Public Sector Audit Appointments Ltd (PSAA) issued the "Statement of responsibilities of auditors and audited bodies". It is available from the PSAA website (https://www.psaa.co.uk/audit-quality/statement-of-responsibilities/).The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The "Terms of Appointment and further guidance (updated April 2018)" issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature.

This report is made solely to the Corporate Affairs and Audit Committee and management of Middlesbrough Council in accordance with the Statement of responsibilities. Our work has been undertaken so that we might state to the Corporate Affairs and Audit Committee and management of Middlesbrough Council those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Corporate Affairs and Audit Committee and management of Middlesbrough Council for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.

01

Overview of our 2021/22 audit strategy

Overview of our 2021/22 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Corporate Affairs and Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from prior year	Details
Risk of fraud in revenue and expenditure recognition	Fraud risk	No change in risk or focus	Under ISA 240, there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively.
Valuation of land and buildings	Significant risk	No change in risk, change in focus	Land and buildings are the most significant assets on the Council's Balance Sheet. The valuation of land and buildings is dependent upon a number of judgements and assumptions, small changes in which can have a significant impact upon the financial statements. In the previous year we attached this risk to investment property and assets held as assets under construction which would be classified as investment property once completed. During 2021/22, the Council acquired further assets which are valued on a similar basis but not classified as investment property. We therefore attach this risk for 2021/22 to all land and buildings valued at 'market value'.
Accounting for infrastructure assets	Significant risk	New risk	We expect to conclude our 2020/21 audit with a limitation of scope included in our audit report with regards to infrastructure assets, as the Council is unable to evidence that infrastructure assets have been appropriately derecognised when replaced. This is a sector-wide issue and amendments to the Council's reporting framework are anticipated before we will conclude our 2021/22 audit to provide a way forward without continuation of the limitation of scope for 2021/22.

Overview of our 2021/22 audit strategy

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from prior year	Details
Valuation of defined benefit pension liability	Inherent risk	No change in risk or focus	The defined benefit pension liability is the most significant liability on the Council's Balance Sheet. The assessment of the present value of future obligations requires detailed actuarial calculations. Small changes in the assumptions used for these calculations can have a significant impact upon the financial statements.
Member and senior officer relationships	Significant value for money risk	Risk evolved during 2021/22	As part of our 2020/21 audit, we reported significant weaknesses in the Council's arrangements to secure value for money during the year to 31 March 2021 arising from strained relationships between the Council's senior officers and elected members, and between elected members, and the impact of those on the effectiveness of the Council's governance processes. Whilst the Council is now taking steps to address these weaknesses, our reporting of them was delayed until July 2022 by the significance and complexity of these matters and the Council's Improvement Plan was not implemented until after the end of the 2021/22 financial year. Multiple stakeholders have highlighted further deterioration in relationships at the Council during 2021/22, as highlighted in the final version of the Council's Annual Governance Statement 2020/21. The Council also had 5 of the 7 members of its Executive resign in May 2021 for reasons connected to these weaknesses.
Provision of Children's Services	Significant value for money risk	No change in risk or focus	External inspections considered during our 2020/21 audit demonstrate that the Council is making positive progress with its Children's Services Improvement Plan, but also highlight that the plan is multi-year and the Council has more to do before its Children's Services can be considered as adequate in all regards. There therefore remains a risk that the Council did not have proper arrangements in place to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people within its children's social care services during 2021/22. We also note that the Council's Children's Services directorate consistently overspends against its allocated budget, generating an overspend of £8.3 million (21% of its budget) for 2021/22 prior to application of flexible capital receipts.

Overview of our 2021/22 audit strategy

In the prior year we also recognised the Council's disclosures around going concern as an inherent risk. Whilst the financial environment remains challenging for local authorities, the focus of our risk was on the uncertain impact of the Covid-19 pandemic on local authority finances. This is now much better understood by the Council and initial concerns of a significant adverse impact did not materialise. We do not therefore recognise a risk in this area for 2021/22 and will address as part of our required audit procedures.

Materiality

Planning materiality

£6.9m

Group materiality has been set at £6.9 million, which represents 1.5% of the gross expenditure on provision of services per the draft Statement of Accounts. We have decreased the threshold used for our materiality assessment from the 1.8% of gross expenditure used in the prior year due to the increased interest in the Council's Statement of Accounts as a result of the significant weaknesses in governance.

Performance materiality

£3.4m

Group performance materiality has been set at £3.4 million, which represents 50% of materiality. We have decreased the percentage of materiality used for performance materiality from 75% to 50% as the volume and size of misstatements identified in recent audits leads us to conclude there is a higher risk of undetected misstatement.

Audit differences

£0.3m

We will report all uncorrected misstatements relating to the primary statements (comprehensive income and expenditure statement, balance sheet, movement in reserves statement, cash flow statement and collection fund) greater than £0.3 million. The reporting threshold for the prior year's audit was £0.4m. Other misstatements identified will be communicated to the extent that they merit the attention of the Corporate Affairs and Audit Committee.

The Council has produced group financial statements for the first time for 2021/22. The production of group financial statements has not had a significant impact on our determination of materiality as the gross expenditure of the subsidiary, Middlesbrough Development Company, is small in relation to the Council.

Other matters

During our audit procedures performed to date, we have identified one instance where the Council has not acted in accordance with applicable laws and regulations which we wish to bring to the attention of the Corporate Affairs and Audit Committee:

- Local authorities which receive amounts under the Community Infrastructure Levy (CIL) are required by The Community Infrastructure Levy (Amendment) (England) (No. 2) Regulations 2019 to publish an annual Infrastructure Funding Statement by the 31 December following the end of each financial year. This requirement was introduced from the 2019/20 financial year, with the first Infrastructure Funding Statement due by 31 December 2020. The Council has not published Infrastructure Funding Statements for either the 2019/20 or 2020/21 financial years, and is therefore not complying with this requirement. Management have advised that they are intending to publish an Infrastructure Funding Statement by 31 December 2022 which will cover the 2019/20, 2020/21 and 2021/22 financial years, however we have not sought to assess whether this is an appropriate remedy under the governing legislation.

Overview of our 2021/22 audit strategy

Audit scope

This Audit Planning Report outlines the work that we plan to perform to provide you with our audit opinion on whether the consolidated and single entity financial statements of Middlesbrough Council (the Council) give a true and fair view of the financial position as at 31 March 2022 and of the income and expenditure for the year then ended.

We are also required to report by exception if we conclude that you have not put in place proper arrangements to secure value for money in your use of resources for the relevant period.

We will also review and report to the National Audit Office (NAO), to the extent and in the form required by them, on the Council's Whole of Government Accounts (WGA) return.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

- Strategic, operational and financial risks relevant to the financial statements;
- Developments in financial reporting and auditing standards;
- The quality of systems and processes;
- Changes in the business and regulatory environment; and
- Management's views on all of the above.

By considering these inputs, our audit is focused on the areas that matter and our feedback is more likely to be relevant to the Council.

Taking the above into account, and as articulated in this Audit Planning Report, our professional responsibilities require us to independently assess the risks associated with providing an audit opinion and undertake appropriate procedures in response to that. Our Terms of Appointment with PSAA allow them to vary the fee dependent on "the auditor's assessment of risk and the work needed to meet their professional responsibilities". PSAA are aware that the setting of scale fees has not kept pace with the changing requirements of external audit with increased focus on, for example, the valuations of land and buildings, the auditing of groups, the valuation of pension obligations, the introduction of new accounting standards such as IFRS 9 and 15 in recent years as well as the expansion of factors impacting the value for money conclusion. Therefore to the extent any of these or any other risks are relevant in the context of the Council's audit, we will discuss these with management as to the impact on the scale fee.

Effects of climate-related matters on financial statements and Value for Money arrangements

Public interest in climate change is increasing. We are mindful that climate-related risks may have a long timeframe and therefore while risks exist, the impact on the current period financial statements may not be immediately material to an entity. It is nevertheless important to understand the relevant risks to make this evaluation. In addition, understanding climate-related risks may be relevant in the context of qualitative disclosures in the notes to the financial statements and value for money arrangements.

We make inquiries regarding climate-related risks on every audit as part of understanding the entity and its environment. As we re-evaluate our risk assessments throughout the audit, we continually consider the information that we have obtained to help us assess the level of inherent risk.

02

Audit risks

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Risk of fraud in revenue and expenditure recognition*

Financial statement impact

Misstatements that occur in relation to the risk of fraud in revenue and expenditure recognition could affect the income and expenditure accounts. These accounts have the following balances in the draft 2021/22 financial statements:

- Income Account: £457 million
- Expenditure Account: £461 million

What is the risk?

Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

We have considered the income and expenditure streams of the Council and our assessment is that the risk is most prominent with regards to:

- Inappropriate recognition of Covid-related grant funding, including incorrect identification of whether the Council is acting as the principle or an agent and whether any associated terms and conditions were met prior to recognition;
- Inappropriate recognition of capital grants and contributions against revenue expenditure;
- Inappropriate capitalisation of revenue expenditure; and
- The omission of expenditure from the financial statements.

What will we do?

- Review the accounting treatment of Covid-related grants for 2021/22, including for consistency with their treatment in 2020/21, to confirm that they have been correctly accounted for as either a principle or agent arrangement;
- Test a sample of Covid-related grants to ensure that any terms and conditions were met prior to recognition as income;
- Test a sample of capital grants and contributions to confirm that they have been recognised in accordance with agreed terms and conditions;
- Test a sample of Revenue Expenditure Funded from Capital Under Statute (REFCUS) to confirm that it meets the criteria set down in governing regulations;
- Test a sample of capital additions to confirm they meet the criteria for capitalisation set out in accounting standards;
- Test samples of invoice postings and cash disbursements made after 1 April 2022 to confirm whether the expenditure to which they relate has been recorded in the correct reporting period; and
- Review minutes of Council and other key meetings to identify any potential accruals or provisions which may have been omitted from the financial statements.

Our response to significant risks

Misstatements due to fraud or error*

What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

What will we do?

- Identifying fraud risks during the planning stages of our audit;
- Inquire of management about risks of fraud and the controls put in place to address those risks;
- Understand the oversight given by those charged with governance of management's processes over fraud;
- Consider the effectiveness of management's controls designed to address the risk of fraud;
- Determine an appropriate strategy to address those identified risks of fraud; and
- Perform mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments made in the preparation of the financial statements, consideration of whether accounting estimates are free from material bias and a review for unusual transactions.

Our response to significant risks

Valuation of land and buildings

Financial statement impact

Misstatements that occur in relation to the risk of valuation of land and buildings could affect the property, plant and equipment and investment property accounts. These accounts have the following balances in the draft 2021/22 financial statements:

- Property, Plant and Equipment: £423 million
- Investment Property: £27 million

What is the risk?

Land and buildings are the most significant assets on the Council's Balance Sheet. The valuation of land and buildings is dependent upon a number of judgements and assumptions, small changes in which can have a significant impact upon the financial statements.

Our assessment is that the risk of misstatement is greatest in those assets whose value is dependent to a large extent on the existence and terms of commercial tenancies.

The number and value of such assets has increased in recent years as a result of acquisitions by the Council, including the Cleveland Centre during 2021/22.

We therefore attach our significant risk to the Council's investment property, including assets under construction which will be reclassified to investment property upon completion, and assets held as land and buildings which are valued on a 'market value' basis. We recognise an inherent risk over the valuation of other land and buildings.

What will we do?

- Consider the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work;
- Request our own valuation specialists undertake a review of higher risk valuations, including the valuations of the Cleveland Centre and Captain Cook Square;
- Sample test key asset information used by the valuers in performing their valuation (e.g. rental terms to support valuations based on rental income);
- Consider the annual cycle of valuations to ensure that assets have been valued within a five year rolling programme as required by the Code. We will also consider if there are any specific changes to assets that have occurred and whether these have been communicated to the valuer;
- Review assets not subject to valuation in 2021/22 to confirm that the remaining asset base is not materially misstated;
- Consider changes to useful economic lives as a result of the most recent valuation; and
- Test accounting entries have been correctly processed in the financial statements.

Our response to significant risks

Accounting for infrastructure assets

Financial statement impact

Misstatements that occur in relation to the risk of accounting for infrastructure assets could affect the property, plant and equipment account. Infrastructure assets had the following balance in the draft 2021/22 financial statements:

- Infrastructure assets: £134 million

What is the risk?

The Council's reporting framework requires that where an asset or component of an asset is replaced, the remaining value of the replaced asset or component is derecognised.

The Council's accounting records for infrastructure assets are not sufficiently detailed to allow identification of individual assets or components. Consequently the Council has not derecognised replaced infrastructure assets or components since the current reporting framework requirement were adopted in 2010. The Council is also unable to quantify the impact of not derecognising such assets or components on the financial statements.

Our audit report for 2020/21 will include a limitation of scope with regards to infrastructure assets as we were unable to determine whether a material misstatement of infrastructure assets existed.

The Council is not the only local authority which has not maintained sufficiently detailed records of infrastructure assets, and modifications to the Council's reporting framework are expected during the course of the audit to enable a 'reset' of infrastructure assets accounting by local authorities which will enable us to conclude on whether a material misstatement exists.

What will we do?

Our response to this risk will depend upon the precise nature of the changes to the Council's reporting framework which are still to be made, but are likely to include

- Reviewing management's assessment of how the revised reporting framework impacts the Council's financial statements, including any required financial statement disclosures or adjustments;
- Considering whether the Council is able to demonstrate material compliance with the revised reporting framework;
- Reviewing any revised financial statement balances or disclosures for consistency with the reporting framework; and
- Evaluating whether, under the revised framework, we are able to conclude on whether a material misstatement exists within the Council's financial statements.

Other areas of audit focus

What is the risk/area of focus?	What will we do?
Valuation of defined benefit pension liability The Local Authority Accounting Code of Practice and IAS 19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by the Council. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. Per the draft financial statements, the Council's net pension liability was £232 million at 31 March 2022. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. The information disclosed is based on the IAS 19 report issued to the Council by the Council's actuary. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	‣ Liaise with the audit team of the Teesside Pension Fund, to obtain assurances over the information supplied to the actuary in relation to the Council. Note that the audit of the Pension Fund is also performed by EY; ‣ Assess the work of the Pension Fund actuary (Hymans Robertson), including the assumptions they have used, by relying on the work of PWC - Consulting Actuaries commissioned by the National Audit Office for all Local Government sector auditors, and considering any relevant reviews by our own EY actuarial specialists; ‣ Request our own pension specialists perform an independent roll-forward of the Council's pension liabilities from 31 March 2021 to 31 March 2022 and assess the consistency of that exercise with the Council's own valuation; and ‣ Review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS 19.

03 Value for money risks

Value for money risks

Council responsibilities for value for money

The Council is required to maintain an effective system of internal control that supports the achievement of its policies, aims and objectives while safeguarding and securing value for money from the public funds and other resources at its disposal.

As part of the material published with its financial statements, the Council is required to bring together commentary on its governance framework and how this has operated during the period in a governance statement. In preparing its governance statement, the Council tailors the content to reflect its own individual circumstances, consistent with the requirements of the relevant accounting and reporting framework and having regard to any guidance issued in support of that framework. This includes a requirement to provide commentary on its arrangements for securing value for money from their use of resources.

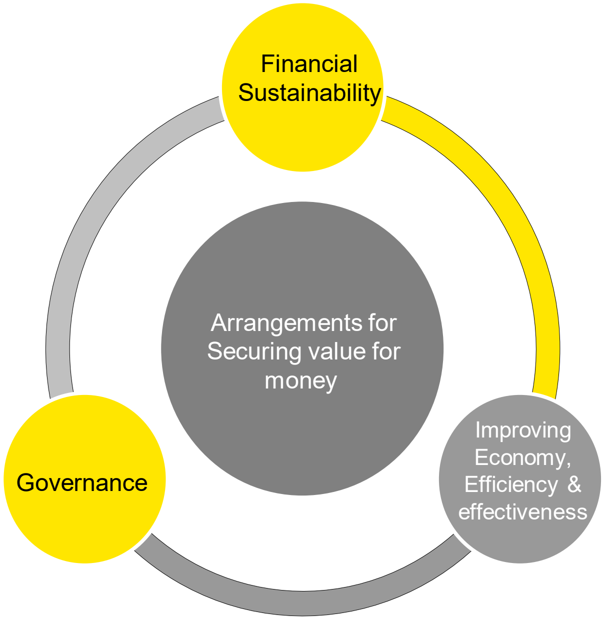
Auditor responsibilities

Under the Code of Audit Practice we are required to consider whether the Council has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness on its use of resources. However, since the Code of Audit Practice was updated in 2020 there is no longer an overall evaluation criterion which we need to conclude on.

Instead the 2020 Code requires the auditor to design their work to provide them with sufficient assurance to enable them to report to the Council a commentary against specified reporting criteria (see below) on the arrangements the Council has in place to secure value for money through economic, efficient and effective use of its resources for the relevant period.

The specified reporting criteria are:

- **Financial sustainability**
  How the Council plans and manages its resources to ensure it can continue to deliver its services;
- **Governance**
  How the Council ensures that it makes informed decisions and properly manages its risks; and
- **Improving economy, efficiency and effectiveness**
  How the Council uses information about its costs and performance to improve the way it manages and delivers its services.



Value for money risks

Planning and identifying VFM risks

The NAO's guidance notes require us to carry out a risk assessment which gathers sufficient evidence to enable us to document our evaluation of the Council's arrangements, in order to enable us to draft a commentary under the three reporting criteria. This includes identifying and reporting on any significant weaknesses in those arrangements and making appropriate recommendations.

In considering the Council's arrangements, we are required to consider:

- The Council's governance statement;
- Evidence that the Council's arrangements were in place during the reporting period;
- Evidence obtained from our work on the accounts;
- The work of inspectorates (such as Ofsted) and other bodies; and
- Any other evidence source that we regard as necessary to facilitate the performance of our statutory duties.

We then consider whether there is evidence to suggest that there are significant weaknesses in arrangements. The NAO's guidance is clear that the assessment of what constitutes a significant weakness and the amount of additional audit work required to adequately respond to the risk of a significant weakness in arrangements is a matter of professional judgement. However, the NAO states that a weakness may be said to be significant if it:

- Exposes – or could reasonably be expected to expose – the Council to significant financial loss or risk;
- Leads to – or could reasonably be expected to lead to – significant impact on the quality or effectiveness of service or on the Council's reputation;
- Leads to – or could reasonably be expected to lead to – unlawful actions; or
- Identifies a failure to take action to address a previously identified significant weakness, such as failure to implement or achieve planned progress on action/improvement plans.

We should also be informed by a consideration of:

- The magnitude of the issue in relation to the size of the Council;
- Financial consequences in comparison to, for example, levels of income or expenditure, levels of reserves (where applicable), or impact on budgets or cashflow forecasts;
- The impact of the weakness on the Council's reported performance;
- Whether the issue has been identified by the Council's own internal arrangements and what corrective action has been taken or planned;
- Whether any legal judgements have been made, including judicial review;
- Whether there has been any intervention by a regulator or Secretary of State;
- Whether the weakness could be considered significant when assessed against the nature, visibility or sensitivity of the issue;
- The impact on delivery of services to local taxpayers; and
- The length of time the Council has had to respond to the issue.

Value for money risks

Responding to identified risks

Where our planning work has identified a risk of significant weakness, the NAO's guidance requires us to consider what additional evidence is needed to determine whether there is a significant weakness in arrangements and undertake additional procedures as necessary, including where appropriate, challenge of management's assumptions. We are required to report our planned procedures to the Corporate Affairs and Audit Committee.

Reporting on VFM

In addition to the commentary on arrangements, where we are not satisfied that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources we are required by the Code of Audit Practice to refer to this by exception in the audit report on the financial statements.

The Code of Audit Practice also states that the commentary should be clear, readily understandable and highlight any issues we wish to draw to the attention of the Council or the wider public. This should include details of any recommendations arising from the audit and follow-up of recommendations issued previously, along with our view as to whether they have been implemented satisfactorily.

Status of our 2021/22 VFM work

As part of our 2020/21 audit, we reported significant weaknesses in the Council's arrangements to secure value for money during the year to 31 March 2021 arising from strained relationships between the Council's senior officers and elected members, and between elected members, and the impact of those on the effectiveness of the Council's governance processes. Whilst the Council is now taking steps to address these weaknesses, our reporting of them was delayed until July 2022 by the significance and complexity of these matters and the Council's Improvement Plan was not implemented until after the end of the 2021/22 financial year.

Our value for money assessment is primarily focused on the arrangements of the Council during the period under audit, however there is also a requirement under the Code of Audit Practice for auditors to report known significant weaknesses in a timely manner. Our value for money work will therefore consist of a combination of our assessment of the arrangements of the Council during the period under audit, 1 April 2021 to 31 March 2022, and the Council's response to the significant weaknesses and recommendations reported as part of the 2020/21 audit. We are still considering the impact of this multi-year circumstance on our auditor reporting.

Our response to risks of significant weaknesses in arrangements

Member and senior officer relationships

What is the risk?

As part of our 2020/21 audit, we reported significant weaknesses in the Council's arrangements to secure value for money during the year to 31 March 2021 arising from strained relationships between the Council's senior officers and elected members, and between elected members, and the impact of those on the effectiveness of the Council's governance processes.

We observed that these strained relationships were a contributing factor in the respective roles and responsibilities of officers and members not being adhered to in the execution of Council policies and procedures.

We reported that in our view, these were serious matters indicative of deep rooted cultural and relationship issues at the Council which required urgent action.

Multiple stakeholders have highlighted further deterioration in relationships at the Council during 2021/22, including as highlighted in the final version of the Council's Annual Governance Statement 2020/21. The Council also had 5 of the 7 members of its Executive resign in May 2021 for reasons connected to these weaknesses.

Whilst the Council is now taking steps to address these weaknesses, our reporting of them was delayed until July 2022 by the significance and complexity of these matters and the Council's Improvement Plan was not implemented until after the end of the 2021/22 financial year.

There is therefore a significant risk that these matters continued to have an adverse impact on the effectiveness of the Council's governance processes during 2021/22.

What will we do?

- We discussed the relationships within the Council with stakeholders throughout 2021/22 as part of our 2020/21 audit work which was ongoing at the time. We will hold further discussions with management, and other stakeholders as appropriate, as part of our 2021/22 audit to confirm our understanding of these, and any impacts upon the Council's governance processes.
- Consider our own observation from direct interactions with officers and members, and from attendance at meetings of the Corporate Affairs and Audit Committee;
- Make enquiries of management, and review reports presented to full Council and the Improvement Board, to understand the Council's progress against the Improvement Plan; and
- Evaluate whether the above indicates that material weaknesses in arrangements were present during 2021/22, and consider the implications for our auditor reporting.

In addition, we note that we continue to receive a high volume of correspondence with regards to the Council. Much of this correspondence is directly or indirectly linked to the significant weaknesses in arrangements we have previously reported.

We consider such correspondence as information brought to our attention for the purposes of our value for money assessment and, where appropriate, design additional procedures to respond to any risks raised by our consideration of that information.

Our response to risks of significant weaknesses in arrangements

Provision of Children's Services

What is the risk?

On 24 January 2020, the Office for Standards in Education, Children's Services and Skills (Ofsted) released the results of its inspection of the Council's children's social care services performed between 25 November 2019 and 6 December 2019. The report concluded that the quality of the Council's children's services had deteriorated since the previous inspection in 2015 and were now inadequate.

Following publication of the Ofsted report, management developed an Improvement Plan to address the findings raised by Ofsted.

The appointed Commissioner for Children's Services in Middlesbrough issued a 12-month review of the Council's progress against the Improvement Plan in July 2021, covering the period to May 2021. This review noted that "considerable progress has been made and there is evidence of real impact" and recommended that the Council be allowed to retain control of its Children's Services.

The report did however note that the Council's Improvement Plan remains a multi-year exercise and, whilst good progress is being made, the Council has more to do before its Children's Services can be considered as adequate in all regards.

We also note that the Council's Children's Services directorate consistently overspends against its allocated budget, generating an overspend of £8.3 million (21% of its budget) for 2021/22 prior to application of flexible capital receipts.

There therefore remains a risk that the Council did not have proper arrangements in place to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people within its children's social care services during 2021/22.

Given the significance of children's services to the Council's activities and the nature of the original conclusions reached by Ofsted, we consider it appropriate to recognise a significant value for money risk in respect of the delivery of children's services.

What will we do?

- Make enquiries of management to understand the further progress being made against the Council's Improvement Plan;
- Review the findings of any subsequent monitoring inspections of the Council's children's services as third party evidence of the progress being made by the Council;
- Enquire of management as to the reasons for recurring overspends within Children's Services and the steps taken by the Council to reduce and/or mitigate these; and
- Evaluate whether the above indicates that a material weakness in arrangements was present during 2021/22, and consider the implications for our auditor reporting.

04

Audit materiality

Materiality

Group materiality

For planning purposes, Group materiality for 2021/22 has been set at £6.9 million. This represents 1.5% of the gross expenditure on provision of services per the draft Statement of Accounts. It will be reassessed throughout the audit process. We have provided supplemental information about audit materiality in Appendix C.

We have decreased the threshold used for our materiality assessment from the 1.8% of gross expenditure on the provision of services used in the prior year due to the increased interest in the Council's Statement of Accounts as a result of the significant weaknesses in governance.

Gross expenditure on provision of services
£461m

Planning materiality
£6.9m

Performance materiality
£3.4m

Subsidiary performance materiality
£0.7m

Audit differences
£0.35m

Specific materiality
£1,000
Remuneration disclosures

Prior year materiality

£438m

£7.9m

£5.9m

£0.4m

We request that the Corporate Affairs and Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

Key definitions

Planning materiality – The amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

Performance materiality – The amount we use to determine the extent of our audit procedures. We have set performance materiality at £3.4 million which represents 50% of Group materiality (rounded).

Audit difference threshold – This has been set as £0.35 million. We propose that misstatements identified below this threshold are deemed clearly trivial. The same threshold for misstatements is used for component reporting. We will report to you all uncorrected misstatements over this amount relating to the comprehensive income and expenditure statement, balance sheet, housing revenue account and collection fund that have an effect on income or that relate to other comprehensive income.

Other uncorrected misstatements, such as reclassifications and misstatements in the cashflow statement or disclosures and corrected misstatements will be communicated to the extent that they merit the attention of the Corporate Affairs and Audit Committee, or are important from a qualitative perspective.

Subsidiary performance materiality – we determine component performance materiality as a percentage of Group performance materiality based on the risk and relative size to the Group of each component. We set performance materiality for the Council as a single entity at the same as Group performance materiality. We set performance materiality for Middlesbrough Development Company at £0.7m.

Specific materiality – We have set a materiality of £1,000 for reporting differences in remuneration disclosures which reflects our understanding of the interest of these areas to the users of the financial statements. We do not apply a specific lower materiality to the audit of related party transactions disclosures, however we do consider the materiality of transactions as they apply to both parties involved, rather than just to the Council.

05

Scope of our audit

Our Audit Process and Strategy

Objective and scope

Under the Code of Audit Practice, our principal objectives are to review and report on the Council's financial statements and arrangements for securing economy, efficiency and effectiveness in its use of resources to the extent required by the relevant legislation and the requirements of the Code.

We issue an audit report that covers:

1. **Financial statement audit**

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK).

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Procedures required by standards

- Addressing the risk of fraud and error;
- Significant disclosures included in the financial statements;
- Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- Auditor independence.

Procedures required by the Code

- Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance Statement; and
- Reviewing and reporting on the Whole of Government Accounts return, in line with the instructions issued by the NAO.

2. Arrangements for securing economy, efficiency and effectiveness (value for money)

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources.

Our Audit Process and Strategy

Audit Process Overview

Our audit involves:

- Identifying and understanding the key processes and internal controls; and
- Substantive tests of detail of transactions and amounts.

For 2021/22 we plan to follow a substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

Analytics

We will use our computer-based analytics tools to enable us to capture and analyse the entirety of the Council's general ledger. These tools:

- Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- Give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Corporate Affairs and Audit Committee.

Internal audit

We will meet with Internal Audit, and review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit plan, where they raise issues that could have an impact on the financial statements.

Group audit approach

The Middlesbrough Council group consist of two components, Middlesbrough Council and Middlesbrough Development Company.

We designate Middlesbrough Council as a full scope component, which means that we perform a full audit of this component. As our opinion covers the consolidated group financial information and the Council's single-entity financial information, we perform our procedures to a materiality level appropriate for the component as well as the group.

We designate Middlesbrough Development Company as a specific scope component, and focus our audit procedures on the component's non-current assets as the only balance within the component which is material to the group. Our approach to this component is to directly test material component balances ourselves and, as we are not the external auditor of Middlesbrough Development Company, we use a materiality level appropriate to our group opinion.

The Council did not produce group statements in the prior year, therefore we did not have a group audit approach in the prior year.

The significant risks identified in section 2 are applicable to the Council as a single-entity only, other than the presumed risk of misstatements due to fraud or error which is applicable to both components.

06

Audit team

Audit team

The engagement team is led by Stephen Reid, who will have responsibility for ensuring that our audit delivers high quality and value to the Council.

Mark Rutter will be the senior manager responsible for the day-to-day direction of audit work and is the key point for contact for the finance team.

When auditing key judgements, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where either EY or third party specialists provide input for the current year audit are:

Area	Specialists
Valuation of land and buildings	Align (management's valuation specialists) EY Real Estate valuation specialists (as auditor's specialists)
Pensions disclosures	Hymans Robertson (management's actuarial specialists) PWC (who undertake work in respect of management's specialists under a national programme overseen by the National Audit Office) EY Actuaries (as auditor's specialists)

In accordance with auditing standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Council's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- Analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- Assess the reasonableness of the assumptions and methods used;
- Consider the appropriateness of the timing of when the specialist carried out the work; and
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

Developing the right audit culture

In July 2021, EY established a UK Audit Board (UKAB) with a majority of independent Audit Non-Executives (ANEs). The UKAB will support our focus on delivering high-quality audits by strengthening governance and oversight over the culture of the audit business. This focus is critical given that audit quality starts with having the right culture embedded in the business.

Our audit culture is the cement that binds together the building blocks and foundation of our audit strategy. We have been thoughtful in articulating a culture that is right for us: one that recognises we are part of a wider, global firm and is clear about whose interests our audits serve.

There are three elements underpinning our culture:

1. Our people are focused on a **common purpose**. It is vital we foster and nurture the values, attitudes and behaviours that lead our people to do the right thing.
2. The essential attributes of our audit business are:
    - **Right resources** – We team with competent people, investing in audit technology, methodology and support
    - **Right first time** – Our teams execute and review their work, consulting where required to meet the required standard
    - **Right reward** – We align our reward and recognition to reinforce the right behaviours
3. The six pillars of **Sustainable Audit Quality** are implemented.

01 **Tone at the top**

The internal and external messages sent by EY leadership, including audit partners, set a clear tone at the top - they establish and encourage a commitment to audit quality

02 **Exceptional talent**

Specific initiatives support EY auditors in devoting time to perform quality work, including recruitment, retention, development and workload management

03 **Accountability**

The systems and processes in place help EY people take responsibility for carrying out high-quality work at all times, including their reward and recognition

04 **Audit technology and digital**

The EY Digital Audit is evolving to set the standard for the digital-first way of approaching audit, combining leading-edge digital tools, stakeholder focus and a commitment to quality

05 **Simplification and innovation**

We are simplifying and standardising the approach used by EY auditors and embracing emerging technologies to improve the quality, consistency and efficiency of the audit

06 **Enablement and quality support**

How EY teams are internally supported to manage their responsibility to provide high audit quality

A critical part of this culture is that our people are **encouraged and empowered to challenge and exercise professional scepticism** across all our audits. However, we recognise that creating a culture requires more than just words from leaders. It has to be reflected in the lived experience of all our people each and every day enabling them to challenge themselves and the companies we audit.

Each year we complete an audit quality culture assessment to obtain feedback from our people on the values and behaviours they experience, and those they consider to be fundamental to our audit quality culture of the future. We action points that arise to ensure our culture continues to evolve appropriately.

2021 Audit Culture Survey result
A cultural health score of 78% (73%) was achieved for our UK Audit Business

We bring our culture alive by investing in three priority workstreams:

- Audit Culture with a focus on professional scepticism
- Adopting the digital audit
- Standardisation

This investment has led to a number of successful outputs covering training, tools, techniques and additional sources. Specific highlights include:

- Audit Purpose Barometer
- Active Scepticism Framework
- Increased access to external sector forecasts
- Forensic risk assessment pilots
- Refreshed PLOT training and support materials, including embedding in new hire and trainee courses
- Digital audit training for all ranks
- Increased hot file reviews and improved escalation processes
- New work programmes issued on auditing going concern, climate, impairment, expected credit losses, cashflow statements and conducting effective group oversight
- Development of bite size, available on demand, task specific tutorial videos

> *"A series of company collapses linked to unhealthy cultures…..have demonstrated why cultivating a healthy culture, underpinned by the right tone from the top, is fundamental to business success."*
>
> Sir John Thompson
> Chief Executive of the FRC

07

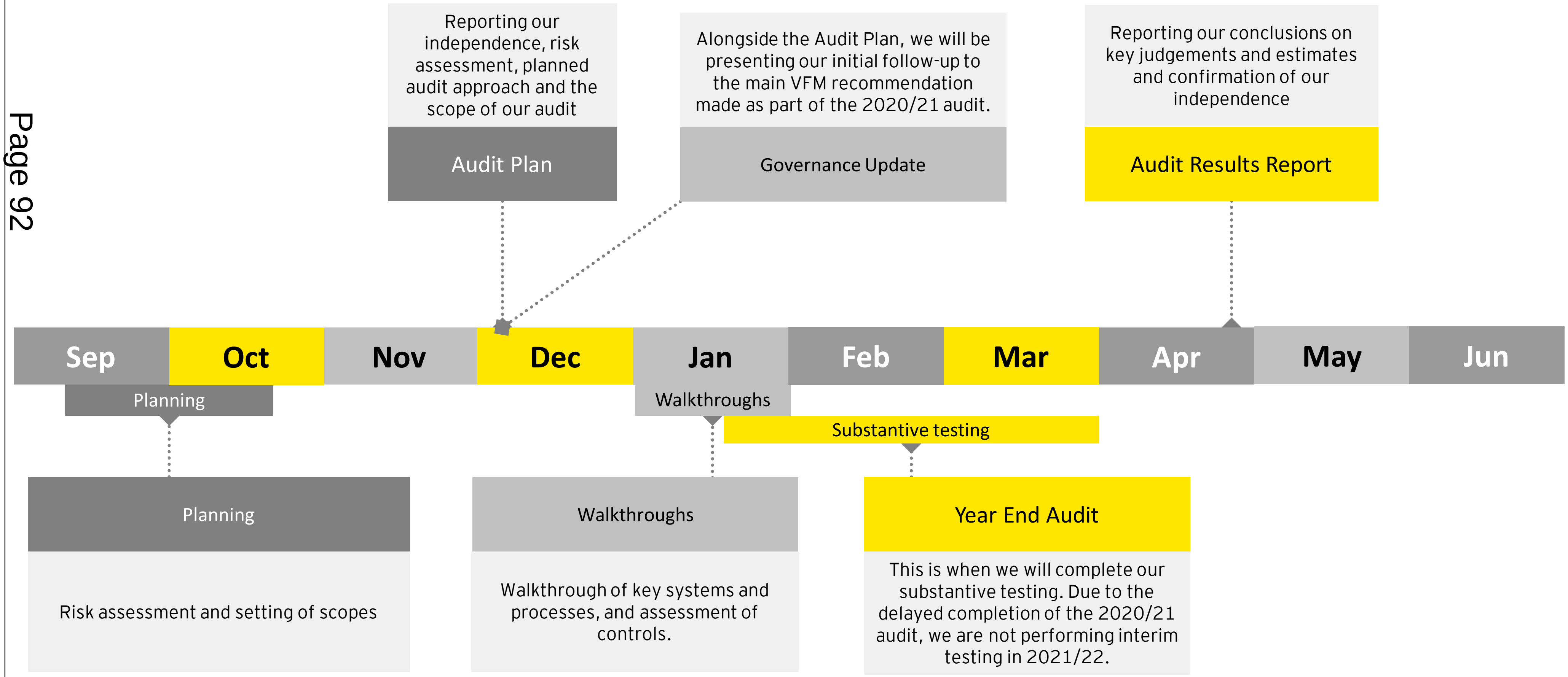
Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2021/22.

From time to time matters may arise that require immediate communication with the Corporate Affairs and Audit Committee and we will discuss them with the Corporate Affairs and Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.



Audit Plan

Reporting our independence, risk assessment, planned audit approach and the scope of our audit

Governance Update

Alongside the Audit Plan, we will be presenting our initial follow-up to the main VFM recommendation made as part of the 2020/21 audit.

Audit Results Report

Reporting our conclusions on key judgements and estimates and confirmation of our independence

Planning

Risk assessment and setting of scopes

Walkthroughs

Walkthrough of key systems and processes, and assessment of controls.

Year End Audit

This is when we will complete our substantive testing. Due to the delayed completion of the 2020/21 audit, we are not performing interim testing in 2021/22.

08

Independence

Introduction

The FRC Ethical Standard and ISA (UK) 260 "Communication of audit matters with those charged with governance", requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in December 2019, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	**Final stage**
▸ The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between you, your affiliates and directors and us; ▸ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review; ▸ The overall assessment of threats and safeguards; ▸ Information about the general policies and processes within EY to maintain objectivity and independence; and ▸ Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard.	▸ In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed; ▸ Details of non-audit services provided and the fees charged in relation thereto; ▸ Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us; ▸ Written confirmation that all covered persons are independent; ▸ Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy; ▸ Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and ▸ An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted.

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, are disclosed.

Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non-audit services if the service has been pre-approved in accordance with your policy.

Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Stephen Reid, your audit engagement partner, and the audit engagement team have not been compromised.

Self interest threats

A self interest threat arises when EY has financial or other interests in your Council. Examples include where we have an investment in related companies; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees, non-audit fees or business relationships and therefore no additional safeguards are required.

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 4.

There are no other self interest threats at the date of this report.

Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no self review threats at the date of this report.

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of your council. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work.

There are no management threats at the date of this report.

Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

Relationships, services and related threats and safeguards

EY Transparency Report 2022

Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the period ended 1 July 2022:

EY UK 2022 Transparency Report | EY UK

09 Appendices

Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Levelling Up, Housing and Communities. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the requirements of the Code of Audit Practice and supporting guidance published by the National Audit Office, the financial reporting requirements set out in the Code of Practice on Local Authority Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.

Description	Planned Fee 2021/22 £	Scale Fee 2021/22 £	Estimated Requested Fee 2020/21 £	*Notes*
Base Audit Fee – Code Work (Council)	88,578	88,578	88,578	*1*
Base Audit Fee – Code Work (Pension Fund)	21,972	21,972	21,972	*1*
Changes in work required to address professional and regulatory requirements and scope associated with risk (Council)	102,312	N/A	81,850	*2, 3*
Changes in work required to address professional and regulatory requirements and scope associated with risk (Pension Fund)	49,199	N/A	39,359	*2, 3*
Revised Proposed Scale Fee	**262,061**	**110,550**	**231,759**	
IAS 19 Procedures – Code Work (Pension Fund)	9,250	N/A	8,500	*4*
Revised Proposed Scale Fee (inc. IAS 19 Procedures)	**271,311**	**110,550**	**240,259**	
Additional specific one-off considerations requiring additional work (Council)	TBC	N/A	148,000	*5, 6*
Additional specific one-off considerations requiring additional work (Pension Fund)	TBC	N/A	5,000	*5, 6*
Total Audit Fee	**TBC**	**110,550**	**393,259**	
Non-Audit Fee – Housing Benefit Certification Work	14,800	N/A	13,450	*7*
Non-Audit Fee – Teachers' Pension Certification Work	5,850	N/A	5,250	*7*
Total Fees	**TBC**	**110,550**	**411,959**	

All fees exclude VAT

Fees

Notes

1) The base audit fees reflect the amounts determined by Public Sector Audit Appointments Limited (PSAA) in March 2020 and applied to subsequent years.
2) We wrote to management and the Corporate Affairs and Audit Committee Chair on 10 February 2020 setting out our considerations on the sustainability of UK local public audit. We have not been able to agree a scale fee variation with management and will therefore asked PSAA to make a determination as to the scale fee variation to be applied once our 2020/21 audit is concluded. The table on the previous page reflects the amount we intend to submit to PSAA as our assessment of the additional fee required to reflect changes in the level of work required to address professional and regulatory requirements and scope associated with risk.
3) We determine our assessment of the additional fee required to reflect changes in the level of work required to address professional and regulatory requirements and scope associated with risk in reference to hourly rates set by PSAA. PSAA have increased these rates by 25% since we determined the amounts for our 2020/21 audit.
4) As part of our audit of the Pension Fund we undertake additional procedures to enable us to report to the auditors of scheduled bodies that are subject to the NAO Code of Audit Practice. These procedures are additional to the procedures we must complete to support our opinion on the financial statements of the Pension Fund. Management may opt to recharge this fee to the relevant member bodies.
5) Where we identified significant risks and other areas of audit focus as part of our 2020/21 audits, as reported to the Corporate Affairs and Audit Committee, we undertook additional procedures to obtain the appropriate levels of evidence to support our opinion. For 2020/21, this included an exceptional level of audit effort to address the additional risk of significant weakness relating to member and senior officer relationships reported in the 2020/21 Audit Results Report which, due to its nature, has had to be performed by the most senior members of the audit team. Audit resources have also been required to respond to a very high level of correspondence we received during the course of the 2020/21 audit. The amounts of £148,000 for the Council and £5,000 for the Pension Fund represents our current estimate of the additional fees we have determined as commensurate with the additional work undertaken, however until our 2020/21 audits are concluded further procedures may be required.
6) We note that there continue to be factors which increase the extent of our audit procedures over and above the levels envisaged by PSAA when determining scale fees. For 2021/22, this will include the production of group accounts consolidating Middlesbrough Development Company, the increasing complexity of the Council's property portfolio, changes made in the NAO's revised 2020 Code of Audit Practice and the implications of the revised Code for our value for money work and the adoption of a new auditing standard *ISA 540: Auditing Accounting Estimates and Related Disclosures* which requires us to perform addition work around accounting estimates. Significant audit effort is also likely to be necessary to respond to the significant value for money risks reported in section 3 and the high levels of correspondence we are continuing to receive in relation to our audit. We will discuss the impact of these factors on our audit fees with management once the full extent of additional effort has been determined.
7) Our fees for the 2021/22 certification work are still to be agreed with management. The amounts presented are our initial estimate based on the work involved.

The fees presented are based on the following assumptions:

- Officers meeting the agreed timetable of deliverables;
- Our accounts opinion being unqualified;
- No material weaknesses in arrangements for us to report on;
- Appropriate quality of documentation is provided by the Council; and
- The Council has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

Required communications with the Corporate Affairs and Audit Committee

We have detailed below the communications that we must provide to the Corporate Affairs and Audit Committee.

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Terms of engagement	Confirmation by the Corporate Affairs and Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The Statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter	The Statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit Planning Report (this report)
Significant findings from the audit	• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures; • Significant difficulties, if any, encountered during the audit; • Significant matters, if any, arising from the audit that were discussed with management; • Written representations that we are seeking; • Expected modifications to the audit report; and • Other matters if any, significant to the oversight of the financial reporting process	Audit Results Report (April 2023)

Appendix B

Required communications with the Corporate Affairs and Audit Committee

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: • Whether the events or conditions constitute a material uncertainty; • Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements; and • The adequacy of related disclosures in the financial statements	Audit Results Report (April 2023)
Misstatements	• Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation; • The effect of uncorrected misstatements related to prior periods; • A request that any uncorrected misstatement be corrected; • Corrected misstatements that are significant; and • Material misstatements corrected by management	Audit Results Report (April 2023)
Fraud	• Enquiries of the Corporate Affairs and Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity; • Any fraud that we have identified or information we have obtained that indicates that a fraud may exist; and • A discussion of any other matters related to fraud	Audit Results Report (April 2023)
Related parties	• Significant matters arising during the audit in connection with the entity's related parties including, when applicable: • Non-disclosure by management; • Inappropriate authorisation and approval of transactions; • Disagreement over disclosures; • Non-compliance with laws and regulations; and • Difficulty in identifying the party that ultimately controls the entity	Audit Results Report (April 2023)

Required communications with the Corporate Affairs and Audit Committee

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence. Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: • The principal threats; • Safeguards adopted and their effectiveness; • An overall assessment of threats and safeguards; and • Information about the general policies and process within the firm to maintain objectivity and independence	Audit Planning Report (this report); and Audit Results Report (April 2023)
External confirmations	• Management's refusal for us to request confirmations; and • Inability to obtain relevant and reliable audit evidence from other procedures	Audit Results Report (April 2023)
Consideration of laws and regulations	• Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off; and • Enquiry of the Corporate Affairs and Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Corporate Affairs and Audit Committee may be aware of.	Audit Results Report (April 2023)
Internal controls	• Significant deficiencies in internal controls identified during the audit	Audit Results Report (April 2023); and Management Letter (May 2023)

Required communications with the Corporate Affairs and Audit Committee

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Representations	Written representations we are requesting from management and/or those charged with governance	Audit Results Report (April 2023)
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise.	Audit Results Report (April 2023)
Auditors report	Any circumstances identified that affect the form and content of our auditor's report.	Audit Results Report (April 2023)
Fee Reporting	• Breakdown of fee information when the audit plan is agreed; • Breakdown of fee information at the completion of the audit; and • Any non-audit work	Audit Planning Report (this report); and Audit Results Report (April 2023)
Group audits	• An overview of the type of work to be performed on the financial information of the components; • An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components; • Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work; • Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted; • Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements.	Audit Planning Report (this report); and Audit Results Report (April 2023)

Appendix C

Additional audit information

Other required procedures during the course of the audit	
In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.	
Our responsibilities required by auditing standards	• Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion; • Obtaining an understanding of internal control relevant to the audit 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 the Council's internal control; • Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management; • Concluding on the appropriateness of management's use of the going concern basis of accounting; • Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation; • Reading other information contained in the financial statements, the Corporate Affairs and Audit Committee reporting appropriately addresses matters communicated by us to the Corporate Affairs and Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and • Maintaining auditor independence.

Additional audit information

Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines the level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

EY | Assurance | Tax | Transactions | Advisory

About EY

Ernst & Young LLP

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

ey.com

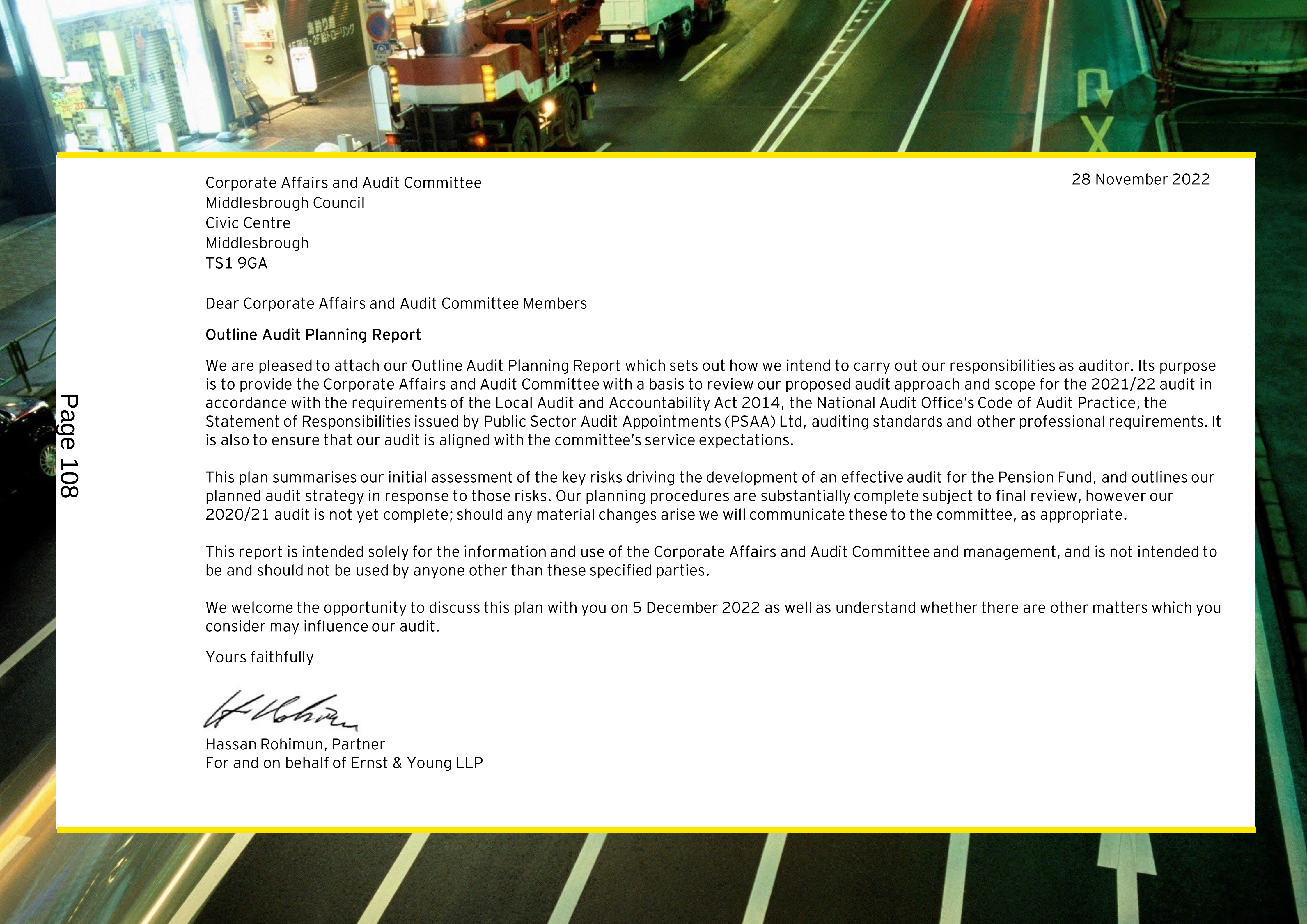
Teesside Pension Fund

Outline Audit Planning Report

Year ended 31 March 2022

November 2022

Building a better
working world



28 November 2022

Corporate Affairs and Audit Committee
Middlesbrough Council
Civic Centre
Middlesbrough
TS1 9GA

Dear Corporate Affairs and Audit Committee Members

Outline Audit Planning Report

We are pleased to attach our Outline Audit Planning Report which sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the Corporate Affairs and Audit Committee with a basis to review our proposed audit approach and scope for the 2021/22 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the committee's service expectations.

This plan summarises our initial assessment of the key risks driving the development of an effective audit for the Pension Fund, and outlines our planned audit strategy in response to those risks. Our planning procedures are substantially complete subject to final review, however our 2020/21 audit is not yet complete; should any material changes arise we will communicate these to the committee, as appropriate.

This report is intended solely for the information and use of the Corporate Affairs and Audit Committee and management, and is not intended to be and should not be used by anyone other than these specified parties.

We welcome the opportunity to discuss this plan with you on 5 December 2022 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Hassan Rohimun, Partner
For and on behalf of Ernst & Young LLP

Contents

Public Sector Audit Appointments Ltd (PSAA) issued the “Statement of responsibilities of auditors and audited bodies”. It is available from the PSAA website (https://www.psaa.co.uk/audit-quality/statement-of-responsibilities/).The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The “Terms of Appointment and further guidance (updated April 2018)” issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature.

This report is made solely to the Corporate Affairs and Audit Committee and management of Teesside Pension Fund in accordance with the Statement of responsibilities. Our work has been undertaken so that we might state to the Corporate Affairs and Audit Committee and management of Teesside Pension Fund those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Corporate Affairs and Audit Committee and management of Middlesbrough Council for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.

01

Overview of our 2021/22 audit strategy

Overview of our 2021/22 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Corporate Affairs and Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from prior year	Details
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively.
Valuation of pooled investment vehicles	Significant risk	**No change** in risk or focus	The majority of the Fund's investments are held as investments in pooled investment vehicles. Judgement is required from Investment Managers to value these investments as prices are not normally publicly available. The material nature of these investments means that any error in these judgements could result in a material valuation error.
Valuation of private market investments	Significant risk	New risk	The Fund has a growing portfolio of private market investments. Valuation of these investments is performed under a number of different frameworks, depending upon the location and jurisdiction of the investment. Greater judgement is required to value these investments as prices are not publicly available and market volatility means such judgements can quickly become outdated, especially where there is a significant time period between the latest audited information and the Fund's reporting date. Any error in valuation or variation since the audited information could have a material impact upon the financial statements. We recognise this as a new risk this year due to the increase in value of such investments since the prior year.
Valuation of directly held property	Significant risk	**No change** in risk or focus	The Fund has a significant portfolio of directly held property investments. The valuation of these properties is subject to a number of assumptions and judgements, small changes in which could have a significant impact upon the financial statements.
Recognition of investment income	Significant risk	New risk	Analysis of the Fund's accounting entries performed as part of our planning work identified a large unexpected increase in investment income. Initial enquiries of management as to the reasons for this identified that amounts had been incorrectly recognised resulting in a material overstatement of investment income in the Pension Fund's draft financial statements.

Overview of our 2021/22 audit strategy

In the prior year we also recognised the Pension Fund’s disclosures around going concern as an inherent risk. Given the significant levels of cash held by the Fund, we are content that additional focus on these disclosures is no longer necessary and do not recognise this as a risk for this year’s audit. We will continue to review these disclosures as part of our standard audit procedures.

Materiality

Planning materiality

£50.7m

Materiality has been set at £50.7m, which represents 1% of the Fund’s net assets at 31 March 2022 per the draft financial statements. Materiality was also set at 1% of the Fund’s net assets for the prior year’s audit.

Performance materiality

£25.3m

Performance materiality has been set at £25.3m, which represents 50% of materiality. We have decreased the percentage of materiality used for performance materiality from 75% to 50% as the size of misstatements identified in recent audits leads us to conclude there is a higher risk of undetected misstatement.

Audit differences

£2.5m

We will report all uncorrected misstatements relating to the primary statements (Fund Account and Net Asset Statement) greater than £2.5 million. The reporting threshold for the prior year’s audit was £2.3m. Other misstatements identified will be communicated to the extent that they merit the attention of the Corporate Affairs and Audit Committee.

Overview of our **2021/22 audit** strategy

Audit scope

This Outline Audit Planning Report covers the work that we plan to perform to provide you with:

- Our audit opinion on whether the financial statements of Teesside Pension Fund give a true and fair view of the financial position as at 31 March 2022 and of the income and expenditure for the year then ended; and
- Our opinion on the consistency of the Fund's financial statements, which are included within the Fund's Annual Report, with the published financial statements of Middlesbrough Council (the administering authority).

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

- Strategic, operational and financial risks relevant to the financial statements;
- Developments in financial reporting and auditing standards;
- The quality of systems and processes;
- Changes in the business and regulatory environment; and
- Management's views on all of the above.

By considering these inputs, our audit is focused on the areas that matter and our feedback is more likely to be relevant to the Pension Fund. Should there be any changes to our plan on the completion of audit procedures we will provide an update to the Corporate Affairs and Audit Committee.

Taking the above into account, and as articulated in this Audit Planning Report, our professional responsibilities require us to independently assess the risks associated with providing an audit opinion and undertake appropriate procedures in response to that. Our Terms of Appointment with PSAA allow them to vary the fee dependent on "the auditor's assessment of risk and the work needed to meet their professional responsibilities". PSAA are aware that the setting of scale fees has not kept pace with the changing requirements of external audit with increased focus on, for example, the valuations of land and buildings, the auditing of groups, the valuation of pension obligations, the introduction of new accounting standards such as IFRS 9 and 15 in recent years as well as the expansion of factors impacting on the valuation of investments. Therefore to the extent any of these or any other risks are relevant in the context of the Pension Fund's audit, we will discuss these with management as to the impact on the scale fee.

Effects of climate-related matters on financial statements

Public interest in climate change is increasing. We are mindful that climate-related risks may have a long timeframe and therefore while risks exist, the impact on the current period financial statements may not be immediately material to an entity. It is nevertheless important to understand the relevant risks to make this evaluation. In addition, understanding climate-related risks may be relevant in the context of qualitative disclosures in the notes to the financial statements and value for money arrangements.

We make inquiries regarding climate-related risks on every audit as part of understanding the entity and its environment. As we re-evaluate our risk assessments throughout the audit, we continually consider the information that we have obtained to help us assess the level of inherent risk.

02 Audit risks

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Misstatements due to fraud or error*

What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

What will we do?

- Identifying fraud risks during the planning stages of our audit;
- Inquire of management about risks of fraud and the controls put in place to address those risks;
- Understand the oversight given by those charged with governance of management's processes over fraud;
- Consider the effectiveness of management's controls designed to address the risk of fraud;
- Determine an appropriate strategy to address those identified risks of fraud;
- Perform mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments made in the preparation of the financial statements, consideration of whether accounting estimates are free from material bias and a review for unusual transactions.

Our response to significant risks

Valuation of pooled investment vehicles

Financial statement impact

Misstatements that occur in relation to the risk of valuation of pooled investment vehicles could affect the pooled investment vehicles account. Pooled investment vehicle assets had the following balance in the draft 2021/22 financial statements:

- Pooled investment vehicles: £3,854m
- Pooled property investments: £68m

What is the risk?

The majority of the Fund's investments are held as investments in pooled investment vehicles. Judgement is required from Investment Managers to value these investments as prices are not normally publicly available. The material nature of these investments means that any error in these judgements could result in a material valuation error.

We have identified the valuation of the Fund's investments in unquoted pooled investment vehicles as a significant risk, as even a small movement in the assumptions underpinning investment manager valuations could have a material impact upon the financial statements.

What will we do?

- Document and walkthrough the process and design of the controls over the valuation process;
- Obtain third party confirmations of the valuation of pooled investments vehicle assets at the reporting date from the investment managers. We will also cross-check the investment manager confirmations to the confirmation of assets held obtained from the Fund's custodian;
- Review the relevant investment manager controls' reports for qualifications or exceptions that may affect the audit risk;
- Compare the movement in valuation of investments in pooled investment vehicles with the returns recognised as investment income per the investment manager confirmations, and investigate any unusual variances; and
- Review the basis of valuation for pooled investment vehicles and ensure it is in line with the accounting policy.

Our response to significant risks

Valuation of private market investments

Financial statement impact

Misstatements that occur in relation to the risk of valuation of private market investments could affect the pooled investment vehicles account. Pooled investment vehicle assets had the following balance in the draft 2021/22 financial statements:

- Pooled investment vehicles: £3,854m

What is the risk?

The Fund has a growing portfolio of private market investments, which for the purposes of our risk are those classified by the Fund as investments in private equity, infrastructure and other alternative assets.

Valuation of these investments is performed under a number of different frameworks, depending upon the location and jurisdiction of the investment. Greater judgement is required to value these investments as prices are not publicly available and market volatility means such judgements can quickly become outdated, especially where there is a significant time period between the latest audited information and the Fund’s reporting date. Any error in valuation or variation since the audited information could have a material impact upon the financial statements.

We have identified the valuation of the Fund’s investments in private market investments as a significant risk, as even a small movement in the assumptions underpinning investment manager valuations could have a material impact upon the financial statements.

What will we do?

The Fund’s private market investments are held as pooled investment vehicles therefore the audit response detailed on the previous page as our response to the risk of valuation of pooled investment vehicles includes coverage of private market investments.

In addition, for the subset of pooled investment vehicles which are also private market investments we:

- Reperform the translation of the net asset value, where reported in a currency other than sterling, to sterling using independently sourced exchange rates;
- Using the Fund's % share of the pooled investment vehicle, as confirmed by the investment manager, reperform the calculation of the valuation of the Fund's assets and compare to the financial statement valuation; and
- Seek explanations and, where appropriate, supporting evidence for any significant changes in valuation between the date of the audited pooled investment vehicle financial statements and the Fund's reporting date.

Our response to significant risks

Valuation of directly held property

Financial statement impact

Misstatements that occur in relation to the risk of valuation of directly held property could affect the properties account. Property assets had the following balance in the draft 2021/22 financial statements:

- Properties: £331m

What is the risk?

The Fund has a significant portfolio of directly held property investments. The valuation of these properties is subject to a number of assumptions and judgements, small changes in which could have a significant impact upon the financial statements.

We have identified the valuation of the Fund's directly held property as a significant risk, as even a small change in assumptions could have a material impact upon the financial statements.

What will we do?

- Agree the valuation of the Fund's property portfolio as a whole back to the valuation report provided by the Fund's external valuer;
- Perform an assessment of the competence, capabilities and independence of the Fund's external valuer as a management specialist;
- Perform an analysis of property valuations, including consistency with valuations of similar assets and changes in valuations from the prior period, to identify any assets with characteristics that indicate a potentially higher risk of misstatement; and
- Based on the above analysis, request our EY Real Estate specialists to review the valuations of a sample of assets sufficient to provide an evidence base on which to conclude on the reliability of the work of management's specialist.

Our response to significant risks

Recognition of investment income

Financial statement impact

Misstatements that occur in relation to the risk of recognition of investment income could affect the investment income account. Investment income had the following balance in the draft 2021/22 financial statements:

- Investment income: £176m

What is the risk?

As part of our audit planning procedures we utilise our data analytics tools to analyse the accounting records of the Pension Fund for unusual or unexpected accounting entries.

These procedures identified a large unexpected increase in investment income, which increased from £13.7m in 2020/21 to £176.4m in 2021/22.

Initial enquiries of management as to the reasons for this increase identified that amounts received and reinvested by investment managers without transactions occurring between the Pension Fund and the investment manager, for example the reinvestment of dividends received from underlying equity investments within equity pooled investment vehicles, had been incorrectly recorded as investment income. Management have confirmed that the balance is materially misstated in the draft financial statements.

We have identified the recognition of investment income as a significant risk, as our audit planning procedures identified a material misstatement within this account.

What will we do?

- Review management's quantification of the amounts incorrectly presented as investment income within the draft financial statements, and agree this to supporting evidence; and
- Confirm that the financial statements are appropriately amended* to correct this misstatement.

Note that we have already agreed with management that the impact of the overstatement of investment income is matched by an understatement of the gain in market value of investments, therefore the misstatement does not impact the valuation of investments at 31 March 2022 presented within the draft financial statements.

03

Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2021/22 has been set at £50.7 million. This represents 1% of the net assets of the Fund per the draft Statement of Accounts. It will be reassessed throughout the audit process. We have provided supplemental information about audit materiality in Appendix C.

Net assets of the Fund at 31 March 2022
£5.1bn

Planning materiality
£50.7m

Performance materiality
£25.3m

Audit differences
£2.5m

Prior year Materiality

£4.6bn

£45.6m

£34.2m

£2.3m

We request that the Corporate Affairs and Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

Key definitions

Planning materiality – The amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

Performance materiality – The amount we use to determine the extent of our audit procedures. We have set performance materiality at £25.3 million which represents 50% of planning materiality (rounded).

Audit difference threshold – This has been set as £2.5 million. We propose that misstatements identified below this threshold are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the Fund Account and Net Asset Statement.

Other uncorrected misstatements, such as reclassifications and misstatements in disclosures and corrected misstatements will be communicated to the extent that they merit the attention of the Corporate Affairs and Audit Committee, or are important from a qualitative perspective.

Specific materiality – We do not apply a specific lower materiality to the audit of related party transactions disclosures, however we do consider the materiality of transactions as they apply to both parties involved, rather than just to the Pension Fund.

04

Scope of our audit

Our Audit Process and Strategy

Objective and scope

Under the Code of Audit Practice, our principal objectives are to review and report on the Fund's financial statements and the consistency of these financial statements with those disclosed within the Fund's Annual Report.

We issue an audit report that covers:

1. Financial statement audit

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK).

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Procedures required by standards

- Addressing the risk of fraud and error;
- Significant disclosures included in the financial statements;
- Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- Auditor independence.

2. Consistency opinion

We are required to consider the consistency of the Fund's financial statements, which are included within the Fund's Annual Report, with the published financial statements of Middlesbrough Council (the Administering Authority).

Our Audit Process and Strategy

Audit Process Overview

Our audit involves:

- Identifying and understanding the key processes and internal controls; and
- Substantive tests of detail of transactions and amounts.

For 2021/22 we plan to follow a substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

Analytics

We will use our computer-based analytics tools to enable us to capture and analyse the entirety of the Pension Fund's general ledger. These tools:

- Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- Give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Corporate Affairs and Audit Committee.

Internal audit

We will meet with Internal Audit, and review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit plan, where they raise issues that could have an impact on the financial statements.

05 Audit team

Audit team

The engagement team is led by Hassan Rohimun, who will have responsibility for ensuring that our audit delivers high quality and value to the Pension Fund.

Mark Rutter will be the senior manager responsible for the day-to-day direction of audit work and is the key point for contact for the finance team.

When auditing key judgements, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where either EY or third party specialists provide input for the current year audit are:

Area	Specialists
Valuation of land and buildings	Cushman and Wakefield (management's valuation specialists) EY Real Estate valuation specialists (as auditor's specialists)
Pensions disclosures	Hymans Robertson (management's actuarial specialists) EY Actuaries (as auditor's specialists)

In accordance with auditing standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Pension Fund's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- Analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- Assess the reasonableness of the assumptions and methods used;
- Consider the appropriateness of the timing of when the specialist carried out the work; and
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

Developing the right audit culture

In July 2021, EY established a UK Audit Board (UKAB) with a majority of independent Audit Non-Executives (ANEs). The UKAB will support our focus on delivering high-quality audits by strengthening governance and oversight over the culture of the audit business. This focus is critical given that audit quality starts with having the right culture embedded in the business.

Our audit culture is the cement that binds together the building blocks and foundation of our audit strategy. We have been thoughtful in articulating a culture that is right for us: one that recognises we are part of a wider, global firm and is clear about whose interests our audits serve.

There are three elements underpinning our culture:

1. Our people are focused on a **common purpose**. It is vital we foster and nurture the values, attitudes and behaviours that lead our people to do the right thing.
2. The essential attributes of our audit business are:
    - **Right resources** – We team with competent people, investing in audit technology, methodology and support
    - **Right first time** – Our teams execute and review their work, consulting where required to meet the required standard
    - **Right reward** – We align our reward and recognition to reinforce the right behaviours
3. The six pillars of **Sustainable Audit Quality** are implemented.

01

Tone at the top

The internal and external messages sent by EY leadership, including audit partners, set a clear tone at the top - they establish and encourage a commitment to audit quality

02

Exceptional talent

Specific initiatives support EY auditors in devoting time to perform quality work, including recruitment, retention, development and workload management

03

Accountability

The systems and processes in place help EY people take responsibility for carrying out high-quality work at all times, including their reward and recognition

04

Audit technology and digital

The EY Digital Audit is evolving to set the standard for the digital-first way of approaching audit, combining leading-edge digital tools, stakeholder focus and a commitment to quality

05

Simplification and innovation

We are simplifying and standardising the approach used by EY auditors and embracing emerging technologies to improve the quality, consistency and efficiency of the audit

06

Enablement and quality support

How EY teams are internally supported to manage their responsibility to provide high audit quality

A critical part of this culture is that our people are **encouraged and empowered to challenge and exercise professional scepticism** across all our audits. However, we recognise that creating a culture requires more than just words from leaders. It has to be reflected in the lived experience of all our people each and every day enabling them to challenge themselves and the companies we audit.

Each year we complete an audit quality culture assessment to obtain feedback from our people on the values and behaviours they experience, and those they consider to be fundamental to our audit quality culture of the future. We action points that arise to ensure our culture continues to evolve appropriately.

2021 Audit Culture Survey result
A cultural health score of 78% (73%) was achieved for our UK Audit Business

We bring our culture alive by investing in three priority workstreams:

- Audit Culture with a focus on professional scepticism
- Adopting the digital audit
- Standardisation

This investment has led to a number of successful outputs covering training, tools, techniques and additional sources. Specific highlights include:

- Audit Purpose Barometer
- Active Scepticism Framework
- Increased access to external sector forecasts
- Forensic risk assessment pilots
- Refreshed PLOT training and support materials, including embedding in new hire and trainee courses
- Digital audit training for all ranks
- Increased hot file reviews and improved escalation processes
- New work programmes issued on auditing going concern, climate, impairment, expected credit losses, cashflow statements and conducting effective group oversight
- Development of bite size, available on demand, task specific tutorial videos

> *"A series of company collapses linked to unhealthy cultures…..have demonstrated why cultivating a healthy culture, underpinned by the right tone from the top, is fundamental to business success."*
>
> Sir John Thompson
> Chief Executive of the FRC

06

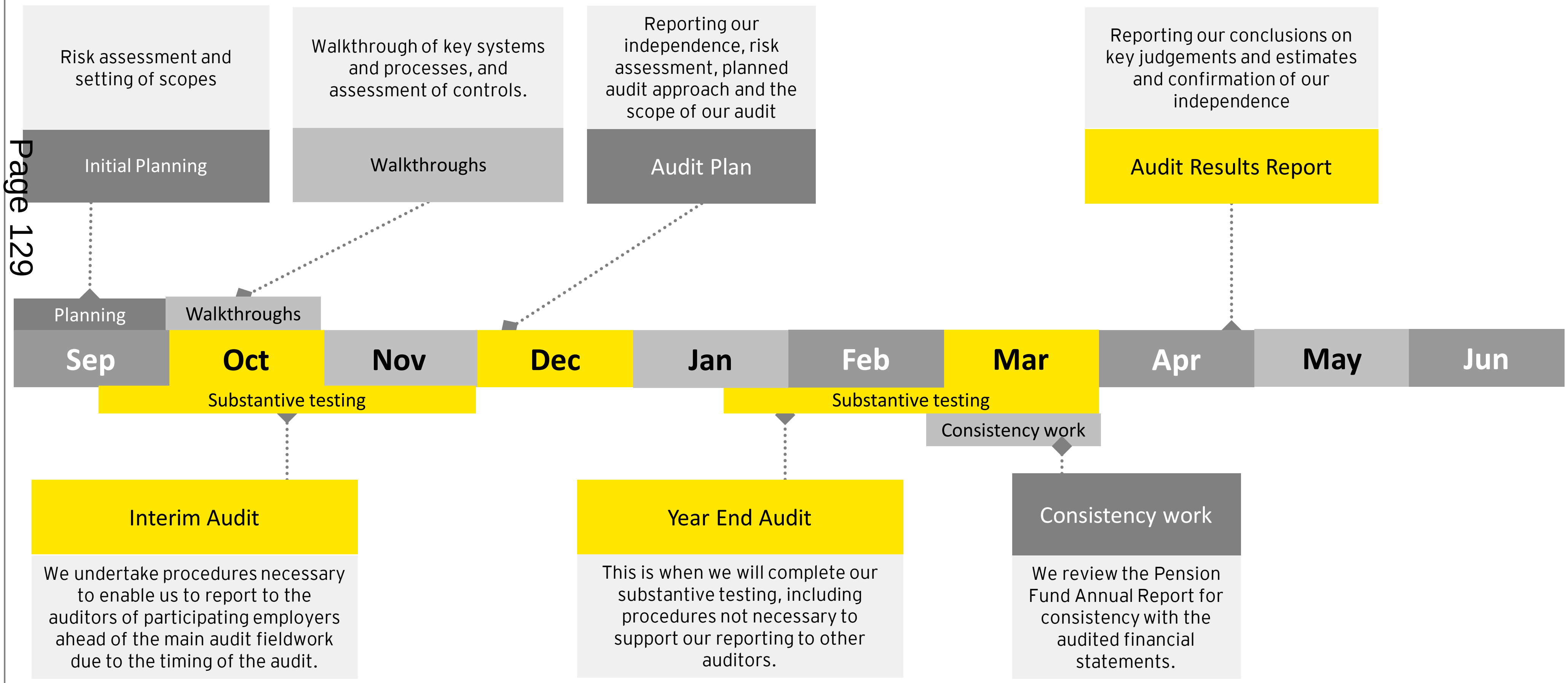
Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2021/22.

From time to time matters may arise that require immediate communication with the Corporate Affairs and Audit Committee and we will discuss them with the Corporate Affairs and Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.



Risk assessment and setting of scopes

Initial Planning

Walkthrough of key systems and processes, and assessment of controls.

Walkthroughs

Reporting our independence, risk assessment, planned audit approach and the scope of our audit

Audit Plan

Reporting our conclusions on key judgements and estimates and confirmation of our independence

Audit Results Report

Interim Audit

We undertake procedures necessary to enable us to report to the auditors of participating employers ahead of the main audit fieldwork due to the timing of the audit.

Year End Audit

This is when we will complete our substantive testing, including procedures not necessary to support our reporting to other auditors.

Consistency work

We review the Pension Fund Annual Report for consistency with the audited financial statements.

07

Independence

Introduction

The FRC Ethical Standard and ISA (UK) 260 "Communication of audit matters with those charged with governance", requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in December 2019, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	Final stage
▸ The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between you, your affiliates and directors and us; ▸ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review; ▸ The overall assessment of threats and safeguards; ▸ Information about the general policies and processes within EY to maintain objectivity and independence; and ▸ Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard.	▸ In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed; ▸ Details of non-audit services provided and the fees charged in relation thereto; ▸ Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us; ▸ Written confirmation that all covered persons are independent; ▸ Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy; ▸ Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and ▸ An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted.

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, are disclosed.

Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non-audit services if the service has been pre-approved in accordance with your policy.

Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Hassan Rohimun, your audit engagement partner, and the audit engagement team have not been compromised.

Self interest threats

A self interest threat arises when EY has financial or other interests in your Pension Fund. Examples include where we have an investment in related companies; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees, non-audit fees or business relationships and therefore no additional safeguards are required.

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 4.

There are no other self interest threats at the date of this report. We have received no fees for non-audit services (see Appendix A).

Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no self review threats at the date of this report.

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of your Pension Fund. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work.

There are no management threats at the date of this report.

Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

Relationships, services and related threats and safeguards

EY Transparency Report 2022

Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the period ended 1 July 2022:

EY UK 2022 Transparency Report | EY UK

08 Appendices

Appendix A

Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Levelling Up, Housing and Communities. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the requirements of the Code of Audit Practice and supporting guidance published by the National Audit Office, the financial reporting requirements set out in the Code of Practice on Local Authority Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.

Description	Planned Fee 2021/22 £	Scale Fee 2021/22 £	Estimated Requested Fee 2020/21 £	*Notes*
Base Audit Fee – Code Work	21,972	21,972	21,972	*1*
Changes in work required to address professional and regulatory requirements and scope associated with risk	49,199	N/A	39,359	*2, 3*
Revised Proposed Scale Fee	**71,171**	**21,972**	**61,331**	
IAS 19 Procedures – Code Work	9,250	N/A	8,500	*4*
Revised Proposed Scale Fee (inc. IAS 19 Procedures)	**80,421**	**21,972**	**69,831**	
Additional specific one-off considerations requiring additional work	TBC	N/A	5,000	*5, 6*
Total Audit Fee	**TBC**	**21,972**	**74,831**	
Fees for non-audit services	-	-	-	
Total Fees	**TBC**	**21,972**	**74,831**	

All fees exclude VAT

Fees

Notes

1) The base audit fees reflect the amounts determined by Public Sector Audit Appointments Limited (PSAA) in March 2020 and applied to subsequent years.
2) We wrote to management and the Corporate Affairs and Audit Committee Chair on 10 February 2020 setting out our considerations on the sustainability of UK local public audit. We have not been able to agree a scale fee variation with management and will therefore ask PSAA to make a determination as to the scale fee variation to be applied once our 2020/21 audit is concluded. The table on the previous page reflects the amount we intend to submit to PSAA as our assessment of the additional fee required to reflect changes in the level of work required to address professional and regulatory requirements and scope associated with risk.
3) We determine our assessment of the additional fee required to reflect changes in the level of work required to address professional and regulatory requirements and scope associated with risk in reference to hourly rates set by PSAA. PSAA have increased these rates by 25% since we determined the amounts for our 2020/21 audit.
4) As part of our audit we undertake additional procedures to enable us to report to the auditors of scheduled bodies that are subject to the NAO Code of Audit Practice. These procedures are additional to the procedures we must complete to support our opinion on the financial statements of the Pension Fund. Management may opt to recharge this fee to the relevant member bodies.
5) Where we identified significant risks and other areas of audit focus as part of our 2020/21 audit, as reported to the Corporate Affairs and Audit Committee, we undertook additional procedures to obtain the appropriate levels of evidence to support our opinion. The amount of £5,000 represents our current estimate of the additional fees we have determined as commensurate with the additional work undertaken, however until our 2020/21 audit is concluded further procedures may be required and will discuss the additional fees with management and will provide an update once this process has been finalised.
6) We note that there continue to be factors which increase the extent of our audit procedures over and above the levels envisaged by PSAA when determining scale fees. For 2021/22, this will include the increasing complexity of the Fund's investment portfolio, changes made in the NAO's revised 2020 Code of Audit Practice and the adoption of a new auditing standard *ISA 540: Auditing Accounting Estimates and Related Disclosures* which requires us to perform addition work around accounting estimates. We will discuss the impact of these factors on our audit fees with management once the full extent of additional effort has been determined.

Additional fees for the work required to discharge responsibilities under the Code of Audit Practice are subject to approval by the PSAA

The fees presented are based on the following assumptions:

- Officers meeting the agreed timetable of deliverables;
- Our accounts opinion being unqualified;
- No material weaknesses in arrangements for us to report on;
- Appropriate quality of documentation is provided by the Pension Fund; and
- The Pension Fund has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

Required communications with the Corporate Affairs and Audit Committee

We have detailed below the communications that we must provide to the Corporate Affairs and Audit Committee.

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Terms of engagement	Confirmation by the Corporate Affairs and Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The Statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter	The Statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit Planning Report (this report)
Significant findings from the audit	• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures; • Significant difficulties, if any, encountered during the audit; • Significant matters, if any, arising from the audit that were discussed with management; • Written representations that we are seeking; • Expected modifications to the audit report; and • Other matters if any, significant to the oversight of the financial reporting process	Audit Results Report (April 2023)

Required communications with the Corporate Affairs and Audit Committee

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: • Whether the events or conditions constitute a material uncertainty; • Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements; and • The adequacy of related disclosures in the financial statements	Audit Results Report (April 2023)
Misstatements	• Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation; • The effect of uncorrected misstatements related to prior periods; • A request that any uncorrected misstatement be corrected; • Corrected misstatements that are significant; and • Material misstatements corrected by management	Audit Results Report (April 2023)
Fraud	• Enquiries of the Corporate Affairs and Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity; • Any fraud that we have identified or information we have obtained that indicates that a fraud may exist; and • A discussion of any other matters related to fraud	Audit Results Report (April 2023)
Related parties	• Significant matters arising during the audit in connection with the entity's related parties including, when applicable: • Non-disclosure by management; • Inappropriate authorisation and approval of transactions; • Disagreement over disclosures; • Non-compliance with laws and regulations; and • Difficulty in identifying the party that ultimately controls the entity	Audit Results Report (April 2023)

Appendix B

Required communications with the Corporate Affairs and Audit Committee

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence. Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: • The principal threats; • Safeguards adopted and their effectiveness; • An overall assessment of threats and safeguards; and • Information about the general policies and process within the firm to maintain objectivity and independence	Audit Planning Report (this report); and Audit Results Report (April 2023)
External confirmations	• Management's refusal for us to request confirmations; and • Inability to obtain relevant and reliable audit evidence from other procedures	Audit Results Report (April 2023)
Consideration of laws and regulations	• Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off; and • Enquiry of the Corporate Affairs and Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Corporate Affairs and Audit Committee may be aware of.	Audit Results Report (April 2023)
Internal controls	• Significant deficiencies in internal controls identified during the audit	Audit Results Report (April 2023); and Management Letter (May 2023)

Appendix B

Required communications with the Corporate Affairs and Audit Committee

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Representations	Written representations we are requesting from management and/or those charged with governance	Audit Results Report (April 2023)
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise.	Audit Results Report (April 2023)
Auditors report	Any circumstances identified that affect the form and content of our auditor's report.	Audit Results Report (April 2023)
Fee Reporting	- Breakdown of fee information when the audit plan is agreed; - Breakdown of fee information at the completion of the audit; and - Any non-audit work	Audit Planning Report (this report); and Audit Results Report (April 2023)

Additional audit information

Other required procedures during the course of the audit

In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.

Our responsibilities required by auditing standards	• Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion; • Obtaining an understanding of internal control relevant to the audit 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 the Pension Fund's internal control; • Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management; • Concluding on the appropriateness of management's use of the going concern basis of accounting; • Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation; • Reading other information contained in the financial statements, the Corporate Affairs and Audit Committee reporting appropriately addresses matters communicated by us to the Corporate Affairs and Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and • Maintaining auditor independence.

Appendix C

Additional audit information

Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines the level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

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Ernst & Young LLP

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MIDDLESBROUGH COUNCIL

Report of:	Head of Internal Audit, Veritau

Submitted to:	Corporate Affairs and Audit Committee, 5 December 2022

Subject:	Internal Audit and Counter Fraud progress report

Summary

Proposed decision(s)
That the Committee: • notes the progress of internal audit and counter fraud work in 2022/23 and the outcomes from work completed since the last report to this committee.

Report for:	**Key decision:**	**Confidential:**
Information	n/a	No

Contribution to delivery of the 2021-24 Strategic Plan		
People	**Place**	**Business**
Receiving details of internal audit and counter fraud work completed will help the Committee perform its role. Internal audit and counter fraud work contributes towards achieving the Council's priorities by identifying potential issues which may obstruct that achievement.	Internal Audit assists management in delivering their priorities by working to an annual programme of work that includes assignments linked to corporate risks and priorities, and which seeks to add value by assessing the quality of controls, ensure value for money and achieve better outcomes for local people.	Delivering balanced budgets, maintaining front line services, and addressing budget shortfalls are priorities for the Council. Ensuring appropriate controls are in place and preventing fraud from occurring and recovering loss helps the Council achieve these aims.

Ward(s) affected
None.

What is the purpose of this report?

1. To provide Members with an update on progress with the delivery of internal audit and counter fraud work and on reports issued and other work completed since the last update report to this committee.

Why does this report require a Member decision?

2. Internal audit professional standards require that internal audit reports to the committee on progress with the delivery of audit plans and on the findings and conclusions from work completed.

Report Background

3. Internal audit provide independent and objective assurance and advice on the Council's operations. It helps the organisation to achieve overall objectives by bringing a systematic, disciplined approach to the evaluation and improvement of the effectiveness of risk management, control and governance processes.

4. The work of internal audit is governed by the Accounts and Audit Regulations 2015 and relevant professional standards. These include the Public Sector Internal Audit Standards (PSIAS), CIPFA guidance on the application of those standards in Local Government and the CIPFA Statement on the role of the Head of Internal Audit.

5. Fraud is a significant risk to the public sector. Annual losses are estimated to exceed £51 billion in the United Kingdom. Veritau are engaged to deliver a counter fraud service for Middlesbrough Council. The service helps the council to mitigate fraud risks and to take appropriate action where fraud is suspected.

6. The purpose of this report is to provide an update on internal audit and counter fraud work carried out in 2022/23. The Council's internal audit and counter fraud work programmes were approved by this Committee in April 2022.

Internal Audit Progress report

7. The internal audit progress report is contained in annex 1. It reports on progress against the internal audit work programme. This includes a summary of current work in progress, internal audit priorities for the year, completed work, and follow-up of previously agreed audit actions.

Counter Fraud Progress report

8. The counter fraud progress report is contained in annex 2. It reports on progress against the counter fraud work programme. A range of work is detailed including activity to promote awareness of fraud, work with external agencies, and information on the level of fraud reported to date.

What decision(s) are being asked for?

9. That the committee:

- notes the progress of internal audit and counter fraud work in 2022/23.

Why is this being recommended?

10. Internal audit professional standards require that progress in delivering internal audit work, and the findings and outcomes from audit work are reported to the committee.

Other potential decisions and why these have not been recommended

11. This report is for information. There are no other options available.

Impact(s) of recommended decision(s)

12. There are no implications to this report in relation to:

- ***Legal***
- ***Financial***
- ***Policy Framework***
- ***Equality and Diversity***
- ***Risk***

13. The Council will fail to comply with proper practice for internal audit if Members are not regularly updated on progress of and outcomes from internal audit work.

Actions to be taken to implement the decision(s)

14. n/a

Appendices

Annex 1 – internal audit progress report December 2022
Annex 2 – counter fraud progress report December 2022

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Background papers

No background papers were used in the preparation of this report

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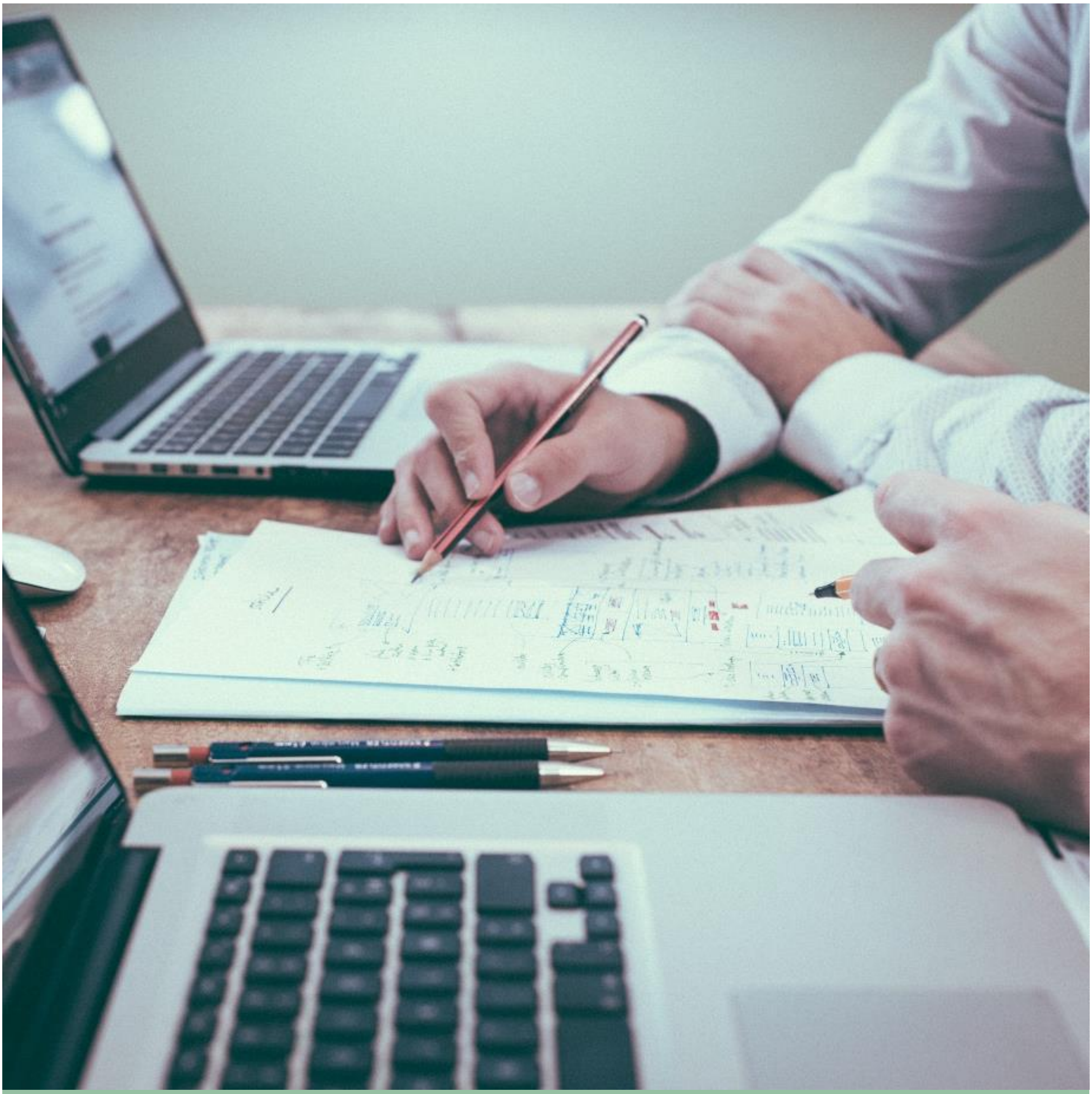
INTERNAL AUDIT PROGRESS REPORT 2022/23

Date: 5 December 2022

Annex 1



BACKGROUND

1 Internal audit provides independent and objective assurance and advice about the Council's operations. It helps the organisation to achieve overall objectives by bringing a systematic, disciplined approach to the evaluation and improvement of the effectiveness of risk management, control and governance processes.

2 The work of internal audit is governed by the Accounts and Audit Regulations 2015 and relevant professional standards. These include the Public Sector Internal Audit Standards (PSIAS), CIPFA guidance on the application of those standards in Local Government and the CIPFA Statement on the role of the Head of Internal Audit.

3 The internal audit work programme was agreed by this committee in April 2022. The plan is flexible in nature and work is being kept under review to ensure that audit resources are deployed to the areas of greatest risk and importance to the Council.

4 The purpose of this report is to update the committee on internal audit activity up to 31 October 2022.

INTERNAL AUDIT PROGRESS

5 Work is underway on a range of audits across Council directorates. Two audits are currently at draft report stage. A summary of internal audit work currently underway, as well as work finalised in the year, is included at appendix 1.

6 The work programme showing current priorities for internal audit work is included at appendix 2. Alongside the work in the 'do now' and 'do next' categories are indicative timescales for when work has commenced or is expected to commence and for when final reports will be produced. These timescales are subject to change and work priorities may also change during the year depending on an ongoing consideration of risk.

7 The programme includes a number of audits in the 'do later' category. The internal audit work programme is designed to include all potential areas that should be considered for audit in the short to medium term, recognising that not all of these will be carried out during the current year (work is deliberately over programmed).

8 One audit report has been finalised since the last report to this committee in September 2022 and details of this are included at appendix 3.

9 Appendix 4 lists our current definitions for action priorities and overall assurance levels.

FOLLOW-UP OF AGREED ACTIONS

10 All actions agreed with services as a result of internal audit work are followed up to ensure that underlying control weaknesses are addressed. A summary of the current status is at appendix 5.

APPENDIX 1: 2022/23 INTERNAL AUDIT WORK

Audits in progress

Audit	Status
Senior management reviews	In progress
Children's commissioning & contract management	In progress
Teesside Pension Fund – Investments	In progress
Supplier relief	In progress
Increase in demand (Children's Services)	In progress
Middlesbrough Development Company	In progress
Firewalls (ICT)	In progress
Creditors	In progress
Towns Fund governance	In progress
Tees Community Equipment Service	In progress
Council Tax and NNDR	In progress
Homecare	In progress
Schools themed audit – Schools Financial Value Standard	In progress
Payroll	In progress
Burial grounds	Draft report issued

Final reports issued

Audit	Reported to Committee	Opinion
Project management – Boho X	July 2022	Limited Assurance
Asset maintenance	July 2022	Substantial Assurance
Teesside Pension Fund – overpayments	July 2022	Substantial Assurance
Schools themed audit – purchasing cards & asset management	July 2022	Substantial Assurance
Future High Streets Fund	September 2022	Substantial Assurance
Home working	September 2022	Substantial Assurance
ICT change management	September 2022	Substantial Assurance
Benefits - overpayments	September 2022	Substantial Assurance
Main Accounting	December 2022	Substantial Assurance

Other work in 2022/23

Internal audit work has been undertaken in a range of other areas during the year, including those listed below.

- A review of grant claims including the Children's Services Practice Improvement Grant and claims relating to Scambusters.
- A review of returns completed by the Council for the Supporting Families scheme .
- A review of Covid grant schemes including Track and Trace and the Contain Outbreak Management Fund.
- Data analysis on debtors accounts to provide feedback on potential data errors including duplicate entries.
- Ongoing governance work relating to allegations made by former Executive members.

APPENDIX 2: CURRENT PRIORITIES FOR INTERNAL AUDIT WORK

Audit / Activity	Rationale for inclusion / change in priority	Expected / Actual start	Expected finish
Corporate & cross cutting			
Category 1 (do now)			
Senior management reviews	Raised by the CAAC as an issue for review.	August 2022	TBC
Supplier relief	Significant priority for the Council.	August 2022	December 2022
Category 2 (do next)			
Financial planning and resilience Risk management Performance management and data quality Corporate governance Strategic planning Ethics and culture Local Plan strategy and development	These audits are considered the next priority audits at this time based on current risk and other work ongoing. Timescales will be determined once other ongoing work progresses further.		
Category 3 (do later)			
Budgeting and savings plans Partnerships Procurement and contract management Workforce planning HR Corporate complaints Information governance	These audits are not considered high priority at the current time but this will be re-evaluated as the year progresses.		

Audit / Activity	Rationale for inclusion / change in priority	Expected / Actual start	Expected finish
Democratic services and elections Environment and climate change Health and safety Business continuity			
Financial / corporate systems			
Category 1 (do now)			
Teesside Pension Fund – Investments	Key financial system.	March 2022	December 2022
Payroll	Key financial system.	August 2022	December 2022
Creditors	Key financial system.	September 2022	December 2022
Council Tax/NNDR	Key financial system.	November 2022	February 2023
Category 2 (do next)			
Debtors	Key financial system. This will follow on from some initial data analysis work.	January 2023	April 2023
Benefits & Council Tax Support	Key financial system.	January 2023	April 2023
Category 3 (do later)			
Capital accounting and assets			
Treasury Management VAT accounting			

Audit / Activity	Rationale for inclusion / change in priority	Expected / Actual start	Expected finish
ICT			
Category 1 (do now)			
Firewall security	Key ICT risk area and agreed with the service as a priority for review.	August 2022	December 2022
Category 2 (do next)			
Strategy and governance ICT risk management Patch management Cyber security	These audits are considered the next priority audits at this time based on current risk and other work ongoing. The next audits will be agreed with the ICT service during the year.		
Category 3 (do later)			
None			
Operational audits			
Category 1 (do now)			
Burial Grounds	Concerns have been raised about the governance in this area. The audit is now in draft and the findings and actions are being agreed with the service.	November 2021	November 2022
Children's Commissioning and Contract Management	Deferred from 2020/21. Links to the audit work carried out last year following the	March 2022	December 2022

Audit / Activity	Rationale for inclusion / change in priority	Expected / Actual start	Expected finish
	Ofsted inspection. There have been delays due to a lack of officer availability.		
Middlesbrough Development Company	Significant priority for the Council.	August 2022	December 2022
Increase in demand (Children's Service)	Recognised nationally as a significant risk. The audit was originally planned as 'Children's caseload management'.	September 2022	February 2023
Towns Fund governance	A significant priority for the Council and an audit was agreed as an action from the Boho X work.	September 2022	December 2022
Tees Community Equipment Service	A review of the service along with compliance with financial procedures. Some initial data analysis is being carried out.	October 2022	February 2023
Homecare	A review of homecare payments was identified as an area for audit following other work; we have identified issues at other Councils.	November 2022	February 2023
Schools themed audit – School's Financial Value Standard	There have been changes to the requirements relating to related party transactions for schools and this will be considered as part of the audit.	November 2022	April 2023

Audit / Activity	Rationale for inclusion / change in priority	Expected / Actual start	Expected finish
Category 2 (do next)			
Selective landlord licensing	This has been raised as an area for review by the relevant DMT.	January 2023	April 2023
Project management – regeneration	An action from the Boho X audit report was to review the project management of other regeneration projects.	January 2023	April 2023
Category 3 (do later)			
Domestic violence Shopping centre development Regeneration projects Planning complaints Transporter Bridge (follow-up)	These audits are considered the next priority audits at this time based on current risk and other work ongoing.		
Social care referrals and assessments Legislative changes Recruitment and retention Liberty Protection Safeguards Public health Environmental health Homelessness Special Educational Needs Exclusions (schools) Recruitment of foster carers Home to school transport Highways and fleet management Planning	These audits are not considered high priority at the current time but this will be re-evaluated as the year progresses.		

Audit / Activity	Rationale for inclusion / change in priority	Expected / Actual start	Expected finish
Economic development Town Hall strategic management			

APPENDIX 3: SUMMARY OF KEY ISSUES FROM AUDITS FINALISED SINCE THE LAST REPORT TO THE COMMITTEE

System/area	Opinion	Area reviewed	Date issued	Comments / Issues identified	Management actions agreed	P1 actions	P2 actions
Main Accounting	Substantial Assurance	Control/suspense accounts, bank reconciliations, feeder systems, journals, virements, budget monitoring.	15 September 2022	Processes are working well with few issues identified.	Reviews of journal descriptions will be carried out and feedback provided to staff where they are inadequate.	0	0

APPENDIX 4: AUDIT OPINIONS AND PRIORITIES FOR ACTIONS

Audit opinions

Our work is based on using a variety of audit techniques to test the operation of systems. This may include sampling and data analysis of wider populations. It cannot guarantee the elimination of fraud or error. Our opinion relates only to the objectives set out in the audit scope and is based on risks related to those objectives that we identify at the time of the audit.

Opinion	Assessment of internal control
Substantial assurance	A sound system of governance, risk management and control exists, with internal controls operating effectively and being consistently applied to support the achievement of objectives in the area audited.
Reasonable assurance	There is a generally sound system of governance, risk management and control in place. Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of objectives in the area audited.
Limited assurance	Significant gaps, weaknesses or non-compliance were identified. Improvement is required to the system of governance, risk management and control to effectively manage risks to the achievement of objectives in the area audited.
No assurance	Immediate action is required to address fundamental gaps, weaknesses or non-compliance identified. The system of governance, risk management and control is inadequate to effectively manage risks to the achievement of objectives in the area audited.

Priorities for actions

Priority 1	A fundamental system weakness, which presents unacceptable risk to the system objectives and requires urgent attention by management
Priority 2	A significant system weakness, whose impact or frequency presents risks to the system objectives, which needs to be addressed by management.
Priority 3	The system objectives are not exposed to significant risk, but the issue merits attention by management.

APPENDIX 5: FOLLOW UP OF AGREED AUDIT ACTIONS

Where weaknesses in systems are found by internal audit, the auditors agree actions with the responsible manager to address the issues. Agreed actions include target dates and internal audit carry out follow up work to check that the issue has been resolved once these target dates are reached. Follow up work is carried out through a combination of questionnaires completed by responsible managers, risk assessment, and by further detailed review by the auditors where necessary. Where managers have not taken the action they agreed to, issues are escalated to more senior managers, and ultimately may be referred to the Corporate Affairs and Audit Committee.

Actions completed

A total of 13 actions have been completed since the last report to this committee. A summary of the priority of the 13 completed actions are included below.

Actions agreed	
Priority of actions	**Number of actions agreed**
1	3
2	4
3	6
Total	**13**

Actions agreed by directorate						
Priority of actions	**Adult Social Care**	**Children's Services**	**Environment and Community**	**Finance**	**Legal and Governance**	**Regeneration**
1	0	0	0	0	0	3
2	0	1	0	0	1	2
3	0	1	0	3	2	0
Total	**0**	**2**	**0**	**3**	**3**	**5**

Actions Outstanding

A total of 21 actions with original due dates that have passed are still outstanding. A summary of the priority of these actions is included below.

Actions agreed	
Priority of actions	**Number of actions agreed**
1	8
2	9
3	4
Total	**21**

Actions agreed by directorate						
Priority of actions	**Adult Social Care**	**Children's Services**	**Environment and Community**	**Finance**	**Legal and Governance**	**Regeneration**
1	0	0	7	0	0	1
2	0	1	6	1	0	1
3	0	1	0	0	3	0
Total	**0**	**2**	**13**	**1**	**3**	**2**

Of the 21 actions outstanding 17 have had a revised date agreed. The remaining 4 actions are currently being followed up.

Actions outstanding for more than 6 months (Priority 1 and 2)

Ten actions have currently been outstanding for longer than 6 months beyond the agreed implementation date and are included in the table below. Revised dates have been agreed and we will follow these up when the new implementation date becomes due.

Audit	Priority	Original Date	Revised Date	Finding / Action	Reason for Delay
Transporter Bridge	2	Mar 21	Apr 23	Management should ensure that maintenance and staff meetings at the Transporter Bridge are regularly held and minuted. All identified actions should be recorded and followed up to ensure that remedial action is delivered by action owners within the agreed timescales.	There is no agreed date for when the bridge will return to operational service. Some initial work has been carried out to address the actions and emergency repairs are being undertaken but this will not make the bridge operational. Officers would require further funding to be agreed to bring the bridge back into full operation. As a result, the remaining actions which largely relate to operational issues have been revised to an implementation date of April 2023.

Audit	Priority	Original Date	Revised Date	Finding / Action	Reason for Delay
Transporter Bridge	2	Mar 21	Apr 23	Senior staff from both Transport & Infrastructure and Property & Commercial Services should meet regularly to ensure that relevant matters are discussed and minuted (e.g. maintenance or inspection programmes and day-to-day issues relating to the Transporter Bridge). All identified actions should be recorded and followed up to ensure that remedial action is delivered by action owners within the agreed timescales.	As Above
Transporter Bridge	1	Mar 21	Apr 23	Management should review the effectiveness of the current management arrangements for the Transporter Bridge. Going forward, the Council should consider external technical consultancy or guidance to ensure that both the service and the structure remain fit for purpose.	As Above
Transporter Bridge	1	Mar 21	Apr 23	Management should ensure that effective governance arrangements are implemented for the Transporter Bridge. This should include performance being regularly reported to all stakeholders and a service level agreement agreed between the Council and Stockton Borough Council which details all management responsibilities to ensure that the facility remains fit for purpose.	As Above

Audit	Priority	Original Date	Revised Date	Finding / Action	Reason for Delay
Transporter Bridge	1	Mar 21	Apr 23	A documented maintenance schedule must be produced (by an appropriately qualified in-house employee or external consultant) to detail what checks are to be carried out at the Transporter Bridge and their associated frequency. Documented systems should be adopted whereby individuals sign for checks carried out on a registered job card as soon as they have been completed. A maintenance log should be created to detail all activities that are undertaken by on site staff as well as outside contractors.	As Above
Transporter Bridge	2	Mar 21	Apr 23	A training needs analysis should be compiled for all staff at the Transporter Bridge. This analysis should highlight the training required, differentiating between mandatory training for legislative requirements and other advisable training for best practice. The analysis should identify how and by whom the training will be delivered and the associated frequency. Training records for all staff should be maintained to ensure an up to date record of all staff training completed and to be completed is available.	As Above
Transporter Bridge	1	Mar 21	Apr 23	Management should ensure that, in the interest of safety for members of staff, public, visitors, activity agents and for the vessels that travel underneath the	As Above (survey completed in December 2021).

Audit	Priority	Original Date	Revised Date	Finding / Action	Reason for Delay
				structure, that the Transporter Bridge has a full structural survey. All remedial actions identified as a result of that survey must be addressed as directed by the survey findings. The facility should remain closed until it has been deemed fit for purpose by surveyors.	
Transporter Bridge	1	Mar 21	Apr 23	Management should organise a risk workshop with all relevant staff for the purposes of compiling a register that captures all risks facing the Transporter Bridge including health and safety risks and those relating to the strategic objectives of the Transporter Bridge i.e. risks that could prevent the attainment of the Council's vision and aims. The risk register should then be periodically reviewed (e.g. at least twice a year) to ensure that the risks remain relevant and that planned mitigation actions are implemented according to timescales.	As Above
Debtors	2	Sep 21	Mar 23	The VAT Officer will investigate cases with incorrect VAT treatment identified during the audit and will provide further training and guidance for relevant staff.	A new VAT officer is now in place who will investigate and produce some key points on the incorrect VAT treatment with further training and guidance provided where necessary.

Audit	Priority	Original Date	Revised Date	Finding / Action	Reason for Delay
Use of CCTV	1	Dec 21	Jul 23	Scheme managers and responsible officers will be identified for all schemes and they will maintain Code Assessment Packs, demonstrating compliance with the Council's local code of practice. The Operational Community Safety Manager will produce an annual report based on a review of annual self-assessments by scheme managers.	The majority of the actions relating to the audit have now been completed however this remains outstanding. Scheme managers will be provided with guidance and training so they can maintain appropriate Code Assessment Packs. In addition, the next annual report will include a review of annual self-assessments.

COUNTER FRAUD PROGRESS REPORT 2022/23

Date: 5 December 2022

Annex 2

BACKGROUND

1 Fraud is a significant risk to the public sector. The government estimates that the taxpayer loses up to £51.8 billion to fraud and error in public spending every year[1]. Financial loss due to fraud can reduce a council's ability to support public services and cause reputational damage.

2 Veritau delivers a corporate fraud service to the Council which aims to prevent, detect and deter fraud and related criminality. We employ qualified criminal investigators to support departments with fraud prevention, proactively identify issues through data matching exercises, and investigate any suspected fraud. To deter fraud, offenders face a range of outcomes, including prosecution in the most serious cases

3 This report updates the Corporate Affairs and Audit Committee on counter fraud activity to date.

FRAUD MANAGEMENT

4 The Council's counter fraud framework was reviewed and updated in September 2022. This included an updated strategy action plan, anti-fraud, corruption, and bribery policy, and fraud risk assessment.

5 In October information was released to members of staff to mark cybersecurity awareness month. The material focussed on mandate fraud (aka payment diversion fraud) a form of cybercrime that has been increasing in terms of sophistication, frequency, and success over the past 12 months. Staff were updated on the latest tactics and tools used by criminals to commit this type of fraud as well as warning signs to look out for. Earlier in the year bespoke and more in depth training was provided to the Creditors Team as they are most likely to be contacted by perpetrators of this type of fraud.

6 An awareness campaign informing staff about the council's anti-bribery and anti-money laundering policies is planned for December.

7 The counter fraud team is starting to work more closely with the Revenues and Benefit teams. Work is being undertaken to review outstanding National Fraud Initiative (NFI) matches.

MULTI-AGENCY WORK

8 The National Fraud Initiative is a large-scale data matching exercise that involves all councils and other public sector bodies in the UK. The work of the NFI is overseen by the Cabinet Office and the exercise runs every two years. Data from a range of council areas has been gathered for the upcoming 2022/23 exercise. The counter fraud team have assisted to

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[1] Fraud and Error (Ninth Report of Session 2021/22), Public Accounts Committee, House of Commons

ensure correct data is sent on schedule. In addition checks have been made to help ensure that the council meets fair processing requirements. Results of the datamatching exercise are expected to be released in February 2023.

INVESTIGATIVE WORK

9 In 2022/23, the counter fraud team has received twenty-three referrals of suspected fraud to date. These cover potential adult social care fraud, council tax reduction and debt recovery issues. Referrals have been made by members of staff, the NFI, and the public. Sixteen investigations have been completed in the current financial year and there are currently seven cases under investigation.

10 An adult social care investigation into deprivation of capital has resulted in a warning being issued to a member of the public who has also been issued an invoice for £18k.

11 Working with Legal Services the team have assisted the Council to trace debtors. To date information has been provided in connection with debts totalling £40k.

MIDDLESBROUGH COUNCIL	Middlesbrough moving forward

Report of:	Director of Finance (S151 Officer)

Submitted to:	Corporate Affairs and Audit Committee

Date:	5 December 2022

Title:	Capital Strategy 2022/23 – Mid Year Update

Report for:	Information

Status:	Public

Strategic priority:	All

Key decision:	Not applicable
Why:	Report is for information only

Urgent:	No
Why:	

Executive summary

The capital strategy is one of the main elements of the Council's budget approach, alongside the Revenue Budget and the Investment Strategy. Although some high-level metrics on progress are reported as part of the quarterly budget monitoring process, it is good practice to review this information in more detail at Quarter 2. Given the remit in relation to the Statement of Accounts, financial probity, and governance, and that the original strategy was bought for consultation on 9 December 2021, the review role best sits with Members of this Committee.

This report therefore reviews the position on the Investment Strategy, any changes that have occurred during the year to date, plus any implications for affordability since the original budget was set in February 2022. In addition, the report reviews the position on treasury management, including borrowing, investments, and debt repayment.

The second aspect of the report considers a change to the Council's current approach to Minimum Revenue Provision. As this will need further consideration by Executive and then approval by Council, we are consulting with the Committee at this initial stage for comments before the report goes forward for approval.

Purpose

1. The Capital Strategy report gives a high-level overview of how capital expenditure, capital financing and treasury management activities contribute to the provision of local public services at the Council. In addition, it also gives an overview of how the associated risks involved are managed and the implications for future financial sustainability.

2. This is a mid-year review of the strategy, which is considered best practice in line with the CIPFA Codes on the Prudential Code of Capital Finance and Treasury Management, to see how the strategy has developed in the first six months of the year. In addition, the Council is considering a change in its policy on Minimum Revenue Provision (MRP). This change in policy needs approval by Full Council as the decision-making body. However, consultation with the Committee is best practice given its roles and responsibilities.

Background and relevant information

3. The Capital Strategy report for the Council covers the following areas:

   - How the Investment Strategy is funded.
   - The relevant Prudential Indicators to monitor the performance, affordability and sustainability of the capital expenditure being proposed in line with the requirements of the prudential code.
   - Treasury Management arrangements in place for investing surplus funds and borrowing to fund capital expenditure.
   - The types of investments the Council makes as part of managing its cash balances – the Annual Investment Strategy.
   - Minimum Revenue Provision policy – including outlining how much the Council sets aside to re-pay debt built up to fund prior year's capital expenditure in the Borough.

4. Capital Expenditure relates to what the Council plans to invest in long-term assets and infrastructure (such as property, equipment, vehicles, roads etc.). The Council must consider how this expenditure is paid for and what the long-term financial implications are of undertaking this investment. The Council is also permitted to borrow funds to finance the investment strategy under the Local Government Act 2003. It needs to consider the impact on the revenue budget of the level of borrowing being proposed, how it funds the repayment of this debt and the period over which this debt is repaid.

5. The Capital Strategy and the key assumptions that influenced the setting of the 2022/23 budget are set out at **Appendix 1** for reference purposes and information.

<u>Prudential Indicators and Capital Investment Plans</u>

6. The Council demonstrates the concepts of affordability, sustainability and prudence on its investment plans by setting a range of Prudential and Treasury Management indicators. These are set out in the various tables in Appendix 1 and are key metrics to the Director of Finance when setting the budget plans each year. Any breach of these indicators during a year indicates either a higher level of indebtedness or a lower level of overall prudence on the capital activities of the Council than when the budget was set. The following paragraphs give a brief commentary on these key indicators to assess any changes that have occurred during the financial year to date.

7. Although the Capital Strategy covers the whole of the medium-term financial planning period, this mid-year review focuses solely on the position for 2022/23. Due to the current review of the Investment Strategy and any further changes that may occur before the financial year-end on 2022/23 budgets, it is not appropriate to review the other years at this stage. These will be updated as part of the budget setting report to Council in February 2023.

8. The position at the end of quarter 2 was as follows. This was reported to Executive as part of the regular quarterly budget monitoring arrangements on 8 November 2022:

Prudential Indicators - 2022/23 Quarter 2

	Budget (£M)	Actual (£M)
Capital Expenditure	124.825	69.241
Financing		
External Sources	74.344	41.579
Own Resources	6.296	3.257
Debt	44.185	24.405
Capital Financing Requirement	295.865	283.324
External Debt	268.350	205.667
Investments	15.630	21.020
Capital Financing	10.466	10.587
Cost as a % of Revenue Budget	8.8%	8.9%

9. The first point to note is that Investment Strategy for 2022/23 has reduced significantly during the financial year to date. In summary, this relates to slippage on approved capital schemes into later years in the programme, with the funding before re-profiled also. Further analysis of this at individual scheme and directorate levels can be seen within the Quarter 1 & 2 budget monitoring reports.

10. It can also be seen that the amounts of funding needed have also reduced below the original budgeted levels. Some of this is for schemes funded by capital grants and contributions by other bodies, but also there is an in-year reduction on the level of borrowing needed of £19.8m (original budget of £44.2m less current budget of £24.4m).

11. There is total outstanding debt of £205.7 million (including debt and lease liabilities) on 30 September 2022, with a further £40 million - £45 million expected to be needed before 31 March 2022. Cash balances are generally higher in the first two quarters of the financial year as grants and contributions tend to be paid in advance of need. This means that the level of external debt above is lower than it should be based on the level of capital expenditure forecast, as borrowing needs have been deferred.

12. The total amount given for additional borrowing in this financial year is higher than the figure quoted in paragraph 10. This is due to additional cash flow demands, as a result of using earmarked reserves to fund the revenue budget position, plus the early use of grant income in advance which needs to be replaced.

13. The forecast overall total long term external debt at the end of 2022/23 is expected to be around £250million. This should be compared with the estimated *Capital Financing Requirement* (the underlying value which the Council needs to borrow to fund capital activities) of £283m million. The Council therefore has an expected under-borrowed position of circa £33 million or 12%, which has provided some annual savings in interest payments, as other revenue and capital cash has been used in lieu of borrowing. This is a key strategic decision each year as to whether the under-borrowing position is increased or reduced and does not diverge from that used as part of the budget position.

14. Table 6 in Appendix 1 shows the profile of outstanding debt over the whole of the medium-term financial planning period and that this was expected to rise to a maximum of £268 million at 31st March 2023, before starting to reduce in the following financial year. This increase in debt is not expected to rise much further than £250m now given the recent review of the capital programme, which has reduced borrowing requirements from when the original budget position was agreed. This position will be updated again as part of the budget setting report.

15. The Council holds revenue budgets for repaying debt (known as Capital Financing Costs). This costs £10.6m (8.9% of the net revenue budget) for the 2022/23 financial year). The Council has a nominal threshold of 10% of its revenue budget as a cap for capital financing, so there is still some headroom for borrowing on urgent priorities if required, subject to overall council affordability

16. Table 9 in Appendix 1 shows that the proportion of capital financing costs is relatively stable at a time when the level of external debt is rising. This is due to the commercial income achieved on recent capital investments in Centre Square, Teesside Advanced Manufacturing Park and Captain Cook Square. It is important that these income levels are maintained otherwise the proportion of the revenue budget attributed to capital financing costs will start to increase.

17. One way to reduce capital financing costs is to reschedule the debt. This means to repay the debt earlier than expected and then to reborrow at a rate lower than the existing interest rate on the loan. This has been very difficult to do since 2008 due to low interest rates and high premiums on any early repayment options. Given the increase in interest rates in recent months, these premiums are starting to reduce and there may be some options for the Council to pursue. These are monitored on a regular basis by our treasury management advisers and if any of these are felt to be financially beneficial, they will be highlighted to Members by the Director of Finance.

18. It is also a statutory requirement for the Council to set an authorised limit for external debt at the start of each financial year. This is an amount beyond which it would be ultra-vires (or outside of the Council's legal powers) to exceed in a particular financial year. The authorised limit for 2022/23 is £356 million.

19. It should be noted that the authorised limit for the Council is currently much higher than either the level of external debt or the capital financing requirement. This is not uncommon within local authorities, to build in extra headroom for unexpected capital investment, possible debt re-financing opportunities and the remote possibility of needing to borrow for exceptional revenue purposes. At present, the Council's authorised limit is set at £73m above its capital financing requirement and allows a degree of flexibility within the Council's planning processes and this legal limit. It should be noted that any unexpected debt financing in a year could breach some of the other prudential indicators so this would need to be identified as part of the quarterly performance monitoring reports to Executive.

Treasury Management

20. Treasury Management is defined as the management of the Council's cash flows, borrowing and investments, and the associated risks. The main risks that affect a local authority include credit risk, interest rate risk, liquidity risk and refinancing risk.

21. The Council is generally cash rich in the short term, as many grants and contributions are paid in advance of need. Because of this, any excess cash is invested with an appropriate counterparty until the funds are required. When making an investment, the Council follows the advice set out in the Local Government Act 2003 and within the Treasury Management Code, with paramount consideration given to the security of the sum invested, followed by the liquidity position of the Council, and finally the interest rate achievable on the investment.

22. Given that credit criteria is the most important factor when making an investment decision, the Council receives regular updates from its external adviser, Arlingclose, on changes in credit ratings for individual financial institutions. They also advise on maximum amounts to be invested with each counterparty and maximum durations for any fixed term deposits made. This framework helps to protect against the loss of any sums invested (credit risk), ensures liquidity is not compromised and earns interest to support the revenue budget (not a major factor at present.

23. In relation to external borrowing, the Council seeks to achieve a low but certain cost of finance, whilst retaining the flexibility to borrow for short-term periods, and to respond to demands of the Investment Strategy as needed. The Council therefore has a balance between taking advantage of currently low rates of interest for short term borrowing (predominantly from other local authorities), versus the need to achieve certainty over rates of borrowing in the longer term from either government or financial institutions (mainly from the PWLB or other banks).

24. Out of the £205.667m worth of external debt on 30 September 2022, 65% is long term from the Public Works Loan Board – the government agency for local authority borrowing and 30% is long term with financial institutions (generally banks). There is around 5% of short term borrowing in place at present from other local authorities. The average interest rate on this debt is around 2.5% with an average life to maturity of just under 25 years. All longer-term debt held by the Council is at fixed rates of interest.

25. Current long term interest rates for borrowing from the PWLB are between 4% and 5% depending on the length of the loan (local authorities can borrow up to 50 years from central government), with short term rates being between 2.8% and 3.9% for up to one

year in duration. These are significantly higher than in recent financial years and reflect the Bank of England's attempt to control the levels of inflation in the UK economy at present. Although it is expected that interest rates for both borrowing and investments will level off over the next 1-2 years and then start to reduce, any borrowing implemented over the remainder of this year is likely to be short-term in nature. Higher than expected interest rates will put pressure on the capital financing budget as the year progresses.

26. On local authority borrowing, there has been much interest from both regulators and the media in recent months around individual councils taking significant amounts of long-term debt from the PWLB for the sole purposes of commercial activity – generally property investment. Under the Prudential Code, local authorities have lots of freedom to conduct and self-regulate their own borrowing and investment activities.

27. Both the Government and the Chartered Institute of Public Finance & Accountancy have said that borrowing for the sole purposes of commercial investment is against the spirit of the Code. The PWLB no longer provides loans for this type of activity from 1st April 2021 with Section 151 Officers having to confirm each year that their investment plans do not contain any of these types of activity. CIPFA is also updating the Prudential Code during 2022/23 to stop any borrowing for yield purposes and to also highlight and non-prudential practices.

28. Although the Council has undertaken some capital projects in recent years that have generated a revenue income stream as set out in paragraph 16 above, the primary aim has always been to regenerate the areas involved and to grow the wider economy within the Town. As a result, these activities would be able to continue under the Code and with funding from the PWLB if required.

<u>Minimum Revenue Provision</u>

29. The Council is required to maintain an annual policy for the repayment of debt incurred over previous financial years. The current policy is split into different elements which are based on: when the borrowing was originally incurred, the type of assets, and the useful economic life of the assets which the borrowing is funding. The Council in 2016/17, amended this policy to more accurately reflect the useful economic life of these assets. No changes have been made since then. The current policy is set out at the end of Appendix 1 of the Capital Strategy report for information.

30. Given the current economic environment the Council has held discussions with our treasury management adviser, Arlingclose, on whether any further changes can be made to the policy whilst still remaining within the statutory guidance issued by government. The rest of the report will set out an option for change on MRP that will better accommodate the revenue costs of the capital programme and provide greater consistency between supported and unsupported borrowing.

<u>What is MRP?</u>

31. Local authorities are required each year to set aside some of their revenue income as a provision for debt repayment. This is termed the Minimum Revenue Provision. There is a simple duty for a Council each year to make an amount of available, which it considers

"prudent". The MRP Guidance makes recommendations to authorities on the interpretation of that term.

32. Local authorities are asked to prepare an annual statement of their policy on making MRP and to have this approved by their decision-making body before the start of each financial year. This is an important element of the budget setting process each year.

<u>What is a prudent provision?</u>

33. The main part to the guidance is concerned with the interpretation of the term "prudent provision". The guidance proposes several options. It explains that provision for repayment of the borrowing, which financed the acquisition of an asset, should be made over a period bearing some relation to that over which the asset continues to provide a service or has economic benefit. It should also cover the gap between the Capital Financing Requirement (the underlying need to borrow) and the various sources of capital income available to the Council to finance its capital programme, such as capital receipts, capital grants, contributions and direct revenue financing.

34. The current options that government recommend for being prudent are set out towards the end of Appendix 1 (Options 1-5). These differ between supported borrowing (pre-2008 debt) and unsupported borrowing (post 2008 debt). The difference between the two relates to the fact that government provided direct funding for supported borrowing, whereas for unsupported borrowing, these resources need to be provided based on the overall resources allocated to the Council via the local government finance settlement.

<u>Council Policy</u>

35. The current Council policy on MRP is as follows:

- For supported capital expenditure, Middlesbrough Council intends to use option 5 - a 2% annuity basis for the coming financial year. This part of the CFR is currently £80.5m.

- For unsupported capital expenditure, Middlesbrough Council intends to use option 3 - the asset life method for the coming financial year. This part of the CFR is currently £202.8m.

36. The total MRP budget for the 2022/23 financial year is £5.9m or 2.05% of the capital financing requirement.

37. The MRP policy for the Council was last reviewed and changed for the 2016/17 year where a 4% allowance for supported debt was changed to a 2% annuity basis. This policy was backdated to 2008 when unsupported borrowing came into being. This resulted in a total backdated saving of £15m plus a lower on-going cost in earlier years. Increased payments in later years have been factored into the Council's budget projections.

38. On unsupported borrowing, the Council maintained the asset life policy which spreads the revenue charges equally over the life of the assets funded by prudential borrowing.

Annuity Basis of MRP

39. An annuity is a type of financial repayment model which repays a loan amount plus interest over the term of the financial instrument. To ensure certainty, it uses a fixed annual payment. Each year of the loan, a combination of principal and interest are repaid.

40. As there is a fixed repayment period, plus a nominal interest rate on the loan, the annuity calculation splits the individual payments between principal and interest. In earlier years, the repayments are predominantly interest based but as the loan period advances, principal is gradually repaid, and the interest charges become lower. In the latter years of the loan the repayments are predominantly principal. This method of debt repayment is very much akin to a mortgage when the sum borrowed is cleared in the later years of the agreement, at the expense of the first half of the term.

41. Increasingly local authorities are moving to an annuity basis of MRP provision which caters for lower debt repayments in earlier years, with the consequence of greater amounts in later years, recognising that interest paid is higher in the earlier years.

Suggested Future Approach for MRP

42. It is proposed that the Council move to an annuity basis of MRP provision on unsupported debt from 2008. This is the significant part of the Council's capital financing requirement.

43. The 2% annuity basis uses a 50-year financial model to allocate principal and interest payments over the life of the asset but as highlighted above, this results in lower charges for the first half of the asset's life and then higher charges over the remaining period. Conversely, interest payments are higher in the early years. This is advantageous to the Council in the light of rising interest rates where new borrowing is required.

44. The impact of the MRP change will be to improve the management of the revenue budget for capital financing and to smooth the total cost of capital financing over many years.

45. Under regulation we are unable to backdate the policy for prior financial years and the Council will continue to hold MRP already provided on our balance sheet. It will only be future charges that are influenced by the new policy.

Is this change prudent?

46. This policy change is fully compliant with the MRP statutory guidance under Section 21(1A) of the Local Government Act 2003. Many local authorities are using this basis for their current MRP policies on both supported and unsupported borrowing, and it is a method that is recommended by treasury management advisers and accepted by government and regulators.

What decision(s) are being recommended?

That the Corporate Affairs and Audit Committee:

- Discuss the current position on the capital strategy for 2022/23.
- Consider the change being proposed on Minimum Revenue Provision and any comments on this prior to submission to Executive & Council.

Rationale for the recommended decision(s)

47. Although there is no formal decision needs to be made, Members should note the progress to date against the key elements of the capital strategy, and challenge any areas that differ from the original assumptions when the budget was set in February. Emphasis should be paid to the change proposed on Minimum Revenue Provision as this will need to go forward to Executive and then Council for decision to change the policy.

Other potential decision(s) and why these have not been recommended

48. Not appropriate to this report.

Impact(s) of the recommended decision(s)

Legal

49. All activity on capital financing, investments and borrowing is under current local authority powers under either the local government act or the capital finance and accounting regulations

Strategic priorities and risks

50. There are no implications for the policy framework of the Council. The main point to note in relation to risk is that all capital investment, borrowing, and investment decisions are of significant value and thereby of necessity involve a significant degree of financial, credit and interest rate risk. The relevant details are always set out for Members to note in either the capital strategy each year or in the financial instrument elements of the Statement of Accounts.

Human Rights, Equality and Data Protection

51. There are no issues to note on these areas as part of this report.

Financial

52. The financial implications of the various issues covered are highlighted within the main body of the report. The MRP already set aside on the balance sheet will be retained, however, we anticipate that the smoothing impact brought about by the change will lower financing costs on the revenue budget. Any in year savings will be set aside to manage future cost pressures possibly through higher interest rates.

Actions to be taken to implement the recommended decision(s)

Action	Responsible Officer	Deadline
To take forward this report to Executive & then Council on 18 January 2022 for decision.	Head of Finance & Investments	By end of Jan 2022

Appendices

1	Capital Strategy Report – Approved version from the Budget Setting Report – 23 February 2022

Background papers

Body	Report title	Date
Corporate Affairs & Audit Committee	Capital Strategy 2022/23	9th December 2021

Contact: Justin Weston, Head of Finance & Investments
Email: justin_weston@middlesbrough.gov.uk

CAPITAL STRATEGY REPORT 2022/23

Introduction

The Capital Strategy report gives a high-level overview of how capital expenditure, capital financing and treasury management activities contribute to the provision of local public services at the Council. In addition, it also gives an overview of how the associated risks are managed and the implications for future financial sustainability.

The report is a requirement of the 2017 Code of Practice on Treasury Management, issued by the Chartered Institute of Public Finance & Accountancy, and has been produced in an accessible way to enhance members' understanding of these often-technical areas. It is a replacement for the prudential indicator and treasury management report included within previous budget setting reports prior to 2019/20 but gives a wider context on the capital financing processes used by the Council.

The Code above is currently out to consultation by CIPFA but it is not expected that any changes being proposed will impact on the Council's borrowing and treasury management approach.

Capital Expenditure and Financing

Capital Expenditure is where the Council spends money on assets, such as property, IT and vehicles that will be used for more than one financial year. In local government, this also includes spending on assets owned by other bodies, finance leases and loans & grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are generally not capitalised.

- For details of the Council's policy on the capitalisation of assets, see the accounting policies section of the annual statement of accounts on the Council's website (www.middlesbrough.gov.uk).

In the 2022/23 financial year, the Council is planning a total capital expenditure of £124.825m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2020/21 **£000** **Actual**	**2021/22** **£000** **Estimate**	**2022/23** **£000** **Estimate**	**2023/24** **£000** **Estimate**	**2024/25** **£000** **Estimate**
Total Capital Expenditure – Investment Strategy	42.078	59.035	121.325	13.500	9.313
Total Capital Expenditure – Finance Leases	0.000	0.000	3.500	0.500	0.500
Total Capital Expenditure	**42.078**	**59.035**	**124.825**	**14.000**	**9.813**

Governance: Service managers generally bid during the previous financial year to include projects in the Council's forward capital programme. Bids are collated by the Council's finance team who calculate the financing costs of each project (which can be nil if the project is fully externally financed). The Council's Management Team (LMT) appraises all bids based on a comparison of service priorities against financing costs and then makes recommendations to Members for which schemes progress against the capital resources available. The final capital programme to support the Medium Term Financial Plan is then presented to Executive and Council in late February each year for approval.

All capital expenditure has to be financed, from either external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and private finance initiative). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

	2020/21 actual	**2021/22 forecast**	**2022/23 budget**	**2023/24 budget**	**2024/25 budget**
External sources	17.476	27.005	74.344	3.577	0.000
Own resources	6.374	15.158	6.296	5.840	9.313
Debt	18.228	16.872	44.185	4.583	0.500
TOTAL	**42.078**	**59.035**	**124.825**	**14.000**	**9.813**

Any external debt (loans and leases) must be repaid over time by other sources of finance. This comes from the revenue budget in the form of Minimum Revenue Provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace/repay debt finance. The Council generally uses capital receipts to finance new capital expenditure rather than to redeem debt. The total cost of MRP included in the Council's revenue budget is as follows:

Table 3: Minimum Revenue Provision in £ millions

	2020/21 actual	2021/22 forecast	2022/23 budget	2023/24 budget	2024/25 budget
Cost to Revenue Budget	4.743	4.892	5.417	6.485	6.695

- The Council's minimum revenue provision statement for 2022/23 is available towards the end of this report.

The Council's cumulative amount of debt finance still outstanding is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure each year and then reduces with minimum revenue provision and capital receipts used to redeem debt.

The CFR is expected to increase by £38.1m or 14.7% during the 2022/23 financial year. This increase is due to the new capital expenditure funded by external debt of £43.8m less the MRP set aside of £5.4, plus other minor income changes on commercially funded investments.

Based on the above plans for expenditure and financing, the Council's estimated CFR for the period of the Medium Term Financial Plan is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

	31.3.2021 actual	31.3.2022 forecast	31.3.2023 budget	31.3.2024 budget	31.3.2025 budget
TOTAL CFR	**245.966**	**257.747**	**295.865**	**293.463**	286.768

Asset disposals: When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or be used to repay debt. The Council is currently also permitted to spend capital receipts on service transformation projects until 2022/23. Repayments of capital grants, loans and investments also generate capital receipts.

The Council plans to receive £6.1m of capital receipts in the coming financial year as follows:

Table 5: Capital receipts in £ millions

	2020/21 actual	2021/22 forecast	2022/23 budget	2023/24 budget	2024/25 budget
TOTAL	**6.374**	**14.616**	**6.072**	**5.840**	**9.313**

- The level of capital receipts for each financial year is monitored between Regeneration, Finance and Valuation & Estates teams, and any significant changes are reported to Executive as part of the Quarterly budget updates.

- The Council has recently adopted the Flexible Use of Capital Receipts Policy where these proceeds may be used for funding service transformation costs that would otherwise be classed as revenue expenditure. This is mainly to fund the current year's children services overspend and would be a device to protect reserves if required.

Treasury Management

Treasury Management is concerned with keeping sufficient but not excessive cash resources, available to meet the Council's spending needs, while managing the risks involved in these investments. Surplus cash is invested until required, whilst a shortage of cash will be financed by borrowing, to avoid excessive credit balances or overdrafts in the bank current account.

The Council is typically cash rich in the short-term as revenue income is received and before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. Revenue cash surpluses are therefore offset against capital cash shortfalls to reduce the overall borrowing amount required, as part of an integrated strategy on Treasury Management. This is in line with best practice.

The Council at the end of January 2022 had £210.2m of borrowing at an average interest rate of 2.5% and £40.6m of treasury investments at an average rate of around 0.1%.

Both investment and borrowing rates available to the Council continue to be at historic lows due to ongoing government policy plus also the impact of the current coronavirus pandemic. It is expected though that interest rates will start to rise from December 2021 but in a slow, stepped approach. It is thought that this will not have a significant on medium to long term interest rates.

Borrowing strategy: The Council's main objectives when borrowing are to achieve a low but certain cost of finance for long-term capital projects whilst retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between using cheap short-term loans (currently available at variable rates between 0.4% & 0.8%) and long-term fixed rate loans where the future cost is known but interest costs are higher (currently between 1.27% to 2.5%). In recent years, the Council has also been in negotiation with funders around lease arrangements as an alternative method of securing external finance for its capital projects.

Projected levels of the Council's total outstanding debt (which comprises borrowing and relevant finance leases) are shown below, compared with its capital financing requirement (need to borrow).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	31.3.2021 actual	31.3.2022 forecast	31.3.2023 budget	31.3.2024 budget	31.3.2025 budget
External Debt	218.756	213.967	**268.350**	261.622	253.272
Capital Financing Requirement	245.966	257.747	**295.865**	293.463	286.768

Statutory guidance is that debt should remain below the capital-financing requirement, except in the short-term where the benefits of short-term borrowing may be taken. As can be seen from Table 6, the Council expects to comply with this in the medium term with debt being lower than the capital-financing requirement in all relevant financial years. There may be some opportunity to take more capital funding than is needed whilst interest rates are at low levels. Discussions are ongoing with our treasury advisers on this position and what approach the Council should take.

Affordable borrowing limit: The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower “operational boundary” is also set as a warning level should debt levels start to approach the legal limit and is a more realistic rather than worst-case view of what will happen during the financial year. Any need to change these during the 2022/23 financial year from the original budget assumptions will be reported by the Director of Finance to the Executive at the earliest opportunity.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2021/22 limit	2022/23 limit	2023/24 limit	2024/25 limit
Authorised Limit (OB + £30m)	315.000	**356.000**	353.000	347.000
Operational Boundary (CFR + £30m)	285.000	**326.000**	323.000	317.000

Investment strategy: Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

The Council’s policy on treasury investments is to prioritise security and liquidity over yield, which focuses on minimising risk rather than maximising returns. Cash that is likely to be spent in the short term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss.

Table 8: Treasury management investments in £millions

	31.3.2021 actual	**31.3.2022 forecast**	**31.3.2023 budget**	**31.3.2024 budget**	**31.3.2025 budget**
Short-term investments	24.810	23.856	15.630	15.000	15.000
Longer-term investments	0.000	0.000	0.000	0.000	0.000
TOTAL	**24.810**	**23.856**	**15.630**	**15.000**	**15.000**

Governance: Decisions on treasury management in relation to investment and borrowing are made daily and are therefore delegated by the Director of Finance to the Head of Finance & Investments and staff within the central finance team, who act in line with the treasury management strategy approved by Council. Quarterly updates on treasury management activity are reported to Executive as part of the regular budget monitoring process.

Revenue Budget Implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to the revenue budget, offset by any investment income received. The net annual charge is reported as capital financing costs; this is compared to the net revenue stream i.e. the amount funded from council tax, business rates and general government grants. This is an important indicator around the affordability of the Council's capital plans going forwards.

Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream

	2020/21 actual	**2021/22 forecast**	**2022/23 forecast**	**2023/24 forecast**	**2024/25 forecast**
Financing costs (£m)	9.955	9.599	**10.489**	11.159	11.216
Net Revenue Budget (£m)	116.397	116.492	**118.329**	124.541	127.686
Proportion of net revenue stream	8.6%	8.2%	**8.9%**	9.0%	8.8%

Sustainability: Due to the very long-term nature of capital expenditure and its financing, the revenue budget implications of this expenditure incurred in the next few years could extend for up to some 50 years into the future.

The figures in table above remain relatively stable at a time when debt levels for the Council are still increasing. Members should be aware that this is as a result of various capital investments in commercial property made by the Council over the last few years for regeneration purposes. This results in around £2.0m of income per year being credited to the capital financing budget by the end of the 2024/25 financial year. It is imperative and a key budget risk that these rental levels are maintained and the income assumed in the estimates above are generated. Progress will be reported as part of future budget monitoring and performance reports each quarter to Executive. The forecasts above may also differ slightly from the total included in the revenue budget for 2022/23 due to timing.

The Director of Finance is satisfied that the proposed capital programme is prudent, affordable and sustainable because appropriate resources have been allocated from the Council's medium term financial plan, any finance leases have been appropriately vetted and any borrowing plans have been fully costed and reviewed.

Table 10 – Total Borrowing required for each year of the MTFP

	2021/22 £000 Estimate	***2022/23 £000 Estimate***	2023/24 £000 Estimate	2024/25 £000 Estimate
Investment Strategy	15,000	***60,000***	10,000	0
Finance Leases	0	***3,500***	500	500
Debt Restructuring	0	***0***	0	0
Total	15,000	***63,500***	10,500	500

This takes into account any debt needed by the Council to either finance the capital programme, in respect of leasing arrangements, or to finance any debt restructuring required.

Current interest rates at present (with historical lows) mean that this is not possible for the next three financial years and therefore no amounts have been factored into the borrowing plans of the Council for this. If this situation changes, this will be reported to Executive at the earliest opportunity.

The prudential indicators & limits set out in this report are consistent with the Council's current commitments, existing plans and the proposals in the budget report for capital expenditure and financing, and with its approved treasury management policy statement and practices.

The Director of Finance confirms that these are based on estimates of the most likely and prudent scenarios, with in addition sufficient headroom over and above this to allow for operational management and some scope for flexibility. For example unusual cash movements or any unbudgeted capital expenditure required. Risk analysis and management strategies have been taken into account; as have plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes.

Prudence – Treasury Management Indicators

It is recommended that the Council sets an upper limit on its fixed interest rate exposures for 2022/23, 2023/24 and 2024/25 of 100% of its estimated total borrowing undertaken.

It is further recommended that the Council sets an upper limit on its variable interest rate exposures for 2022/23, 2023/24 and 2024/25 of 25% of its estimated total borrowing undertaken.

This means that the Director of Finance will manage fixed interest rate exposures on total debt within the range 75% to 100% and variable interest rate exposures on total debt within the range 0% to 25%.

It is also recommended that the Council sets upper and lower limits for the maturity structure (when the debt needs to be repaid) of its total borrowing as follows.

Amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate at the start of the period:

	Upper limit	**Lower limit**
under 12 months	50%	0%
12 months and within 24 months	30%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and above	90%	20%

Currently investments are limited to a maximum of 3 years, with any deals being arranged so that the maturity will be no more than 3 years and one month after the date the deal is arranged.

The maximum % of the total of all investments that have an outstanding period of one year or longer, at the time the investment is made, is 10%.

Knowledge and Skills

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Head of Finance and Investments has in excess of 20 years' experience in local government treasury management. There is similar experience within the finance teams in relation to budgeting & accounting for capital expenditure and financing. The Council also pays junior staff to study towards relevant professional qualifications including CIPFA, CIMA, ACCA, AAT and other relevant vocational studies.

Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

- Further details on staff training and the policy on the use of external advisers can be seen with reference to its Treasury Management Practices document which is on the Council's website.

Treasury Management Practices

Further details of how the treasury management function operates, the procedures used to manage banking, treasury and capital market transactions, how risk is managed by the in-house team and how this fits with the CIPFA Code of Practice is included in the Council's set of Treasury Management Practices.

This document is available to Members for further information on request.

ANNUAL INVESTMENT STRATEGY

& TREASURY

MANAGEMENT POLICY STATEMENT 2022/23

1. In accordance with revised guidance from the Ministry of Housing, Communities and Local Government (MHCLG) a local authority must prepare and publish an Annual Investment Strategy which must be approved by full Council before the start of the financial year to which it relates.

2. The MHCLG guidance offers councils greater freedom in the way in which they invests monies, providing that prior approval is received from Members by approving the Annual Investment Strategy. The guidance also considers the wider implications of investments made for non-financial returns and how these can be evaluated.

3. The Local Government Act 2003, which also introduced the Prudential Code, requires that a local authority must have regard to such guidance as the Secretary of State issues relating to prudent investment practice.

4. In addition the Chartered Institute of Public Finance & Accountancy (CIPFA) has published a revised Code of Practice for Treasury Management in the Public Services in December 2017. This replaces the 2011 Code which had been adopted in full by Middlesbrough Council. The revised Code requires the Council to clearly state, in the Annual Investment Strategy document, its policy on effective control, and monitoring of its treasury management function. These controls are set out in Treasury Management Practices (TMP's) which have been approved as part of acceptance of the previous Code.

5. The revised Strategy, showing where the Guidance has determined Council policy, can be set out as:

ANNUAL INVESTMENT STRATEGY 2022/23

6. Middlesbrough Council will create and maintain as the cornerstones for effective treasury management:

   - a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities;

   - suitable treasury management practices (TMPs), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

7. The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of this organisation. Such amendments will not result in the organisation materially deviating from the Code's key principles.

8. Middlesbrough Council will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy in advance of the year, a mid-year review which will include an annual report on the previous year, in the form prescribed in its TMP's. Revised Strategies can be presented to the Council for approval at any other time during the year if the Director of Finance considers that significant changes to the risk assessment of significant parts of the authority's investments has occurred.

9. Middlesbrough Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Director of Finance. The execution and administration of treasury management decisions is further delegated to *the Head of Finance & Investments*, who will act in accordance with the organisation's policy statement and TMPs and CIPFA's *Standard of Professional Practice on Treasury Management.*

10. Middlesbrough Council nominates the Corporate Affairs & Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

11. The Council is very circumspect in its use of credit rating agencies with the section on Specified Investments setting out the current policy. Ratings are monitored on a real time basis as and when information is received from either our treasury management consultants or any other recognised source. Decisions regarding inclusion on the Approved List are made on the basis of market intelligence drawn from a number of sources.

12. All staff involved in treasury management will, under the supervision of *the Head of Finance & Investments*, act in accordance with the treasury management practices and procedures, as defined by the Council. Such staff will undertake relevant training, identified during the Council's induction process and, on an on-going basis, the Council's appraisal policy.

13. The general policy objective contained in the guidance is that local authorities should invest prudently the short-term cash surpluses held on behalf of their communities. The guidance emphasises that priority should be given to security and liquidity rather than yield. Within that framework the authority must determine a category of borrowers, who must be of "high credit quality" classified as **Specified Investments**, with whom it can invest surplus cash with minimal procedural formalities and further identify a category of borrowers classified as **Non-Specified Investments**, with whom it can also invest but subject to prescribed limits.

14. Although the guidance definition of Non-Specified Investments is "one not meeting the definition of a Specified Investment", the authority is required to identify which categories of investments are identified as prudent to use and the limits on any such

investment either individually or in total. It is because some organisations do not subscribe to credit rating agencies that they have to be included as Non-Specified Investments, rather than any concern over their creditworthiness.

15. The guidance defines investment in such a way as to exclude pension fund and trust fund investments. In practice, Middlesbrough Council, in its role as Administering Authority for the Teesside Pension Fund, follows similar procedures as approved by Members as part of compliance with the CIPFA Code of Practice, albeit with different limits.

LIMITS & DEFINITION OF SPECIFIED INVESTMENTS

16. The following are currently determined as meeting the criteria for Specified Investments:

17. The investment is made with the UK Government, or a local authority (as defined in the Local Government Act 2003), or a police authority, or fire, or a UK Nationalised Industry, or UK Bank, or UK Building Society.

18. The investment is made with a Money Market Fund that, at the time the investment is made, has a rating of AAA.

19. The investment is made with one of the bodies listed in section 4 of Schedule 1E of the current version of the Treasury Management Practices document which, at the time the investment is made, has a short-term "investment grade" rating with either Standard & Poors, Moody's Investors Search Ltd or Fitch Ratings Ltd (or in the case of a subsidiary the parent has such a rating). Where ratings awarded differ between the rating agencies any one award below investment grade will prevent the investment being categorised as a Specified Investment. The rating of all listed bodies must be monitored on a monthly basis. Where officers become aware of a downward revision of rating, that moves the body out of the "investment grade" category, between such monthly checks, the body should be removed from the list of Specified Investments and, if considered appropriate, the investment should be recalled.

20. All specified investments must be denominated in sterling and must be one where the authority may require it to be repaid or redeemed within 12 months of the date on which the investment is made and must be considered of high credit quality. This is defined as having met the criteria set out above. The investment must not constitute the acquisition of share capital or loan capital in any body corporate.

- The minimum % of the total of all investments which must be Specified Investments, at the time the investment is made, is 70%
- The maximum investment with any one counterparty is £15 million, except for the Debt Management Office which is has no limit.

- The maximum investment in any one group (i.e. a bank and its wholly-owned subsidiaries) is £15m.

LIMITS & DEFINITION OF NON-SPECIFIED INVESTMENTS

21. These categories of investment currently meet the criteria for non-specified investments:

22. The investment is made with a UK bank, or UK building society, or a UK subsidiary of an overseas bank.

23. The investment is made with one of the bodies listed in section 4 of Schedule 1E of the current version of the Treasury Management Practices document, which is not a Specified Investment.

24. The investment is for a period of one year or longer.

25. All non-specified investments must be denominated in sterling. The investment must not constitute the acquisition of share capital or loan capital in any body corporate.

- The maximum % of the total of all investments which can be non-specified investments, at the time the investment is made, is 30%.
- The maximum investment with any one counterparty is £15 million
- The maximum investment in any one group (i.e. a bank and its wholly-owned subsidiaries) is £15m.
- The maximum % of the total of all investments that have an outstanding period of one year or longer, at the time the investment is made, is 10%.

26. The maximum period for which an investment can be made is 3 years, with the maturity date no more than 3 years and 1 month from the time the deal is agreed.

27. As referred to earlier in the report, borrowing should be kept at, or below, the expected capital financing requirement over the medium term to reduce the risk of exposure to interest rate fluctuations. The balance of ‘net borrowing’ (loans less investments) should also be monitored to, where prudent, minimise interest rate differences.

28. The Council considers that it is empowered by Section 12 of the Local Government Act 2003 for the temporary investment of funds borrowed for the purpose of expenditure in the reasonably near future. While not “borrowing to invest” it is prudent to invest monies raised in advance of expenditure. As required by the Guidance such

investment is permitted providing the anticipated expenditure is within this or the next financial year or within a period of eighteen months, whichever is the greater.

TREASURY MANAGEMENT POLICY STATEMENT

29. Middlesbrough Council defines its treasury management activities as:
'The management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.'

30. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation and any financial instruments entered into to manage those risks.

31. The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

32. The high-level policies and monitoring arrangements adopted by the Council for Borrowing and Investments are as follows:

Borrowing

- Any borrowing decisions will aim to strike an appropriate risk balance between securing low interest rates and achieving cost certainty over the periods for which funds are required. Economic forecasts available from our treasury management advisers and any other available sources will be used to form a view on the target borrowing rates and overall borrowing strategy;
- Any decisions should also look to maintain the stability and flexibility of the longer term debt portfolio, given the current low interest rate environment where short term borrowing or borrowing from internal resources offer revenue budget savings;
- The main sources of funding for external borrowing for the Council are the Public Works Loan Board, Other Local Authorities and private sector financial institutions;

Investments

- The CIPFA and MHCLG guidance require the Council to invest its funds prudently and to have regard to security, liquidity and yield when making these decisions;
- Security being the arrangements in place to protect principal sums invested by a local authority;
- Liquidity being to ensure that enough cash resources are available on a day to day basis for transactional needs;

- Yield being the interest rate and total financial return applicable to the investment being made;
- With these strategic issues in mind, the management of credit risk (or security) is key to the Council’s investment strategy and any subsequent activity. The Council uses the external advisers’ credit worthiness matrix to determine limits with individual counterparties.

MINIMUM REVENUE PROVISION POLICY 2022/23

INTRODUCTION

33. Local authorities are required each year to set aside some of their revenue income as provision for debt repayment. There is a simple duty for an authority each year to make an amount of revenue provision, which it considers “prudent”. (Minimum Revenue Provision) MRP Guidance makes recommendations to authorities on the interpretation of that term.

34. Authorities are legally obliged to “have regard” to any such guidance – which is exactly the same duty as applies to other statutory guidance including, for example, the CIPFA Prudential Code, the CIPFA Treasury Management Code and the CLG Guidance on Investments.

35. Authorities are asked to prepare an annual statement of their policy on making MRP and to have this approved by the body before the start of each financial year.

MEANING OF “PRUDENT PROVISION”

36. The main part to the guidance is concerned with the interpretation of the term “prudent provision”. The guidance proposes a number of options. It explains that provision for repayment of the borrowing, which financed the acquisition of an asset, should be made over a period bearing some relation to that over which the asset continues to provide a service or has economic benefit. It should also cover the gap between the Capital Financing Requirement and the various sources of capital income available to the Council to finance its capital programme, such as capital receipts, capital grants, contributions and direct revenue financing.

OPTIONS FOR PRUDENT PROVISION

Option 1: Regulatory Method

37. For debt supported by (Revenue Support Grant) RSG in previous years, authorities will be able to continue to use the formulae in regulations, since the RSG was provided on that basis.

Option 2: CFR Method

38. This is a technically simpler alternative to Option 1 and may also be used in relation to supported debt. While still based on the concept of the Capital Financing Requirement (CFR), which can be derived from the balance sheet, it avoids the complexities of the formulae in the regulations.

Option 3: Asset Life Method

39. For new borrowing under the Prudential system (from 2008) for which no government support is given, there are two main options. Option 3 is to make provision for debt repayment in **equal annual instalments** over the estimated life of the asset for which the borrowing is undertaken. This is a possibly simpler alternative to the use of depreciation accounting (Option 4), though it has some similarities to that approach.

40. The formula allows an authority to make **voluntary extra provision** in any financial year that this is affordable.

41. In the case of the construction of a new building or infrastructure, MRP would not need to be charged until the new asset comes into service. This "**MRP holiday**" would be perhaps 2 or 3 years in the case of major projects and could make them more affordable. There would be a similar effect in the case of Option 4 under normal depreciation rules.

Option 4: Depreciation Method

42. Alternatively, for new borrowing under the prudential framework for which no Government support is being given, Option 4 may be used. This means making MRP in accordance with the standard rules for depreciation accounting.

43. Councils will normally need to follow the standard procedures for calculating depreciation when making this revenue provision.

Option 5: 2% Annuity Method

44. This method recognises the time value of money and the useful life of the assets funded from borrowing and is seen as a fairer way of charging MRP. It is supported by the Council's treasury management advisers (Arlingclose) and is being adopted by many local authorities nationally as the way of accounting for pre 2008 debt.

2022/2023 MINIMUM REVENUE PROVISION -

STATEMENT FOR MIDDLESBROUGH COUNCIL

45. The Secretary of State recommends that before the start of each financial year a local authority prepares a statement of its policy on making MRP in respect of that financial year and submits it to the full council as part of its budget setting process. The statement should indicate which of the options listed above are to be followed in the financial year.

46. For supported capital expenditure Middlesbrough Council intends to use option 5, a 2% annuity basis for the coming financial year.

47. For unsupported capital expenditure Middlesbrough Council intends to use option 3, the asset life method for the coming financial year.