Leicestershire County Council

CONSTITUTION COMMITTEE – 27th JULY 2018

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

STATEMENT OF ACCOUNTS & PENSION FUND ACCOUNTS 2017/18

PURPOSE

1. The purpose of this report is to:

   a) present the 2017/18 Statement of Accounts, attached as Appendix A to this report, for approval;
   b) inform the Committee of the main areas of the accounts;
   c) report the key findings from the external audit of the accounts;
   d) provide an update on the external auditor appointment for 2018/19.

BACKGROUND

2. The Accounts and Audit Regulations 2015 require authorities to approve and publish their accounts, including the auditor's opinion by the end of July (previously September) following the end of the financial year.

3. A copy of the external auditor's, KPMG LLP, report on the accounts is attached as Appendix B. The letter of representation is attached as Appendix C.

4. The Corporate Governance Committee will consider the auditor's report at its meeting on 25 July 2018. The auditor is required to communicate the results of the audit to those charged with governance prior to certifying the financial statements. The minutes from that meeting will be reported to the Constitution Committee. The auditor anticipates issuing an unqualified audit opinion.

5. The Statement of Accounts is prepared under the International Financial Reporting Standards (IFRS) based Code of Practice on Local Authority Accounts.

STATEMENT OF ACCOUNTS

6. The main areas of the financial statements are set out below:

   Narrative Statement

7. The purpose of the Narrative Statement is to offer interested parties an effective guide to the most significant matters reported in the accounts. It includes a summary of the economy, efficiency and effectiveness, and the financial and non-financial performance of the Authority, and an explanation of the contents of the accounts.

Movement in Reserves Statement (MIRS)

8. This statement shows the movement in year on the different reserves held by the County Council, analysed into ‘usable reserves’ i.e. those that can be applied to fund expenditure and ‘unusable reserves’ which cannot be used to fund services. Unusable reserves include reserves that hold unrealised gains and losses as well as adjustments for the differences between amounts charged in accordance with accounting standards and amounts charged for statutory purposes. An example is the short term accumulating compensated absences adjustment account (STACAAA). This account holds the estimated value of untaken annual leave and time-off-in-lieu as at the balance sheet date. The charge is recognised by the accounting standards but statutory mitigation allows it to be reversed out via the STACAAA to avoid it being a charge to the General Fund.

9. Overall, usable reserves which comprise the General Fund, Earmarked Funds and Capital Funds, have increased as at 31 March 2018 from £156m to £163m.

10. The General Fund totalled £24m as at 31 March 2018 (£26m 31 March 2017) and contains delegated funding for schools, carry forwards and the uncommitted balance of the County Council. Details of the Fund are shown in note 11 to the accounts. The decrease at year end is mainly due to a reduction in the level of school balances resulting from academy conversions.

11. The uncommitted balance is held for unforeseen risks to the Council. It allows the Council to manage unforeseen financial events without the need to make immediate offsetting savings, with the potential real impact on County Council services. The Council’s policy is to hold a balance in the range of 4% to 5% of net budgeted expenditure (excluding schools). The balance at 31 March 2018 was unchanged at £14.8m and represents 4.1% of the net budgeted expenditure for 2018/19.

12. Earmarked funds, excluding dedicated schools grant, totalled £125m as at 31 March 2018 (£109m 31 March 2017). The main reason for the increase was due to resources being set aside to fund the increased demand for capital investment. This is primarily projects that reduce liabilities and ongoing costs, generates income or investment in County Council services. The investments approved at year end include highways maintenance and the future developments fund. The timing of these projects meant that funding was carried forward in earmarked funds. Details of the funds can be found in note 12 to the accounts.

13. The significant earmarked funds held are:

- Capital Financing £61m. This fund is used to hold MTFS revenue contributions to fund capital expenditure in later years of the approved 4 year capital programme. It also holds funding set aside for the future developments programme to fund projects that achieve ongoing revenue savings and support necessary service investment. Holding this fund is an essential part of the Council’s approach to avoiding incurring additional debt where possible. The amount shown in the accounts to the accounts is after £20m investment in Pooled Property Funds. The investment is temporarily shown against the capital financing fund but in effect is funded from the overall balance of earmarked funds and can be realised in the future when required.

- Insurance Funds £12m. Held to meet future claims, or parts of claims, that are not covered by insurance policies. This could be due to policy limits and deductibles or claims relating to periods when the insurer has failed, such as Municipal Mutual Insurance or The Independent Insurance Company.

- Transformation £12m. Funding set aside to invest in transformation projects to achieve efficiency savings and service improvements across the County Council and to fund potential restructuring costs of reconfiguring those services. The amount shown in note 12 to the accounts is after the £3m balance from the temporary investment of £8.4m in the Local Authority Mortgage scheme - £5.4m was repaid during 2017/18). The remaining £3m is due to be repaid in 2018/19. The investment was advanced to Lloyds Bank temporarily funded from the overall balance of earmarked funds.

14. The required level of earmarked funds is kept under review during the year. Formal assessments are undertaken and reported during the autumn, in February as part of the Medium Term Financial Strategy (MTFS) and also at year end.

<u>Comprehensive Income and Expenditure Statement (CIES)</u>

15. The CIES shows the accounting cost of providing services in accordance with accounting standards rather than the amount funded from taxation and income. The County Council raises taxation to cover expenditure in accordance with statutory regulations which can be different from the accounting cost.

16. The headings used in the CIES align with the main reporting areas of the County Council. However the CIES cannot be directly compared to the outturn position reported to the Cabinet because the financial accounts comply with various reporting standards whereas the management accounts are compiled on a slightly different basis. The key differences relate to the way depreciation, impairment and earmarked funds are reported.

17. The CIES shows a deficit on the Provision of Services for 2017/18 of £6.1m compared with a surplus of £4.3m in 2016/17). The main reason for the change is the reduction in Central Government Grants, mainly the Revenue Support Grant which reduced by £17m in 2017/18 – see note 38 to the accounts.

18. The Narrative Statement, on page 6 to the accounts, explains the net outturn position in the context of the County Council's budget. In summary, this shows a gross underspend of £0.3m (after movements to earmarked funds for additional investment approved at year end) which has been set aside to fund carry forwards to 2018/19.

<u>Balance Sheet</u>

19. The Balance Sheet shows the value of the assets and liabilities recognised by the County Council as at the balance sheet date. As at 31 March 2018 net assets of the County Council were £312m (31 March 2017, £213m). The principal reason for the change is an increase in the value of Property, Plant and Equipment of £63m, due to capital improvements during the year (from the capital programme) and also a reduction in the net pension liability of £25m.

20. As at the balance sheet date, the net deficit on the pension fund had improved to £589m compared with £614m at the same time last year. This is mainly due to an increase in the value of the pension fund assets of £41m (County Council's notional share). This improvement is offset by an increase in estimated liabilities of £16m over the same period. Details are shown in note 16 to the accounts.

21. The pension fund balance represents all pension entitlements that have been earned to date but which are not yet in payment and has a substantial impact on the net position of the balance sheet. However, statutory arrangements will result in the deficit being made good through increased contributions by the employer, over the remaining working life of employees, as assessed by the pension fund scheme's Actuary. The County Council has agreed a strategy with the Actuary to achieve a funding level of 100% over the next 20 years.

22. The Balance Sheet also shows total provisions of £7.3m (£7.8m 31 March 2017). Provisions are held to fund liabilities of uncertain timing or amount and are shown in greater detail in note 27 to the accounts. The main provision held is for Insurance, £4m, and represents the estimated value of outstanding unsettled claims at 31 March 2018.

23. Cash and Cash Equivalents have increased from £23m to £34m as at 31 March 2018. Cash equivalents are highly liquid investments that mature within 3 months or less from the date of acquisition, shown in note 24 to the accounts. This is mostly due to an increase in investments held short term as at the balance sheet date of £9m due to an anticipated Bank of England Base Rate rise.

24. The balance sheet also shows the amount of short and long term investments, which total £227m as at the year end. This includes £20m investment in Pooled Property Funds shown under long term investments, and £7m investment in Private Debt. Both investments are made in order to achieve a higher rate of return than deposits with banking institutions.

25. During 2017/18 the County Council set aside £10.8m as part of the minimum revenue provision (MRP) for the repayment of debt. This has the effect of reducing the capital financing requirement (CFR) and the ongoing MRP charge to the revenue budget, the financing costs of capital totals c.£23m each year. The CFR is shown in note 41 to the accounts and stands at £257m at the year end. The CFR is a measure of capital expenditure incurred historically that has yet to be financed. Actual debt as at the balance sheet was £265m. The difference between the CFR and actual debt is a temporary overborrowed position of £8m and is pending opportunities for the early repayment of debt where the savings outweigh the redemption penalties. This position is kept under regular review by as part of the Councils Treasury Management Strategy.

Annual Governance Statement

26. The Statement of Accounts is accompanied by the Annual Governance Statement (AGS) signed by the Chief Executive and Leader of the County Council. The statement sets out the purpose of the system of internal control, how it operates in the County Council and how its effectiveness has been reviewed. The AGS has been approved by the Corporate Governance Committee.

Pension Fund Accounts

27. The Statement of Accounts includes the Pension Fund accounts for the Local Government Pension Scheme administered by the County Council.

28. The last available triennial actuarial valuation of the pension fund showed that as at 31 March 2016 the fund's assets covered approximately 76% of the liabilities accrued up to that date. This funding level was an increase on the 72% position reported in the 2013 valuation. The deficit puts significant upward pressure onto the contribution rates of employing bodies but these were contained somewhat for tax raising bodies by using a smoothing mechanism and by the use of a 20 year deficit-spreading period.

29. To ensure that the fund remains financially sound to meet benefit payments, the Actuary will recommend the rate of employer contributions on an individual employer basis for each employing body in the fund for a three year period. In 2017/18 the average employer rate was 22.7% of pay (21.8% 2016/17).

30. The overall net assets of the fund increased during the year from £3.9bn at the start to £4.1bn as at 31 March 2018. This was due to an increase in the value of the investments, shown in note 9 to the Pension Fund Accounts.

Key Findings of the External Auditor

31. The external auditor has reviewed the financial statements and has concluded that there are no material accounting issues. The external auditor anticipates issuing an unqualified opinion for:

    a) the Statement of Accounts and Pension Fund Accounts – give a true and fair view of the financial position of the authority as at 31 March 2018, and have been prepared in accordance with proper accounting practice, the CIPFA Code of practice on Local Authority Accounting in the United Kingdom 2017/18.

    b) Value for Money arrangements – putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of those arrangements.

32. Arising from the audit the auditor has raised five recommendations:

    - No periodic user access responsibility review (to the financial system, Oracle). The last significant review was 3 years ago. There had been some initial delays in developing suitable reports, but these have now been resolved and a full review will be undertaken during 2018.

    - Timely revoking of system (Oracle) access for leavers. From a full review of all assignment (employment) end dates, there were 20 cases where access to the system was still available after the end dates. Subsequent testing showed no inappropriate actions had been undertaken. A review of the process will be undertaken to ensure that end dates are updated on a timely basis.

- Payroll BACS authorisation. For one payroll in December 2017 the file was prepared and approved by the same person. A shortage of staff at the time resulted in the team manager certifying the preparation and approval of the file to meet the payroll deadlines. This will be reviewed to ensure adequate cover is available in future.

- Pension Fund – Investment Asset Reconciliation. The quarterly Net Asset Valuations (NAV) reports from fund managers are reconciled for each quarter but are not input into the general ledger until year end. The council has agreed that best practice is to input them quarterly and this will be implemented during 2018.

- Pension Fund – Bank Reconciliation. The pension fund bank account is reconciled on a daily basis and reviewed by a senior officer at the end of each month, but there is no formal monthly reconciliation statement signed by the preparer and the approver. This will be implemented in 2018.

33. There was one correction to the accounts identified during the audit. This related to the valuation of assets, £1.4m, and was due to a difference between the valuation system and the fixed asset register. The issue has been identified and changes will be made for next year. The correction, to reduce the value of land and buildings, has been made in the 2017/18 accounts.

EXTERNAL AUDITOR APPOINTMENTS FOR 2018/19 – update

34. The audit of the 2017/18 accounts is the final year of KPMG LLP as the external auditor of the County Council.

35. The Local Audit and Accountability Act 2014 introduced changes allowing Local Authorities to appoint their own external auditor from 2018/19. Following reports to the Corporate Governance Committee and the County Council in 2016, the County Council opted to join Public Sector Audit Appointments Limited (PSAA), the sector led body set up by the Local Government Association for the appointment of external auditors. Of 493 eligible local bodies, 484 opted into the PSAA scheme.

36. The PSAA have completed their procurement exercise and have awarded contracts, based on lots, to six auditing firms. Following a consultation period, Grant Thornton (LLP) was appointed as the new external auditor for the County Council and the Pension Fund. The contract will cover a five year period commencing with the audit of accounts for 2018/19. PSAA has an option to extend the contracts for a further two year period, to a total of seven years, if it chooses to do so.

37. As a result of the procurement exercise external audit fees will reduce from £105,000 per annum for the County Council and Pension Fund, to £80,000 per annum from 2018/19, a reduction of 24%.

RECOMMENDATION

38. The Committee is recommended to approve the Statement of Accounts for 2017/18.

BACKGROUND PAPERS

Provisional revenue and capital outturn, Cabinet - 22 May 2018
http://politics.leics.gov.uk/documents/s137593/Cabinet%2022%20May%20-%20Prov%20Outturn%20v5.pdf

Provisional revenue and capital outturn, Scrutiny Commission - 6 June 2018.
http://politics.leics.gov.uk/documents/s137872/Provisional%20Outturn%20Report.pdf

CIRCULATION UNDER THE LOCAL ISSUES ALERT PROCEDURE

None.

EQUAL OPPORTUNITIES IMPLICATIONS

None.

APPENDICES

Appendix A – Statement of Accounts 2017/18
Appendix B – External Auditors Report
Appendix C – Letter of Representation

OFFICERS TO CONTACT

Mr C Tambini, Director of Corporate Resources,
Corporate Resources Department,
☎0116 305 6199 E-mail Chris.Tambini@leics.gov.uk

Mr D Keegan, Assistant Director (Strategic Finance and Property),
Corporate Resources Department,
☎0116 305 7668 E-mail Declan.Keegan@leics.gov.uk

This page is intentionally left blank