

AUDIT COMMITTEE

A meeting of the Audit Committee was held on Thursday, 3 October 2024.

PRESENT: Councillors J Ewan (Chair), B Hubbard (Vice-Chair), I Blades, D Branson, D Coupe, G Wilson and L Young.

ALSO IN ATTENDANCE: C Andrew (Forvis Mazars)
P Jeffrey (Internal Auditor) (Veritau)
M Kirkham (Forvis Mazars)
M Rutter (External Auditor) (Ernst Young).

OFFICERS: C Benjamin, C Heaphy, A Johnstone, S Lightwing and J Weston.

APOLOGIES FOR ABSENCE: None.

24/26 **WELCOME AND EVACUATION PROCEDURE**

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

24/27 **DECLARATIONS OF INTEREST**

| MEMBER | TYPE OF INTEREST | ITEM/NATURE OF INTEREST |
|----------------------|------------------|---|
| Councillor J Ewan | Non Pecuniary | Agenda Item 10 Member of Teesside Pension Fund |
| Councillor B Hubbard | Non Pecuniary | Agenda Item 10 Member of Teesside Pension Fund |

24/28 **MINUTES - AUDIT COMMITTEE - 22 AUGUST 2024**

The minutes of the Audit Committee meeting held on 22 August 2024 were submitted and approved as a correct record.

24/29 **CORPORATE GOVERNANCE IMPROVEMENT PLAN AND SECTION 24 ACTION PLAN PROGRESS REPORT**

A report was presented that set out the key activities and progress since the last update to Committee, in response to the Section 24 recommendations made by the Council's External Auditors and the Council's Corporate Governance Improvement Plan.

Overall performance in relation to delivery of activity across the two improvement plans (excluding activity not yet planned to start and not due to be delivered yet), was set out at paragraph 5.2 of the submitted report. Ninety-nine percent of planned activity had either been delivered or was on-track for delivery in relation to the Corporate Governance Improvement Plan, with one planned activity across the ten workstreams measuring as off-track. In relation to the off-track action, further information was awaited from Grant Thornton prior to progressing with a model of finance.

One hundred percent of activity in relation to the Section 24 delivery plan was on-track or had been delivered. It was highlighted that the report stated at paragraph 5.4 that there was one activity showing as off-track. This was an error in the report. The action related to the recruitment of two senior officers which was on track to be completed by March 2025.

A Member asked whether the Senior Management Review had been completed. The Chief Executive explained that the Senior Management Review had not yet been undertaken. Following agreement with the Mayor of the target operating model, the Review would be

undertaken.

A Member highlighted that in relation to cultural transformation and sustainable leadership the impact trend was stated as “Worse”. It was explained that one of the measures for this activity was the number of agency staff employed and unfortunately this had increased in areas including waste services and public health.

It was also noted that the data had not been updated in relation to setting a balanced budget for 2024/2025 to 2026/2027. The Chief Executive clarified that the budget setting process had started and proposals would be presented to the Executive in December 2024.

The Chair asked when the report from Grant Thornton would be received and the Chief Executive explained that whilst the report had formed the basis of the decision not to renew the Best Value Notice, and the Government had stated that the Council could have sight of it, the report had not yet been forthcoming.

AGREED that the Audit Committee noted the progress against the Corporate Governance Improvement Plan and Section 24 Action Plan.

24/30

BEST VALUE NOTICE - UPDATE

A report of the Chief Executive was presented to update the Committee on the Government's decision not to renew the Council's Best Value Notice and the planned further report to Council which would set out the next steps.

Government issued a Best Value Notice to the Council in January 2023 which was extended in January 2024. Progress against that Notice had been well documented to the Audit Committee and full Council, through regular reports on the delivery of both the Corporate Governance Improvement Plan and the action plan put in place to respond to the External Auditor's Section 24 report.

As a result of the progress the Council had made to date in addressing the issues raised, the Ministry of Housing, Communities and Local Government had decided that it would not renew the Best Value Notice that was in place. The Chief Executive and Committee Members acknowledged the work that had been undertaken by the Council to reach this position.

A Member raised a query in relation to the financial cost to the Council of the improvement work and the Chief Executive agreed to provide this information.

Work would continue with the Improvement Board until March 2025 and also work in terms of monitoring the Council's financial position in terms of this year's budget and beyond.

A copy of the letter outlining government's decision was appended to the submitted report for information.

A typo was highlighted in the recommendations of the report at paragraph 2.1, second line – the word “review” to be replaced with “renew”.

AGREED as follows that:

1. Audit Committee noted the Government's decision not to renew the Council's Best Value Notice
2. Audit Committee noted the Planned next steps in the Council's ongoing improvement journey.
3. Information in relation to the cost to the Council for the improvement journey would be provided to the Audit Committee.

24/31

INTERNAL AUDIT AND COUNTER FRAUD PROGRESS REPORT

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

The internal audit progress report was contained in appendix 1 of the submitted report. This

included a summary of current work in progress, internal audit priorities for the year, completed work, and follow-up of previously agreed audit actions.

The Auditor highlighted that in relation to audits in progress, it was anticipated that the final report on Agency Staff (Children's Services) would be completed in the next few weeks.

Annex C to the submitted report provided a summary of key issues from audits finalised since the last report to the Audit Committee.

The Audit opinions and priorities for actions detailed at Annex D to the submitted report had been updated, with a new category – Opportunity – added.

A summary of progress against previously agreed actions was included at Annex E to the submitted report and of the 6 actions outstanding, all 6 had had a revised date agreed.

In relation to the planned audit of Members' allowances and declarations of interest, a member asked whether Officers' interests could also be audited. The Auditor agreed to check with Officers to see where there was capacity to add this to the planned work.

Home to School Transport was listed as Category 3 audit priority and a Member commented that this topic was currently being investigated by scrutiny and it might be useful for Internal Audit to feed their findings into the scrutiny review.

The counter fraud progress report was attached at Appendix 2 of the submitted report. 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 counter fraud team and Council officers worked together as part of an annual National Blue Badge Day of Action in May 2024. Checks were made on 53 badges in Middlesbrough town centre to confirm they were being used lawfully and two penalty charge notices were issued. The team had completed four investigations into blue badge misuse in 2024/2025 resulting in warnings being issued to three people.

It was highlighted that investigative work to date in 2024/2025 had helped identify £70k of loss due to fraud, error and debt evasion. The counter fraud team supported the Council to recover losses identified as part of investigations. Counter fraud savings were also tracked by monitoring repayments to the Council and calculating the value of stopping ongoing frauds. To date £68k of counter fraud savings had been identified, which was twice the amount found in 2023/24.

AGREED that the latest update on internal audit and counter fraud work was noted by the Audit Committee.

24/32

BACKSTOP PROGRESS ON THE 2021/22 AND 2022/23 STATEMENT OF ACCOUNTS APPROVAL

The Head of Finance and Investment provided the Audit Committee with an update on Backstop Progress on the 2021-2022 and 2022-2023 Statement of Accounts (SOA).

As previously notified, the external audits of the Council's 2021/22 and 2021/22 draft SOA, had been delayed for some time pending government direction on how to address the national backlog. This applied to over 1,000 sets of unsigned local authority accounts across the country, with many local authorities being in a similar position to Middlesbrough of having more than one set of accounts not being audited.

The government had now set out and laid the legislation (9 September 2024) in relation to the statutory backstop dates. These were the dates by which an external audit for a particular financial year needed to be finalised.

The first backstop date (13 December 2024) would clear the backlog of unaudited accounts up to and including 2022/23. Where auditors had been unable to complete audits, they would issue a 'disclaimed' or 'modified' audit opinion. Auditors were likely to issue hundreds of 'disclaimed' audit opinions and needed to make clear that this is not the fault of the organisation involved but of issues with the local audit system itself.

The five further backstop dates up to and including financial year 2027/28 allowed full assurance on external financial reporting to be rebuilt over several audit cycles. It was the aspiration of the Government and key local audit system partners that, in the public interest, local audit recovered as early in this five-year period as possible. This meant disclaimed opinions driven by backstop dates should, in most cases, be limited to the next two years (up to and including the 2024/25 - backstop date of 27 February 2026), with only a small number of exceptional cases, continuing thereafter.

While there would be modified or disclaimed opinions in relation to the external audit of financial statements, auditors' other statutory duties – including to report on Value for Money (VfM) arrangements, to make statutory recommendations, and to issue Public Interest Reports – remained a high priority.

For Middlesbrough Council, the 2021/22 accounts audit was partially undertaken by Ernst & Young (EY) between July 2022 and March 2023. At that point the audit was paused, given the Council's finance team had to close down and prepare the 2022/23 accounts. The audit should have restarted by July 2023 but did not, due to central government considering what to do about the backlog position nationally and there being uncertainty for external auditors about how to continue.

No further work had been carried out on the Council's financial statements for 2021/22 since March 2023, except for a specific piece of work requested by the S151 Officer in relation to the collection fund bad debt provision. EY had however continued their work on the Value for Money assessment and on the Teesside Pension Fund. Both audits were progressing to a conclusion and the issue of the appropriate audit opinion.

Since the issue of the government legislation, EY had indicated that they could not give formal assurance on the 2021/22 council financial statements given the amount of work undertaken to date. As a result of this, the audit opinion on these statements would be 'disclaimed'.

In relation to the 2022/23 external audit process, the position was very similar to 2021/22. The work on the Value for Money assessment and the Teesside Pension Fund, would be completed and reported to Members. Work on the audit of the Council financial statements had not started given the delay on the 2021/22 accounts. As a result, those financial statements would also be disclaimed in line with 2021/22.

The Value for Money interim results for 2021/22 and 2022/23 had been reported to the Audit Committee on 25 July 2024. The results of the Teesside Pension Fund work for these years (including a finalised audit opinion) would be reported to a future meeting of the Audit Committee.

EY had provided further details on the process for disclaiming the financial statements audits for 2021/22 and 2022/23. Given the number of potential disclaimed opinions needing to be issued, this work was being undertaken by a central disclaimer hub rather than the local EY team. The information required would be submitted by the Council as soon as possible.

In terms of the 2021/22 and 2022/23 years, the financial statements and notes had been updated following of the conclusion of EY's work on the revision to the bad debt provision on council tax and business rates. Since these were material adjustments to the accounts, it was necessary for the responsible officer to re-certify the statement of responsibilities within the SOA document. This was actioned by the Director of Finance on Tuesday 24 September 2024 and updated versions of these accounts would be published on the Council website. These restatements were important since they influenced the opening balances for the 2023/24 accounts.

Once the legacy statements of accounts for 2021/22 and 2022/23 had been reviewed by the EY disclaimer hub, disclaimed opinions would be issued by the external auditor to finalise the audit process for these financial years. These would accompany the value for money opinion and the true and fair view on the Teesside Pension Fund accounts. The approval process for the audited accounts would then follow the normal process under the Accounts and Audit Regulations 2015.

The External Auditor, EY, commented that whilst the opinion on the financial statements was

expected to be disclaimed there were still certain actions to be completed, including obtaining representations from management, in order to ensure compliance with the legislation. Whilst there had been a slight delay in obtaining some of the information, the Auditor was confident that the reports on the disclaimer and Teesside Pension Fund accounts would be finalised for reporting to the next Audit Committee meeting.

A Member asked whether the Covid-19 pandemic had impacted on the audit process. The Head of Finance and Investment stated that the pandemic had only caused a minor hold-up. The reason for delay was mainly due to complexity in the local audit and financial markets which had got progressively worse over a period of time and was a national issue. In terms of future, the finance team were very confident that the Council would meet the deadlines in terms of preparation. The statutory dates had moved from the end of May to the end of June. Additional investment had been made into the finance team to ensure there was sufficient capacity.

A Member asked whether the bad debt provision took account of the outstanding business rates. It was explained that the Council had a methodology to state the amount of debt within a financial year and how that would be provided for. A fair provision for the level of debt outstanding was included in the accounts and the auditors would examine that provision to check it was fair. An active team continued to pursue debts from current and previous years and they would only be written off when it was no longer viable to chase them.

The Chair asked whether there would be any saving on audit fees. The External Auditor stated that the Council and taxpayers would not be charged for audit work that had not taken place. Dialogue would take place with the Auditors and the Public Sector Audit Appointments (PSAA) and the views of the Chief Executive and Section 151 Officer would be included in discussion.

AGREED that the position on the 2021/22 and 2022/23 external audit processes, and the subsequent steps required to finalise and approve the accounts for these years before the statutory backstop date of 13 December 2024, was noted by the Audit Committee.

24/33

FORVIS MAZARS PROGRESS REPORT - 2023/24

A report of the External Auditor was presented to provide a progress update on the 2023/2024 audit. The report also included information in relation to national publications and other updates.

The Auditor had reported to previous meetings in relation to the national backlog in local authority financial reporting and audit and the proposed arrangements including backstop dates. EY, the predecessor auditor, had reported their intention to issue disclaimed opinions on the outstanding accounts for 2021/22 and 2022/23 by the backstop date of 13 December 2024. The lack of assurance on balances brought forward to 2023/24 and the limited amount of time available meant a disclaimed opinion on the 2023/24 accounts would be issued by the backstop date of 28 February 2025. The table at page 5 of the submitted report set out the Auditor's intended approach to building assurance and moving towards an unmodified opinion on the Council's accounts.

AGREED that the information provided was received and noted.

24/34

DRAFT STATEMENT OF ACCOUNTS AND THE ANNUAL GOVERNANCE STATEMENT 2023/24

A report of the Section 151 Officer was presented for Members to consider the draft Statement of Accounts and the Annual Governance Statement for the 2023/24 financial year.

Under the Accounts and Audit Regulations 2015, the 2023/24 accounts should have been published by 31 May 2024. However, there was a major issue in terms of a national audit backlog of prior year audits that were still on-going, as previously reported to the Audit Committee. At the statutory publication date, very few local authorities were able to make their draft accounts available. Central Government were in the process of re-setting the external audit process so that local authorities could publish their accounts in a timelier manner going forwards. However, this would take several audit cycles to resolve.

In addition, the S151 Officer, in response to a change to the relevant international accounting standard (IAS 37), requested a review of the methodology in relation to the Collection Fund bad debt provision to ensure that the accounts presented a true and fair view.

At the end of 2021/22 financial year, the total collection fund debt was £47.2m with a provision for bad debts totalling £33.99m, an assumption that 72% of debt outstanding at that point would not be collected. The calculation of the bad debt provision was based upon a profile of the aged debt outstanding but involved an element of officer judgement. Any debt over 5 years old was also provided for at 100%. The change in requirements around IAS37 (which required a determination of any impairment involved on the carrying value of the debt) meant that this was not an appropriate methodology for the provision. It should be based on historical evidence and actual debt recovery levels informed by actual collection performance data.

Since recovery of outstanding debt typically took 10 years and debt was still being actively recovered for debt older than 10 years, the provision of £34.005m (at 31 March 2022) was assessed to be overly prudent. A new methodology based up on long term collection rates (adjusted to account for previous debt write off) over the last 30 years was developed and applied to both 2021-22 and 2022-23 collection fund debt. The change in methodology was then applied to 2021/22 and 2022/23 accounts and resulted in a release of £9.617m from the bad debt provision. Middlesbrough's share of this was £7.160m which was then transferred to the Collection Fund Adjustment Account. At this point, the revised bad debt provision for the Collection Fund totalled £24.388m.

An existing surplus of £1.7m against other changing factors within the collection fund resulted in a total available of £8.9m at the end of 2022/23. Current forecasts for the 2023/24 Collection Fund outturn position were predicting that there would be a net in-year deficit of £0.6m on the Collection Fund. £8.3m was therefore available to the Council at the end of the 2023/24 financial year and for budgeting purposes in 2024/25.

Although the draft accounts for 2021/22 and 2022/23 had not been audited fully, the amendments on the bad debt provision plus some other minor changes in narrative due to the passage of time, meant that the revised statement of accounts needed to be recertified and reissued to comply with statutory regulation. This was done by the Director of Finance on 24 September 2024, and these have been updated on the Council website.

The importance of reissuing these accounts was that the balances on assets and liabilities roll forward and had an impact on the opening position for the 2023/24 financial year. Even though the management accounts and financial statements for the latest full financial year had been complete for some time, it was important to confirm the position on the bad debt provision with EY before the accounts were finalised and released to stakeholders. It was highlighted that whilst the previous year's accounts were unaudited, the figures, totals and narrative that accompanied these had been produced to a high-quality standard and a significant degree of professional compliance.

The draft accounts for 2023/24 had also been certified as a true and fair view of the Council's financial position by the Director of Finance and were opened for public inspection on 30 September 2024, for a period of 30 working days. Any enquiries from members of the public would be responded to and resolved in a timely manner and reported to Members as appropriate.

The Draft Statement of Accounts 2023/2024 was attached to the submitted report and included the following: a Narrative Report, Financial Statements, Notes to the Accounts, Group Accounts, Collection Fund Accounts and Collection Fund Income and Expenditure Account, Teesside Pension Fund Accounts and Notes and the Annual Governance Statement.

Members' attention was drawn to some significant differences between the Council's financial statements, which were part of the Statement of Accounts document and its management accounts which were reported for budget and operational purposes. This related to technical accounting adjustments and timing issues in how certain totals were reported. Two important areas to note were the presentation of reserves and the net worth of the Council's balance sheet.

The total value of usable reserves in the Balance Sheet as of 31st March 2024 was £75.702m. This was much higher than the £12.055m total that had been reported in the budget monitoring process for 2024/25 and lower than the amount recommended by the S151 Officer. The reason for the higher total figure included capital and revenue grants unapplied (those amounts paid over in past financial years but to be expended on committed items), as well as any other committed revenue reserves, such as school reserves and the Better Care Fund from the NHS. In particular, capital grants being rolled forward to future year's capital schemes was a significant value at £51.760m.

The net worth of the Council's balance sheet at the 31 March 2023 was a positive one totalling £279.3m. Assets available exceeded liabilities due by a significant margin. The net worth position overall though had decreased in year of £130.1m (31.8%). The decrease predominantly related to retirement benefits under IAS 19 and a change in the discount rate applied to the liabilities that formed part of the local government pension scheme, making this arrangement comparatively more expensive. Any pensions movements would not affect the Council's financial position for revenue budget purposes as it would influence future pensions payments over the next 20-40 years.

A Member queried the significant increase in the number of employees in receipt of an annual salary over £50K. It was explained that this was due to the latest pay award.

In relation to the accounting standards issued but not yet adopted, it was clarified that the statutory override was still being applied to the valuation of roads.

Members requested further information in relation to: the total cost of the latest pay award and associated pension cost, loss of income from planning fees to the Middlesbrough Development Corporation, costs associated with the Best Value Notice and the value of The Crown building on the Balance Sheet and where it was referenced.

AGREED as follows that:

1. Audit Committee noted the draft Statement of Accounts for 2023/24 had been approved by the Director of Finance for publication on 24 September 2024 and were currently on the Council website and out to public inspection until 8 November 2024.
2. The Head of Finance and Investment would provide Committee Members with further information in response to the queries raised at the meeting regarding:
 - The total cost of the latest pay award and associated pension costs.
 - Loss of income from planning fees to the Middlesbrough Development Corporation.
 - Costs of the measures put in place to address the issues that led to the Best Value Notice in 2023.
 - Value of The Crown building on the Balance Sheet and where it was referenced in the Statement of Accounts.

24/35 **WORK PROGRAMME (STANDARD ITEM)**

A copy of the current work programme for the Audit Committee had been circulated for information. This was a live document that was updated after each meeting.

AGREED as follows that:

1. The information provided was received and noted.
2. A report on Treasury Management would be added to the work programme.

24/36 **ANY OTHER URGENT ITEMS WHICH IN THE OPINION OF THE CHAIR, MAY BE CONSIDERED.**

None.