

Report of:	Interim Director of Finance (S151 Officer)
Submitted to:	Audit Committee
Date:	6 October 2023
Title:	Update on Audit of Accounts progress
Report for:	Information
Status:	Public
Strategic priority:	All
Key decision:	Not applicable
Why:	Report is for information only
Urgent:	Not applicable
Why:	Not applicable

Executive summary

This report updates the Committee on the current progress with the 2021/22 external audit of the Council's Statement of Accounts. This is in the light of much longer audit processes for the previous two sets of accounts for 2019/20 and 2020/21. In addition, the Council's draft Statement of Accounts for 2022/23 has not yet been published due to the need to take account of audit adjustments to the 2021/22 ongoing audit.

The issue of local authority statutory audits over-running and being significantly behind statutory deadlines is not just an issue affecting this Council but is a national one faced by many local authorities. The report sets out the main reasons for the delays and gives some information to allow Members to understand the scale of the national problem facing local government.

The Department for Levelling up Homes and Communities (DLUHC) has set out proposals to address the audit backlog for consultation. The measures ultimately taken could have significant implications for the current and future audits of statutory accounts and impacting upon local authority finance teams, external auditors, and Members as they consider and approve sets of accounts going forward.

Purpose

1. To update the Committee on the audit of the Council's Statement of Accounts and provide new information on action proposed by DLUHC to address the current audit backlog.

Background and relevant information

2. This report provides an update on the outstanding audit of the Council's Statement of Accounts for 2021/22. In addition, the Council draft accounts for 2022/23 have yet to be finalised for publication although the statutory date for doing this was 31 May 2023.
3. There is also an update from DLUHC in relation to the national backlog of audits currently outstanding within the local government sector and initial proposals on how to address this.
4. The completion of the external audit of the Council's last two years financial statements and value for money assessment took significantly longer to finalise than in previous years:
 - a. For 2019/20, this was completed on 2 March 2021 (the statutory date for these audited accounts was 30 November 2020).
 - b. For 2020/21, this was completed on 29 April 2023 (the statutory date for these audited accounts was 30 September 2021).

In previous years to these, the statutory deadlines had been achieved.

5. The reasons for the delays have been reported to this Committee several times before. However, for new members of the Committee, these can be grouped into three main categories:
 - 1) Onerous regulatory requirements for external auditors, mainly from the National Audit Office and the Financial Reporting Council. This has required extensive additional work to be undertaken and evidence to be gathered by auditors as part of their examination of the Council's financial statements and transactions. This has been in response to a high number of corporate failures in the private sector.
 - 2) A significant amount of additional work has been required on the value for money assessment, mainly in relation to the Ofsted judgement on the quality of Children's Services being delivered by the Council, and the governance issues within the Council which has recently led to a set of statutory recommendation being issued.
 - 3) Extra work, evidence and focus on the Going Concern Assessment, given the well-publicised issues on local authorities and their financial sustainability.
6. In addition, there have been resource constraints and recruitment issues within both the Council's financial team and for Ernst & Young (EY), our external auditors, over most of this period.
7. Prior to this, in June 2019 the then known Ministry of Housing, Communities and Local Government, commissioned a review of the effectiveness of local audit and the

transparency of local authority financial reporting. The review, published in September 2020, is known as the Redmond Review. A report to this Committee on 4 March 2021 which gives further details. The timing of that review indicated that there were issues with the local audit market before the impact of the pandemic, namely the growing regulatory demands on audit partners for additional diligence in their review of all systems supporting the production of an authority's accounts. The additional work placed upon authorities to respond to the pandemic and associated accounting and reporting requirements, further compounded the challenges and resulting delays that were already prevalent in audits of the local government sector. Similar themes to those highlighted above.

The Accounts and Audit Regulations

8. The Accounts and Audit Regulations 2015 set out the detailed requirements for local authorities in relation to its annual audit and accounting processes. From the outset of the pandemic in 2020, the Government have extended the deadlines for producing a draft set of accounts and for those accounts to be audited.
9. The following table sets out the dates the Council published its draft accounts in comparison to the required statutory dates:

Financial Year	Due date	Published date
2022/23	31/05/2023	Pending
2021/22	31/07/2022	08/08/2022
2020/21	31/07/2021	20/07/2021
2019/20	31/08/2020	16/07/2020
2018/19	31/05/2019	24/05/2019
2017/18	31/05/2018	23/05/2018
2016/17	31/05/2017	23/05/2017

10. The deadline for publication of the draft accounts for 2022/23 was consulted on by DLUHC during April 2023 due to some concerns as to whether this could return to normal following the pandemic. The outcome of this was announced on 3 April 2023 and the deadline returned to 31st May date. There is no penalty for failing to meet the statutory deadlines. However, it is important for local authorities and their stakeholders to have assurance of the Council's financial position and therefore timely reporting and audit is an essential aspect of robust financial management. For recent years the statutory deadlines can be summarised as:

Financial Year	Draft Accounts	Audited Accounts
2018/19	31-May	30-Sep
2019/20	31-Aug	30-Nov
2020/21	31-Jul	30-Sep
2021/22	31-Jul	30-Nov
2022/23	31-May	30-Sep

11. The percentage of Councils that met these dates in 2021/22 was 9% of English local authorities for the draft accounts and for the audited accounts was 12%, even though the deadline was re-aligned back two months to 30 November, from the 30 September the previous year.

12. The table below shows the recent data on (A) the number of audit opinions that remained outstanding and (B) the proportion of audits that were completed by the audit deadline.

Financial Year	(A) Outstanding audits at 30 Nov 2022	(B) % of audits completed by the due date
2015/16	1	97%
2016/17	1	95%
2017/18	3	87%
2018/19	10	57%
2019/20	45	45%
2020/21	161	9%
2021/22	411	12%

13. Despite the obvious difficulty for local authorities to meet the less stringent deadlines of the past 3 years, the revised deadline has been reduced by 2 months for the financial year 2022/2023 to reinstate the original statutory deadline of 31 May. The Council has not yet issued the draft statutory accounts due to the need to take account of audit amendments that are likely to flow from the 2021/22 audit.

Update form DLUHC (July 2023)

14. Lee Rowley, the parliamentary under-secretary of state for local government and building safety, outlined proposals in a letter to Clive Betts, chair of the Levelling Up, Housing and Communities (LUHC) Committee inquiry into financial reporting and audit in local authorities. The proposals include setting statutory deadlines and issuing qualifications and disclaimers of opinion in the short term.

15. Working together, the National Audit Office (NAO) and DLUHC intend to set a series of statutory deadlines for accounts preparers and auditors to clear the backlog of delayed audits for financial years 2015/16 to present.

16. It should be noted that it has been highlighted that to achieve these deadlines, it may result in qualifications and disclaimers of opinions on statutory accounts in the short term for a number of local bodies.

17. DLUHC confirm that the proposals have been agreed in principle with key partners across the local audit system. The National Audit Office (NAO) is considering whether to develop a revised Code of Audit Practice to give effect to the changes. Legislative change may also be needed to address any knock-on effects of the proposals which may impact the audit of opening balances within the accounts for future years. Under these proposals, Section 151 officers will be expected to work with Audit Committee members to approve the final accounts by the statutory deadline for the audit opinion to be issued at the same time.
18. The proposed deadlines being considered for audit completion (or 'backstop' dates) are set out as follows but it should be noted that these are not yet confirmed:

Financial Year	Deadline
2015/16 – 2019/20	31/12/2023
2020/21 – 2021/22	30/03/2024
2022/23	30/09/2024
2023/24	31/03/2025
2024/25	30-09/2025

Statement of Accounts audit for 2021/22 & Draft Accounts for 2022/23

19. The draft Statement of Accounts for 2021/22 was authorised for issue by the former Director of Finance on 8 August 2022. They were subsequently presented to this Committee on 29 September 2022. EY have been working on the 2021/22 audit of accounts with the internal finance team since the start of September 2022. There was a period of concentrated work on this audit between early September 2022 and the end of March 2023. At that point, the audit was paused to allow the finance team to focus on the closure of accounts process for 2022/23 and to prepare a draft Statement of Accounts for the latest financial year.
20. At the end of March 2023, a significant number of queries had been received on the draft 2021/22 accounts and responded to (200+). The bulk of the key audit items (review of the Statement of Accounts full document, review of the individual financial statements and notes to the accounts prepared, initial work on value for money, sampling of year end accruals, etc.) had been either completed or advanced to a satisfactory degree. Weekly meetings had been undertaken between EY and the Council's finance team to review both queries raised and the overall progress on the audit. At present, around two thirds of the audit fieldwork have been completed.
21. The audit for 2021/22 was due to re-commence in mid-July 2023, post the closure of accounts for 2022/23. Due to the announcement by DLUHC in relation to the proposed re-set of the audit market and the need for external audit firms to respond in terms of the impact upon their scheduling of all outstanding audits, EY have not re-started this work. At the end of September, no further work has been undertaken on the financial statements audit, apart from a specific review of the Collection Fund bad debt provision methodology in line with changes in accounting standards requested by the s151 Officer to enable finalisation of the 2022/23 draft accounts as set out below. EY may be able to give a further verbal update at the meeting and their plans to complete the 2021/22 financial statements audit.

22. There are several key areas within the 2021/22 audit that still need to be completed. One area that EY have been working on relates to the Collection Fund Bad Debt provision. The debt on both council tax and business rates is around £50m in total, so any judgement on the level of bad debt provision is significant. The Council reviewed its bad debt provision formula in 2021/22 because of comments made on the previous year's audit and a general recognition that the existing provision was overstated in comparison to neighbouring authorities.
23. Also, given recent changes in relation to IAS 37 on provisions and contingent liabilities, the accounting standard that informs the local authority accounting code in this area, a stronger link was needed between the provision being held in the accounts and the actual collection of council, tax, and business rates debts from within the local community. The final bad debt provision included within the 2021/22 accounts was around £36m. This included the element of a new formula and a buffer for future collection issues, following the pandemic. Officers are in discussion with the external auditor in relation to this change which could result in a material adjustment to the 2021/22 accounts and will need to be fed through the 2022/23 draft accounts.
24. As a result of this potential audit adjustment and any possible changes needed for opening balances for the 2022/23 accounts, plus the delay in restarting the 2021/22 audit whilst awaiting further details from DLUHC, the Director of Finance has decided that the 2022/23 accounts will be published once the adjustment has been determined to enable her to be satisfied that the accounts present a true and fair view of the Council's financial position at 31 March 2023. It is anticipated that the 2022/23 draft pre audited accounts will therefore be signed and issued before the end of this calendar year to enable the audit to commence subject to EY's planned approach. and will be brought for consideration by this Committee at the earliest opportunity thereafter.

What decision(s) are being recommended?

This report is for information only. No decisions are required from Members.

Rationale for the recommended decision(s)

25. Given that the audit for the 2021/22 accounts and preparation of the 2022/23 accounts are currently out of cycle and behind the statutory dates. It is useful for the Committee to receive regular updates on progress and to consider the implications and any actions required.

Other potential decision(s) and why these have not been recommended

26. Not Applicable for this report.

Legal Implications

27. The publication of the draft statement of accounts is a legal requirement under the Accounts & Audit Regulations 2015.
28. As the Council is not currently achieving the statutory dates for the audit of its accounts, a notice has been included on the Council website to this effect in line with

the regulations. This allows any stakeholders to be aware of this position, when looking for or reviewing the Accounts. The 2015 regulations allow for this and the audit of the accounts to continue under this provision.

Strategic priorities and risks

29. As the Statement of Accounts covers all financial transactions of the Council and various other corporate financing reporting responsibilities, it encompasses all strategic priorities and risks.

Human Rights, Equality and Data Protection

30. There are no relevant considerations in these areas in respect of this report.

Financial Implications

31. The Council has a corporate budget for external audit fees. This has been under significant pressure in recent years due to the length of recent audit processes and the additional workload required from the auditors to give an opinion on both the financial statements and the value for money assessment.

32. The table below was included by EY in their 2020/21 annual audit letter and illustrates the scale of the fee increases in recent years. The note references are not appropriate for the purposes of this report.

Description	Final Fee	Planned Fee	Final Fee
	2020/21	2020/21	2019/20
	£	£	£
Base scale fee – Council (note 1)	88,578	88,578	88,578
Base scale fee - Pension Fund (note 1)	21,972	21,972	21,972
Increase for changes in risk and regulatory environment – Council (notes 2,3,8)	81,850	-	53,960
Increase for changes in risk and regulatory environment – Pension Fund (notes 2,3,8)	39,359	-	14,033
Revised base fee	231,759	110,550	178,543
IAS 19 procedures (Code work) (notes 4,5)	8,500	N/A	6,000
IAS 19 procedures (non-Code work) (notes 4,5)	-	N/A	2,000
Revised base fee (inc. IAS 19 procedures)	240,259	110,550	186,543
Additional audit fee for response to specific audit findings – Council (notes 6,7,8)	184,572	-	20,745
Additional audit fee for response to specific audit findings – Pension Fund (notes 6,7,8)	5,000	-	5,202
Total audit fee	429,831	110,550	212,490
Non-audit services – Housing Benefit certification work	13,450	N/A	12,800
Non-audit services – Teachers Pension certification work	5,250	N/A	5,000
Total fees	448,531	110,550	230,290

33. The audit fees are set by the Public Sector Audit Appointments (PSAA), the government agency responsible for managing the external audit contracts nationally with audit firms. For the Council, they consist of base (scale) fee for auditing the

Council and a separate fee for auditing the Teesside Pension Fund. For both 2019/20 and 2020/21, these were set at a total of £110,550.

34. Due to changes in the risk and regulatory environment and additional work required in relation to the value for money assessment, fees have increased. Additionally, EY have undertaken work in respect of several grant claims on behalf of relevant bodies. The total fees payable has ended up much higher than the original base levels set by PSAA. £230,290 for the 2019/20 audit and £448,531 for the 2020/21.
35. As audit work is performed once the relevant financial year's accounts are closed, in general these costs for accounted for one year in arrears in line with when the audit work is undertaken. The costs for the 2021/22 audit were accounted for in the 2022/23 accounts and the costs for the 2022/23 audit will be accounted against the current financial year 2023/24 and 2024/25 financial year. Given the ongoing nature of the audit for 2021/22, an estimate was made in 2022/23 accounts for the total expected cost of the audit. This was estimated at a total of £400,000 to reflect a similar cost for the financial statements' element but a slightly reduced cost on the value for money work, but this will only be known with certainty once the audit is complete.
36. A similar estimate of £400,000 is also being used for the 2022/23 audit with costs expected to fall at the latter end of 2023/24 and into 2024/25. as this information is required as part of the current budget monitoring process. The allocated budget for audit fees is £182,000, resulting in a £218,000 overspend. This is being managed as part of the overall corporate financial position for the Council.
37. PSAA undertook the latest national procurement of audit contracts during 2022. These contracts commence from the 2023/24 audit. As part of the roll-out of the new contracts, they need to consult with audited bodies on the recommended level of base fees to charge for the financial year. Given the fact that these fees have become outdated and are not in line with the actual work involved as part of the external audit, it is not a surprise that PSAA have taken the opportunity to increase these significantly.
38. The 2023/24 fees being consulted on for Middlesbrough are £321,074 for the Council audit and £102,380 for the Teesside Pension Fund audit. A total of £423,454. This would bring the fees broadly in line with the last fully complete external audit and just slightly higher than current expected costs. The additional costs will need to be incorporated into the Medium-Term Financial Planning process, as the first financial year these increased base fees will affect is 2024/25.

Actions to be taken to implement the recommended decision(s)

Action	Responsible Officer	Deadline
Not Applicable for this report		

Appendices

1	There are no appendices to this report
---	--

Background papers

Body	Report title	Date
Corporate Affairs & Audit Committee	Draft Statement of Accounts 2021/22	29 September 2022
Corporate Affairs & Audit Committee	Audited Statement of Accounts 2020/21	29 April 2023

Contact: Justin Weston, Head of Finance & Investments
Email: justin_weston@middlesbrough.gov.uk