

Manchester City Council Report for Information

Report to: Audit Committee – 13 June 2023

Subject: Update on Progress on the Audit of the Final Accounts for 2020/21 and 2021/22 and finalising the Draft Accounts for 2022/23

Report of: The Deputy Chief Executive and City Treasurer

Summary

This report is to update the Committee on the progress of the audit of the council's final accounts and outlines the national and local context behind the delays.

The report sets out the national and local context for the delays to the completion of the audits for the council's final accounts. The completion of the Audits are a statutory requirement and the issues outlined in this paper pose a real threat to the reputation of local government.

Recommendations

It is recommended that the Audit Committee note the national and local position in relation to the annual audit of accounts.

Wards Affected: All

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Background documents (available for public inspection):

None

1. Introduction and Background

- 1.1. This report is to update the Committee on the progress with the audit of the council's final accounts. As of June 2023, the last fully audited accounts are for 2019/20. The report will set out the reasons for the delays and the expected dates that the audited sets of accounts will come to this committee.

2. National Context

- 2.1. The delays are in the context of a number of challenges facing the local authority financial reporting and local audit system. Since the Audit Commission was disbanded in 2012 there have been several issues related to the system's fragmented leadership. The Redmond Review was commissioned in June 2019 to address these challenges. The outcome of the Review was reported in September 2020 with 23 recommendations. The review aimed to deliver a new framework for effective local audit, proposed a standard annual financial statement to enable all stakeholders to hold local authorities to account for their performance together with a robust and effective audit reporting regime. It was also recognised that the fee structure used in the initial Public Sector Audit Appointments (PSAA) procurement process did not enable auditors to fulfill the role in an entirely satisfactory way. With 40% of audits failing to meet the required deadline for report in 2018/19, this signaled a serious weakness in the ability of auditors to comply with their contractual obligations. A revised audit deadline of 30 September was recommended (this would have been reverting back to the previous deadline before it was accelerated to 31 July. Historically it was 31 December). It was acknowledged that the implementation of recommendations contained in the Review would, in part, require regulatory or legislative change but it is important to note that many of the issues identified in the report require urgent attention, given the current concerns about local audit demonstrated in the Review.
- 2.2. A key recommendation was the establishment of a new body, the Office of Local Audit and Regulation (OLAR), to manage, oversee and regulate local audit with the key responsibilities including the procurement of local audit contracts, monitoring performance, determining the code of local audit practice and regulating the sector. This has only been partially implemented. In October 2022 the Financial Reporting Council (FRC) appointed a Director of Local Audit who has is currently the shadow local audit system leader until 2024 when the FRC becomes the Audit, Reporting and Governance Authority.
- 2.3. The challenges in the local authority financial reporting audit system remain. The January 2023 National Audit Office (NAO) report found that only 9% of local government bodies received audit opinions in time to publish audited accounts for 2020-21 and 12% for 2021/22 by the extended statutory publication deadline of 30 September and that 35% of local government bodies who had not received opinions in time to publish 2020-21 audited accounts 12

months after the statutory deadline, as reported by Public Sector Audit Appointments Ltd.

- 2.4. The reasons for the delays can be attributed to a combination of:
- A lack of capacity within the local audit firms to complete the work to deadlines, potentially driven by the low fee rates, capacity pinch points such as the audit of the NHS accounts and challenges in recruiting.
 - Similar capacity issues within local authorities who were having to make large cuts which this has impacted on the quality of the working papers and accounts prepared.
 - An enhanced regulatory focus on material balance sheet items where there is a degree of estimation or uncertainty driven by previous failures in private sector audit such as Carillion. This has required local authorities to produce more detailed evidence and working papers to support areas such as property asset and pension fund valuations. There has been no differentiation between commercial assets or assets held for sale where the valuation is material and those which are hard to value and we will never sell and such as roads and investment assets.
 - Deadlines for 2022/23 have been set without taking into account the pressures in the system.
- 2.5. In early 2022 a query was raised by a local audit firm on the quality of the supporting evidence for highways valuations. These are included in the accounts at depreciated historic cost. The main 'technical issue' relates to subsequent expenditure on highways infrastructure assets and specifically on whether local authorities should be assessing if there is any residual value remaining in replaced components that needs to be de-recognised when the subsequent expenditure is added. While this is standard practice for many fixed assets, it may not generally be being implemented for (highways) infrastructure assets because there are a variety of significant practical difficulties in applying the standard approach to such assets. This is, particularly in relation to roads, where the engineering records used to maintain, replace and add to the (highways) infrastructure assets have not been created to map against identifiable components.
- 2.6. While a resolution to the issue was being sought no local authority audits could be signed off. This significantly contributed to the delays and was only resolved with the issuance of a statutory override by DLUHC which came into effect on 26 December 2022 and the subsequent updates to the CIPFA Accounting Code of Practice issues in January 2023.
- 2.7. A further national issue was identified in April 2023 linked to the delay in signing off historic accounts. External auditors highlighted an issue with the value of IAS19 liabilities in the 2021/22 accounts following the triennial valuation. The valuation contained updated data, particularly on demographic factors which could mean that the information used in the 2021/22 pension valuations used

for the accounts is materially incorrect. This issue further delayed the sign off of any outstanding 2021/22 accounts. On 17 May 2023 CIPFA issued revised guidance (Bulletin 14) on the application of the Code. To enable authorities to determine the impact of the triennial valuation on their IAS 19 valuation as at 31st March 2022 an updated IAS 19 report from the actuary may be required. Should the updated report show a material difference it is expected that the 2021/22 financial statements will be updated. Concerns about the delays in the local audit process have now been escalated to ministerial level and there is a working group in place to resolve the issues.

- 2.8. It is disappointing that in the context of the above delays and capacity issues, DLUHC decided to return to the deadlines of 31 May 2023 for the production of draft 2022/23 accounts and 30 September 2023 for the completion of the audit process.

3. Manchester City Council Position

- 3.1. The Manchester position echoes the national one. It should also be noted that Manchester's Annual Accounts are particularly complex due to both the range of joint ventures, the value and complexity of assets held and the requirement to consolidate Manchester Airport Group and Manchester Central into the group accounts.

2020/21

- 3.2. The 2020/21 accounts had been delayed prior to the national highways issue due to reduced capacity in the corporate finance team, issues in obtaining the quality of valuations data required and capacity issues with the local audit team working with tight deadlines across a number of local authorities. As previously stated, it has taken some time to get the valuations data now required. There were also issues with the journal reports produced from the finance system and in the completion of the cashflow statement. As a result, Internal Audit carried out a lessons learnt review to make sure these issues were not replicated in future audit processes.
- 3.3. Following the resolution of the national infrastructure issue early 2023, the target deadline for signing off the 2020/21 accounts was March 2023 Audit Committee. A local issue arose relating to the valuations in the Greater Manchester Pension Fund accounts. These issues have now been resolved and the audit is materially complete with the Audited Accounts scheduled for July 2023 Audit Committee.

2021/22

- 3.4. Whilst the audit of the 2021/22 accounts has seen some challenges, notably with obtaining the right quality of valuations information, the audit is now

substantially completed. In order to finalise the audit of the pensions valuation a revised actuarial report is required. This has been requested and should enable the completion of the audit in time for September 2023 Audit Committee.

2022/23

- 3.5. The Accounts have not been completed by the statutory deadline of 31 May. With the backlog of accounts issues from previous years and the time required to finalise them, limited capacity within the corporate finance team, the challenges with obtaining all of the valuations information now required and the later timescales that Manchester Airport Group (MAG) work to for their accounts it has not been possible to complete the consolidated draft accounts for the 31 May deadline. The advert confirming the delay has been published.
- 3.6. Manchester are not unique in our position and CIPFA have published a supporting statement for Chief Finance officers to share with their Audit Committees, this is copied below. Both CIPFA and our Auditors have stressed the importance of accuracy to facilitate a more efficient audit process.

“Statutory provisions for reporting require the effective publication of unaudited financial statements by 31 May 2023. As a professional accounting institute, CIPFA will always recognise the statutory nature of the deadline.

“However, some senior leaders in local government finance have told us the 31 May deadline will not be achievable without considerable risk to their organisations and their professional standing.

“Many are concerned about the wellbeing of teams who have worked hard to deal with a difficult budget setting process and are now facing the challenge of producing accounts against the backdrop of significant and continuing audit delays. These delays present chief financial officers with gaps in the assurance processes which make exercising professional judgement about a true and fair position more difficult.

“CIPFA recognises the significant challenges CFOs and their finance teams are facing and we would encourage senior leaders to take a considered and transparent approach. Sensible steps would be to ensure conversations have taken place with key stakeholders such as senior members, the chair of audit committee (or equivalent), the chief executive and monitoring officer and any other interested parties. Clarity about the reasons for any decisions about publication of the unaudited financial statements will allow members and others to monitor the situation, maintaining appropriate transparency and accountability over the process.

“It is important that all those involved understand the reality that a balance is struck between the timeliness and the quality of unaudited financial statements produced in the coming weeks.”

- 3.7. The draft accounts are scheduled for July 2023 Audit Committee. However, with the historic accounts still to clear, Mazars have confirmed that they cannot start their audit process for the 2022/23 accounts until September 2023. This would mean it is unlikely the Audited Accounts would be ready before January 2024.

4. Conclusion

- 4.1. This report sets out the national and local context for the delays to the completion of the audits for the council's final accounts. The completion of the Audits are a statutory requirement and the issues outlined in this paper pose a real threat to the reputation of local government. As a S151 Officer, I take the audit of our accounts extremely seriously and I am deeply concerned about the issues raised in this report. It is hoped that the increased focus on this issue will lead to a resolution that will mean that we are not in this position again.