Leicestershire County Council

CONSTITUTION COMMITTEE – 7 DECEMBER 2021

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

STATEMENT OF ACCOUNTS, ANNUAL GOVERNANCE STATEMENT & PENSION FUND ACCOUNTS 2020/21

Purpose

1. The purpose of this report is to:

   a) present the 2020/21 financial statements, Appendix A, for approval,
   b) inform the Committee of the main areas of the financial statements, and
   c) report the key findings from the external audit of the accounts.

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 following the end of the financial year. As a result of Covid-19 the Accounts and Audit (Amendment) Regulations 2021 amended the deadlines for the external audit of the financial statements to the end of September 2021.

3. During the audit planning phase the County Council agreed with the external auditor to a revised deadline for the external audit, to the end of November 2021. This was to allow more time due to the implementation of the new financial system part way through the financial year. It also allowed more time for increased assurance work that auditors are required to carry out nationally with respect to pensions and asset valuations.

4. A copy of the external auditor's, Grant Thornton UK LLP, report on the financial statements is attached as Appendix B. Letters of representation for the Statement of Accounts and Pension Fund are attached, Appendix C and Appendix D.

5. The Corporate Governance Committee will consider the auditor's report at its meeting on 3 December 2021. 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.

6. The 2020/21 financial statements have been produced in exceptional circumstances:

   - During 2020/21 the County Council implemented a new finance and human resource system, Oracle Fusion Cloud services. The finance modules went live

part way through the financial year in November 2020 with the HR modules went live in April 2021.
- The Covid-19 pandemic resulted in both exceptional changes to working practices and a 25% one off increase in the amount of funding received by the County Council compared to the net revenue budget.
- The level of audit testing has continued to increase compared to previous years.

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

Statement of Accounts

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

Narrative Statement

9. 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)

10. 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 accounting standards, but statutory mitigation allows it to be reversed out via the STACAAA to avoid it being a charge to the General Fund.

11. Overall, usable reserves which comprise the general fund, earmarked funds and capital funds, have increased as at 31 March 2021 to £203m from £159m as explained below:

Fund	31 March 2020	31 March 2021
	£m	£m
General Fund	27.0	26.7
Earmarked Funds	128.9	175.0
Capital Funds	3.5	1.6
Total	**159.4**	**203.3**

General Fund

12. The General Fund includes delegated funding for schools and the uncommitted balance of the County Council. Until 1 April 2020 it also included the deficit on the Dedicated Schools Grant (DSG), but following legislation implemented during 2020/21 the balance is now required to be reported separately in a new unusable

reserve, the DSG Adjustment Account, shown in the bottom half of the balance sheet.

13. A summary of the General Fund balance is shown in Note 11 to the accounts and below:

General Fund	31 March 2020	31 March 2021
	£m	£m
Delegated Funding for Schools	8.0	9.7
DSG Reserve – Growth Funding	3.0	0.0
DSG Reserve – High Needs Deficit	(7.1)	0.0
Uncommitted Balance	23.1	17.0
Total	**27.0**	**26.7**

14. The uncommitted fund as at 31 March 2020 included £7.1m to manage variations in the DSG High Needs balance. Due to the legislation changes above, this element has now been transferred to the budget equalisation earmarked reserve.

<u>Earmarked Funds</u>

15. Earmarked funds totalled £175m as at 31 March 2021 (£129m 31 March 2020). The main reasons for the increase was both the capital financing reserve £10m due to slippage on the capital programme and the new budget equalisation reserve £24m.

16. Details of the earmarked funds can be found in Note 12 to the accounts. The significant earmarked funds held are:

- Capital Financing £64m. Holds MTFS revenue contributions to fund capital expenditure in the approved four 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 is net of £25m investment in Pooled Property Funds. The investment is shown against the capital financing reserve, but in effect is funded from the overall balance of earmarked funds and can be realised in the future when required.

- Budget Equalisation £24m. This reserve is held to manage variations in funding across financial years. This includes the increasing pressures on the High Needs element of the Dedicated Support Grant which was in deficit by £17m at the end of 2020/21 and is forecast to increase to £86m by the end of 2025/26.

- Insurance £14m. Funds 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.

- Other earmarked funds £73m. Funds for a range of issues including ongoing Covid-19 pressures, council tax shortfalls, business rates retention and a range of service developments / initiaves including transformation projects as detailed in the Note to the accounts.

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

Capital Funds

18. Capital funds reduced to £1.6m as at year end. The balance held represents earmarked capital receipts and capital grants and contributions not yet used. The amounts vary as and when capital projects complete.

Comprehensive Income and Expenditure Statement (CIES)

19. 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.

20. 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.

21. The CIES shows a surplus on the Provision of Services for 2020/21 of £46m compared with a surplus of £7m in 2019/20. The main change is due to the increase in earmarked reserves.

Balance Sheet

22. 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 2021 net assets of the County Council were £316m (31 March 2020, £448m). The principal reason for the decrease is due to an increase in the net pension liability of £229m.

23. As at 31 March 2021, the net deficit on the pension fund had increased to £836m from £607m at the same time last year. This was mainly due to a decrease in the discount rate used to calculate the present value of future pension fund liabilities (the lower the discount rate used the higher the present value of future liabilities). During the year corporate bond yields decreased, resulting in a lower discount rate in the IAS19 pension fund valuation report used in the accounts.

24. 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 triennial fund valuation, most recently as at 1 April 2019, informs the levels of future contributions required. The County Council has agreed a strategy with the Actuary to achieve a funding level of 100% over the next 17 years.

25. The Balance Sheet also shows the valuation of Property, Plant and Equipment owned by the County Council. During 2020/21 the value increased by £71m to £1.1bn. This reflects capital additions in year through the capital programme, revaluation gains and losses, less depreciation.

26. Provisions total £6.7m as at 31 March 2021 (previously £7.4m). 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, £3.4m, and represents the estimated value of outstanding unsettled claims at 31 March 2021. Provisions also include £2.8m for the County Council's 'notional' share of the seven Leicestershire District Councils Business Rates appeals and bad debt provisions, an increase of £0.5m compared with the previous year. The element in the County Council's accounts is notional as it is required to be reversed out via the Collection Fund Adjustment Account (shown at the bottom of the Balance Sheet) in order that it is not a charge to the General Fund.

27. Investments include Cash and Cash Equivalents (highly liquid investments that mature within 3 months or less from the date of acquisition) and short and long term investments. These total £360m as at 31 March 2021, compared with £288m at the same time last year. The increase is mainly related to the increase in the balance of earmarked reserves as at year end.

28. During 2020/21 the County Council revised its minimum revenue provision (MRP) policy for the repayment of debt. The revised policy reduced the annual charge to £6.2m from £10m for the previous year, although the same overall amount is still repayable, but is now equalised over a 40 year period representative of the average remaining useful economic life of capital assets funded by previous borrowing. The MRP has the effect of reducing the capital financing requirement (CFR), shown in Note 39 to the accounts and totals £232m 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 £263m. The difference between the CFR and actual debt is a temporary overborrowed position of £31m which will be reversed over the MTFS due to planned increases in the CFR from (internal) borrowing to fund the four year capital programme, £166m. This position is refreshed annually as part of the MTFS.

Annual Governance Statememt

29. The financial statements are 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 is approved by the Corporate Governance Committee.

Pension Fund Accounts

30. The financial statements also include the Pension Fund Accounts for the Local Government Pension Scheme administered by the County Council.

31. The last available triennial actuarial valuation of the pension fund showed that as at 31 March 2019 the fund's assets covered approximately 89% of the liabilities accrued up to that date. This funding level was an increase on the 76% position reported in the 2016 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 17 year deficit-spreading period.

32. 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 2020/21 the average employer rate was 25.4% of pay (24.5% 2019/20). There were 283 employers within the fund and just over 104,000 members in the pension scheme as at the balance sheet date.

33. The overall net assets of the fund increased during the year from £4.2bn at the start to £5.1bn at year end. For all LGPS Funds, investment returns have been significantly higher than last year, mainly due to a faster than expected recovery from Covid-19. Details of the investments held are shown in Note 12 to the Pension Fund Accounts.

Key Findings of the External Auditor

34. 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 the Statement of Accounts and Pension Fund Accounts.

35. There was one adjustment required to the main statements for both the County Council and Pension Fund Accounts. This related to the use of estimates for hard to value pension fund assets, mainly private equity where the actual valuations are not known until after the draft accounts have been produced. The accounts have been updated for the actual valuations.

36. During the audit a small number of amendments were also agreed to be made to the Notes to the Accounts. The main amendments were:

- County Council (Note 2b) – the note had incorrectly grossed up movements to and from reserves.
- Pension Fund (Note 20) – the fair value classification of some investment assets has been amended from level 1 to level 2. The levels relate to the quality and reliability of the information used to determine fair value.

37. The auditor has made four recommendations for improvements as shown in section A of their report.

Year-end bank reconciliations

38. Following the implementation of the new Oracle Fusion system part way through the financial year a number of new processes were implemented that have affected the timely clearance of differences. These have now been reduced and isolated to a number of smaller transactions and are being tackled as a priority to clear.

Year-end sales ledger reconciliation

39. In the same way as mentioned above, there are also new system reports available to reconcile balances. There is a small difference on the sales ledger ageing report that

officers are working through. Additional work has been undertaken that provides assurance over the balances in the accounts, and that the issue relates to the aged debt report and or the timing of entries. Work is continuing to ensure the differences are resolved as a priority.

Pension Fund Annual Report

40. There was a small number of additional disclosures required by the new CIPFA guide on preparing the Annual Report that were not included in the 2020/21 Pension Fund Annual Report. These will be included in the 2021/22 report. The gaps in the 2020/21 report were discussed with the Local Pension Committee when it met to approve the Annual Report on the 26th November 2021. The audit opinion is not subject to completion of these disclosures.

IT Audit Report

41. As part of the external audit a specialist team within Grant Thornton undertook a detailed IT audit of the design and implementation of IT General Controls within the IT environment as they affect the financial statements and financial audit for the year ended 31st March 2021.

42. There was one recommendation reported that had a significant control deficiency. This related to the segregation of access in Oracle Fusion to make changes to both the development and production (live) system environments. There is a small number of the systems implementation partner staff and members of the internal systems admin team that have access to both environments. Access for the implementation partner has been necessary in order that they can implement the new Fusion system. This is required while the new system is being rolled out in phases and is scheduled to be completed in January 2022 when their access will be removed. Post go-live changes deployed to production are carried out by the systems admin team. This is a small team who have access to both development and production environments to carry out their duties. There are agreed procedures to manage these processes including monitoring changes. Further work will be undertaken to understand where controls can be further improved.

Value for Money Arrangements

43. On the 1 April 2020 the National Audit Office (NAO) introduced a new Code of Audit Practice for 2020/21. This included a revised and more detailed approach to the audit of the Value for Money (VFM).

44. The external audit of this area is underway and has not yet been completed. As a result the auditor will not be able to issue the Annual Audit Report at this time. No significant weaknesses have been identified in arrangements to date, the auditor expects to issue the Annual Report by the end of January 2022. This does not affect the auditor signing the accounts.

External Audit Fee

45. The proposed external audit fees for 2020/21 per the audit plan are £107,602 for the County Council and £34,530 for the Pension Fund. The final fees for 2020/21 have not yet been advised.

Recommendation

46. The Committee is recommended to approve the financial statements for 2020/21.

Background papers

Provisional revenue and capital outturn, Cabinet - 22 June 2021
http://politics.leics.gov.uk/documents/s161900/20-21%20MTFS%20prov%20outturn.pdf

Circulation under the Local Issues Alert Procedure

None.

Equality and Human Rights Implications

None.

Appendices

Appendix A – Financial Statements 2020/21
Appendix B – External Auditors Report
Appendix C – Letter of Representation – County Council
Appendix D – Letter of Representation – Pension Fund

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