

Item

STATEMENT OF ACCOUNTS 2018/19

To:

Civic Affairs Committee 04/06/2020

Report by:

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Wards affected:

None directly affected

1. Introduction

- 1.1 The external audit of the Statement of Accounts for 2018/19 by EY is largely complete. Before giving their formal opinion on the accounts there is a requirement to present their audit findings and to obtain a Letter of Representation signed by both the Head of Finance and a member on behalf of 'those charged with governance'. Under the Council's constitution, this responsibility rests with the Civic Affairs Committee.
- 1.2 EY will be at the meeting to present and discuss their audit findings.

2. Recommendations

- 2.1 That the Committee receive the Audit Results Report presented by EY.
- 2.2 That the Statement of Accounts for the year ended 31 March 2019 be approved, subject to any remaining amendments per recommendation 2.3.

- 2.3 That authority be delegated to the Chair of the meeting to approve any amendments to the Statement of Accounts arising from remaining audit procedures, provided that these do not have a material impact on the Council's reserves.
- 2.4 That the Chair of the meeting be authorised to sign the Letter of Representation and Statement of Accounts for the financial year ended 31 March 2019 on behalf of the Council.

3. Background

- 3.1 Civic Affairs Committee reviewed the accounting policies and significant areas of judgement in relation to 2018/19 at its meeting on 30 January 2019.
- 3.2 Draft unaudited accounts were published on the Council's website on 26 July 2019, in line with the requirement in the Accounts and Audit Regulations to publish accounts by 31 July each year.
- 3.3 EY commenced the audit of the draft Statement of Accounts in September 2019, and the audit is now almost complete. A revised Statement of Accounts is attached at Appendix 1.
- 3.4 Within the Statement of Accounts, there is one disclosure note still to complete (note 42) in respect of additional disclosures required concerning the impact of Covid-19 on the Council's finances. This is a recent development, and officers are currently working with EY to agree suitable wording for the note. Further details are set out at paragraph 6.3 below.
- 3.5 This year's audit has taken significantly longer than usual due to a number of factors. The loss of several key officers within the Finance service had an adverse impact on the timeliness and quality of the draft Statement of Accounts and supporting working papers, which meant that EY were required to input more time and effort to complete their audit procedures. In addition, EY have acknowledged that some of this additional time was not used as efficiently as it might have been due to their own resourcing challenges. Finally, the impact of Covid-19 and resulting lockdown provisions has led to further delay towards the end of the process.

4. Council Financial Results for 2018/19

- 4.1 The Council's financial performance is summarised in the main financial statements.
- 4.2 The Movement in Reserves Statement shows an overall increase in the Council's usable reserves of £32.5 million, to £144.9 million.
- 4.3 There was a net increase of £14.6 million in respect of the capital receipts reserve which can only be used to support capital expenditure. This reserve will be utilised in future years in accordance with the capital programme.
- 4.4 General Fund unallocated reserves increased by £2.4 million to £15.8 million, whilst General Fund earmarked reserves increased by £0.2 million to £25.0 million.
- 4.5 HRA reserves increased by £2.6 million to £11.6 million. HRA earmarked reserves increased by £4.6 million to £15.7 million. This increase most notably reflects a 'set-aside' contribution to reserves in respect of possible future debt redemption or reinvestment.
- 4.6 A more detailed analysis of the movement of both General Fund and HRA earmarked reserves is shown in note 6 to the Statement of Accounts.
- 4.7 There is a table of page vii of the Narrative Report which reconciles the outturn position of portfolios reported to scrutiny committees to the movement on General Fund and HRA general and earmarked reserves. The Expenditure and Funding Analysis (note 1 to the Statement of Accounts) then reconciles this position to the statutory accounting results detailed in the Comprehensive Income and Expenditure Statement.
- 4.8 The Comprehensive Income and Expenditure Statement shows a net surplus on provision of services (measured according to proper accounting practice) of £4.5 million, compared to a net surplus of £17.8 million in 2017/18. Major reasons for the change include:
- Revaluation losses of £13.2 million were charged to HRA expenditure in respect of Council dwellings, compared with gains credited of £6.6 million in 2017/18. Note that while this impacts on the surplus on provision of services, the effect is reversed out of

the HRA through the Movement in Reserves Statement, so there is no impact on the Council's usable reserves.

- Financing and investment income is net of £7.7 million revaluation losses in respect of investment property, compared with gains of £2.7 million in 2017/18.
- Taxation and non-specific grant income includes capital grants of £21.7 million, compared with £7.4 million in 2017/18. Most of the difference relates to £13.6 million of devolution grant funding from central government for the delivery of new Council homes.
- There was a decrease in net expenditure on the Communities portfolio of £2.5 million, due primarily to a revaluation loss of £3.1 million which was recognised in 2017/18 on the Clay Farm Community Centre, compared with a small gain of £22,000 in 2018/19.

4.9 The Balance Sheet details the value of the Council's assets and liabilities. The Council's total net assets have decreased by £17.9 million, to £732.7 million. Key movements to note include:

- Net revaluation losses of £16.3 million on property, plant and equipment, consisting of a net loss of £18.1 million on Council dwellings, and a net gain of £1.8 million on other land and buildings.
- Net revaluation losses of £7.7 million on investment properties, consisting of a loss of £10.9 million on the central Cambridge shopping centre portfolio, and a £3.2 million gain on other investment properties.
- An increase in the net pension liability of £24.4 million, of which £19.3 million relates to actuarial losses.

5. Group Financial Statements

5.1 The Group Financial Statements consolidate the performance of the Council with its subsidiaries (Cambridge City Housing Company, Cambridge Live, and Cambridge Live Trading Ltd), and the Cambridge Investment Partnership (CIP) entities.

5.2 The accounts of the Cambridge City Housing Company (CCHC) show a profit for the year of £189k. After eliminating transactions with the Council and aligning accounting policies with the group, the total comprehensive income for CCHC included in the Group Financial Statements is £388k. However, under the Council's accounting policies £128k (relating to property revaluations) is

credited to unusable reserves, leaving a net credit to usable reserves of £260k (compared to a net charge of £18k in 2017/18).

- 5.3 The accounts of Cambridge Live and Cambridge Live Trading Ltd (together the Cambridge Live Group) have been consolidated into the Group Financial Statements for the first time this year. The Council took direct control of these entities on 1 October 2018, and recognised an impairment of £480k at this date to reflect the value of the net liabilities assumed. Between 1 October 2018 and 31 March 2019, the accounts of the Cambridge Live Group show a further loss of £947k, which includes impairment of property, plant and equipment of £237k, and actuarial losses on the pension fund of £565k. After eliminating transactions with the Council, the total comprehensive expenditure for the Cambridge Live Group included in the Group Financial Statements (excluding the initial impairment) is £1,047k.
- 5.4 The total cost to the Group as a whole in 2018/19 of assuming the Cambridge Live Group operations was £1,405k. However, it should be noted that this includes £839k in relation to the pension fund liability, which will be transferred to the Council's pension reserve in 2019/20. The impact on usable reserves was therefore £566k.
- 5.5 As a joint venture the Council is required to include its share of the financial results of CIP as a single line in the Group Comprehensive Income and Expenditure Statement and the Group Balance Sheet. During the year, 2 new CIP entities were set up, so that there are now 3 entities in total; an overall operating company, plus 2 specific development companies for Mill Road and Cromwell Road. Two of these entities (the operating company and Cromwell Road development company) had no transactions during the year, and nil net assets at year-end. The Mill Road development company accounts showed a loss of £500k, reflecting the fact that development was ongoing and sales of finished units had not yet commenced at year-end. The Council's share of the partnership's net liabilities at year-end was £457k. Taking this into account, and in accordance with proper accounting practice, the consolidation value in the Group Financial Statements was nil.

6. Audit Results

- 6.1 International Auditing Standards require the auditor to communicate a number of matters to those charged with governance before

issuing their audit opinion. EY's Audit Results Report is attached at Appendix 2. They will be at the meeting to discuss their report and audit findings.

- 6.2 Subject to completion of the outstanding audit work set out on page 5 of their report, EY propose to issue an unqualified audit report. A draft is provided at Section 3 of the Audit Results Report.
- 6.3 The current Covid-19 situation poses a risk to financial resilience for all local authorities, and as a result EY have sought additional evidence on the Council's future financial resilience and the impact this may have on the Statement of Accounts. This work is currently in progress and EY have highlighted that this may impact the audit report, which will need to go through an EY internal consultation process to ensure that it provides the appropriate assurance to the Council and its stakeholders. EY will provide a verbal update on this at the meeting.
- 6.4 The combined impact of the issues set out at paragraph 3.4 above has resulted in a higher than usual volume and value of adjustments to the draft Statement of Accounts. These are set out in detail within Section 4 of the Audit Results Report. It should be noted, however, that many of the adjustments made do not impact upon the Council's usable reserves as they are either presentational in nature, or relate to transactions where the impact is reversed through the Movement in Reserves Statement (such as property revaluations). It should be further noted that many of the adjustments are complex in nature, and that one adjustment often impacts on several parts of the financial statements. For example, a change in property valuations can impact the Movement in Reserves Statement, Comprehensive Income and Expenditure Statement, Balance Sheet, Housing Revenue Account Statement and several disclosure notes.
- 6.5 The table below summarises the impact of the audit adjustments made on the Council's reserve position and surplus on provision of services. The most significant adjustments are explained in more detail below the table:

(£000)	General Fund	HRA	Other Usable Reserves	Unusable Reserves	Total Council Reserves	(Surplus) on provision of services
Draft Statement of Accounts	15,415	11,539	102,339	631,239	760,532	(6,881)
Total impact of audit adjustments	362	81	15,152	(43,436)	(27,841)	2,332
Revised Statement of Accounts	15,777	11,620	117,491	587,803	732,691	(4,549)
Adjustments include:						
1) Council dwellings revaluation	0	0	0	(30,516)	(30,516)	9,511
2) Capital grant recognition	0	0	0	0	0	(13,505)
3) Adjustments in respect of property, plant and equipment and investment property	(68)	82	(7)	3,267	3,274	10,875
4) Capital financing adjustment – Cromwell Rd	0	0	9,834	(9,834)	0	0
5) S106 contributions – timing of income recognition	0	0	4,938	0	4,938	(4,938)
6) Pension Fund liability revaluation	0	0	0	(4,902)	(4,902)	0
Other adjustments	430	(1)	387	(1,451)	(635)	389
Total	362	81	15,152	(43,436)	(27,841)	2,332

6.6 Council dwellings revaluation – The Council is required to revalue its Council dwellings on an annual basis, and an external valuer’s report is commissioned for this purpose. Upon review of this valuation report, EY identified that the indexation applied by the valuer did not cover the full year, and as a result the valuation was overstated by £30.5m. Of this amount, £21.0m has been charged to the revaluation reserve, whilst the remaining £9.5m is charged initially to the HRA, but then reversed out through the Movement in Reserves Statement so that there is no overall impact on usable reserves. We have already engaged in discussions with the valuers with a view to working with them to minimise the risk of a similar issue occurring in future years. However, it should be said that the risk can never be completely eliminated due to the timing of the valuation and the audit; by the time the audit is undertaken there will invariably be additional market data available to auditors which was not available to the valuer at the time of valuation.

6.7 Capital grant recognition – This adjustment of £13.5m reflects capital grant income which was initially recognised directly in the capital grants unapplied reserve, rather than the correct treatment which is to recognise this first as income in the Comprehensive Income and

Expenditure Statement, and then transfer the amount to the capital receipts reserve through the Movement in Reserves Statement. This is an accounting adjustment – there is no impact on the Council's net asset or total reserve position.

- 6.8 Adjustments in respect of property, plant and equipment and investment property – This line reflects a number of adjustments which were required following issues in maintaining the Council's fixed asset register, and reconciling this to the general ledger at year-end. The vast majority of these adjustments have no impact on usable reserves under statutory accounting requirements.
- 6.9 Capital financing adjustment – Cromwell Rd – This is an accounting adjustment to the timing of the application of capital financing in respect of the Cromwell Road development. Whilst the capital receipts reserve has increased by £9.8m as a result, this balance remains committed to the project and will be applied in future years.
- 6.10 S106 contributions – timing of income recognition – When the Council receives S106 contributions with conditions attached, it has historically held these contributions on the Balance Sheet until the conditions were met. However, the Code requires instead that income be recognised when it is probable that conditions will be met, which represents a slightly earlier point of recognition. As a result, £4.9m of contributions have been released to the capital grants unapplied reserve. Again, the funds remain committed to their respective projects, and will be expended in future years in line with the capital programme.
- 6.11 Pension Fund liability revaluation – This adjustment reflects late changes to the actuarial estimate of the net pension fund liability as a result of the McCloud ruling, and differences between earlier estimates of pension fund asset values and their actual values at the year-end. As a result, the pension fund liability increased by £4.9m.
- 6.12 In addition to the audit adjustments, EY have also made a number of recommendations throughout their report in relation to Council systems, processes and internal controls. The recommendations made relate to the following areas:-
- Property valuations, including a recommendation that more information is provided to the Council's external valuers at the

start of the valuation process, and that management review the appropriateness of any indexation applied by valuers.

- Maintenance of the Council's fixed asset register.
- Issues with the technical spreadsheet model used to produce the draft Statement of Accounts, which contributed towards some of the audit issues found.
- Management review of the draft Statement of Accounts prior to audit.

These recommendations are set out in full at Appendix 4 to this report, together with details of the steps already taken by officers to address them.

7. Letter of Representation

7.1 International Auditing Standards require the auditor to have received a Letter of Representation drawn up by the Council that provides written confirmation on matters that might be relevant or significant to the Statement of Accounts. This letter is signed as near as possible to the date of the auditor issuing opinion. The auditing standard requires that the letter is 'discussed and agreed by those charged with governance and signed on their behalf...to ensure that all those charged with governance are aware of the representations on which the auditor intends to rely in expressing the auditor's opinion on those financial statements.'

7.2 A draft Letter of Representation has been provided at Appendix 4. EY will be present at the meeting to answer any questions.

8. Audit Fee

8.1 As set out at paragraph 3.4 above, this year's audit has taken longer than usual, and has required a significant level of additional input by both auditors and Council officers. This will impact on the level of audit fee charged, and EY have provided further details of their fee proposal on page 40 of their Audit Results Report. It should be noted that the fees proposed are still subject to agreement with the authority and Public Sector Audit Appointments (PSAA), who oversee the external audit regime for all local authorities.

9. 2019/20 Statement of Accounts and Audit

9.1 Given the issues encountered during the 2018/19 audit, there has been early positive engagement between officers and EY to ensure

that lessons have been learned for 2019/20. Some of the steps already taken include:

- Agreement of a revised and realistic timetable which sees a draft Statement of Accounts published by mid-July (approximately 2 weeks earlier than last year), and the audit complete in time to report to the Civic Affairs meeting in October 2020.
- Improvements to the resourcing situation within the Finance service, including the recruitment of a permanent Deputy Head of Finance and Senior Accountant (Technical & Financial Accounting).
- Improvements to the approach for project managing the closedown process, including making use of Microsoft Teams for the first time, regular progress meetings, and more robust review processes for the draft Statement of Accounts, supporting working papers, and key reconciliations.
- An agreement with the auditors to focus on higher risk areas (e.g. property valuations) early on in the audit wherever possible.

As a result, we are confident that the process for 2019/20 will be a lot smoother.

- 9.2 The current Covid-19 situation does provide additional challenges in terms of changes to our normal ways of working. However, this also presents an opportunity to make better use of technology throughout the audit process, for example holding virtual meetings with the auditors through Microsoft Teams, and providing audit evidence remotely through the EY client portal and screen sharing. This has worked well so far, and we intend to continue these positive steps going forwards.
- 9.3 It should be noted that, due to the Covid-19 situation, MHCLG have recently extended the deadline for the publication of 2019/20 until 30 November. However, draft accounts will still need to be published by 31 August to allow the public inspection period to commence. We are currently in discussions with EY about what this may mean for the audit timetable, although it is not anticipated that there will be any significant impact on the original plan to report audit findings to the Civic Affairs Committee in October 2020, as set out above.

10. Implications

a) Financial Implications

Included in the report above.

b) Staffing Implications

None

c) Equality and Poverty Implications

None

d) Environmental Implications

None. Paper copies of the Statement of Accounts document will only be produced on request. An electronic version will be available on the Council's website.

e) Procurement Implications

None

f) Community Safety Implications

None

11. Consultation and communication considerations

The Statement of Accounts will be published on the Council's website with a notice advertising that the audit of the accounts has been concluded.

12. Background papers

Background papers used in the preparation of this report:

- Statement of Accounts 2018/19

13. Appendices

- Appendix 1 – Statement of Accounts 2018/19
- Appendix 2 – EY Audit Results Report
- Appendix 3 – Audit Recommendations and Responses

- Appendix 4 – Draft Letter of Representation

14. Inspection of papers

To inspect the background papers or if you have a query on the report please contact Jody Etherington, Deputy Head of Finance, tel: 01223 - 458130, email: jody.etherington@cambridge.gov.uk.