



CONSTITUTION COMMITTEE – 21 MARCH 2023

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

STATEMENT OF ACCOUNTS, ANNUAL GOVERNANCE STATEMENT & PENSION FUND ACCOUNTS 2021/22

PURPOSE

1. The purpose of this report is to:
 - a) present the 2021/22 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 2022.
3. During the audit planning phase the County Council and the external auditor agreed to a revised deadline for the final audit opinion to early 2023. This was to allow for time for new legislation to be passed, and subsequent Cipfa guidance to be received, in respect of the revised accounting treatment for Infrastructure (highways) assets.
4. A copy of the updated financial statements is attached as Appendix A.
5. Copies of the external auditor's, Grant Thornton UK LLP, audit findings reports for the County Council and its Pension Fund are attached as Appendix B and Appendix C respectively.
6. Copies of the letters of representation for the County Council and its Pension Fund are attached as Appendix D and Appendix E.
7. The Corporate Governance Committee will consider the auditor's reports at its meeting on 16 March 2023. 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 on the County Council and the Pension Fund accounts.

8. The level of audit testing has continued to increase significantly compared to previous years. This stems from increased requirements on auditors from their regulators, the National Audit Office, and is reflected in the increasing levels of audit fees.
9. The Statement of Accounts is prepared under the International Financial Reporting Standards (IFRS) based Code of Practice on Local Authority Accounts.

STATEMENT OF ACCOUNTS

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

Narrative Statement

11. 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)

12. 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.
13. Overall, usable reserves, which comprise the General Fund and earmarked revenue and capital reserves, total £255m as at 31 March 2022:

Usable Reserves	31/3/21	31/3/22
	£m	£m
General Fund – Delegated Funding for Schools	9.7	11.3
General Fund – Uncommitted Balance	17.0	18.0
Total General Fund	26.7	29.3
Earmarked Reserves	176.6	225.4
Total Usable Reserves	203.3	254.7

General Fund

14. The General Fund includes delegated funding for schools and the uncommitted balance of the County Council which is held for unforeseen risks that require short term funding. The balance of £18m represents 3.8% of the net budget (excluding schools' delegated budgets for 2022/23) which is slightly below the target level of 4% to 7% set out in the Council's reserves policy. The new MTFS 2023-27 includes plans to increase the uncommitted fund to £23m by the end of 2026/27.

Earmarked Revenue and Capital Funds

15. Earmarked funds totalled £225m as at 31 March 2022 compared with £177m at the same time the previous year. The main reason for the change was an increase in the capital financing reserve due to slippage on some projects and the approach to apply other sources of capital funding, e.g. grants, where the grant conditions allow, before using the funding in the capital financing reserve.
16. Details of the earmarked revenue funds can be found in Note 12 to the accounts. The significant earmarked funds held are:
- Capital Financing £111m. 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, both in 2022 and 2021, is net of £25m investment in Pooled Property Funds. The funding of the £25m 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 £32m. 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 £29m at the end of 2021/22 and is forecast to increase to £91m by the end of 2026/27.
 - Insurance £16m. 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 £65m. Funds for a range of issues including health and social care initiatives, public health initiatives, business rates reset and a range of service developments and initiatives including transformation projects as detailed in Note 12 to the accounts.
17. Capital receipts and capital grants unapplied total £1m. The balance held represents funds received, but not yet used. The amounts vary as and when capital projects complete.
18. 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.

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 net surplus on the Provision of Services for 2021/22 of £20m compared with a net surplus of £48m in 2020/21. The reduction is mainly due to an increase in gross expenditure in the Adults and Communities and Children and Family Services (C&FS) departments arising from MTFs growth, and the write out of academy conversions within C&FS.

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 2022 net assets of the County Council were £485m (31 March 2021, £125m). The principal reason for the increase is due to a decrease in the net pension liability of £259m and the increase in reserves mentioned earlier in the report.
23. As at 31 March 2022, the net deficit on the pension fund as assessed under international accounting standard 19 (IAS19) had decreased to £576m from £836m at the same time last year. This was mainly due to an increase in the discount rate used to calculate the present value of future pension fund liabilities (the higher the discount rate used the lower the present value of future liabilities). During the year corporate bond yields increased, resulting in a higher 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.
25. However, it is the triennial fund valuation, most recently as at 31 March 2022, that actually informs the levels of future contributions required. The results of the latest valuation reported that the fund had increased to a 105% funded position (89% previously), which was a remarkable improvement largely driven by investment return over the last 3 years.
26. The Balance Sheet also shows the valuation of Property, Plant and Equipment owned by the County Council. The total held was £984m as at year end compared with £958m for the previous year end. The increase reflects capital additions in year

through the capital programme, revaluation gains and losses, and reductions for depreciation.

27. Accounting provisions increased slightly to £8m from £7m previously. 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, representing the estimated value of outstanding unsettled claims at 31 March 2022, the County Council's 'notional' share of the district councils' business rates appeals and a provision for the restoration of Firs Farm. The share of business rates appeals 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.
28. 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 totalled £465m as at 31 March 2022, compared with £360m at the same time last year. The increase is mainly related to the increase in the balance of usable reserves and long term capital grants received in advance (section 106 receipts not yet applied) as at year end.
29. The capital financing requirement (CFR) is shown in Note 39 to the accounts and totals £214m 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 £49m which will be reversed over the MTFS due to planned increases in the CFR from (internal) borrowing to fund the four year capital programme. This position is refreshed annually as part of the MTFS.

ANNUAL GOVERNANCE STATEMENT

30. 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

31. The financial statements also include the Pension Fund Accounts for the Local Government Pension Scheme administered by the County Council.
32. The last available triennial actuarial valuation of the pension fund showed that as at 31 March 2022 the fund's assets covered approximately 105% of the liabilities accrued up to that date. This funding level was a significant increase on the 89% position reported in the 2019 valuation. Although the funding level of individual employers will vary the positive position indicated that the contribution rates for the majority of employing bodies is expected to have peaked
33. While this is a positive position there are still significant risks. In November 2022 the Pension Committee received a report on the draft results and noted that taking the long-term funding view, careful consideration needed to be given to the result and

how it impacted the employer individual results particularly with inflation at levels above 10%.

34. To ensure that the fund remains financially sound to meet benefit payments, the Fund Actuary recommended the rate of employer contributions on an individual employer basis for each employing body in the fund for the next three year period. The proposed levels have been consulted on with employers and confirmed by the Pension Committee at its meeting on 3 March 2023. The Actuary is scheduled to issue the final valuation report, including the final employer rates, later in March 2023.
35. There were 286 employers within the fund and over 99,000 members in the pension scheme as at 31 March 2022.
36. The overall net assets of the fund increased during the year to £5.8bn from £5.2bn at the end of last year end. For all LGPS Funds, investment returns have been significantly higher than last year. Details of the investments held are shown in Note 12 to the Pension Fund Accounts.

KEY FINDINGS OF THE EXTERNAL AUDITOR

Audit Findings Report – Leicestershire County Council 2021/22

37. The auditor has reviewed the financial statements and anticipates issuing an unqualified opinion. The auditor will provide an update to the Corporate Governance Committee on 16 March 2023.
38. It should be noted that, as a result of increasing regulation on audit firms, the external audit for 2021/22 has increased significantly in its coverage and expectations. This is also reflected in the increase in fees in recent years and those advised for the new audit contract from 2023/24.
39. While there were some issues identified during the audit the auditor has reported that in respect of the significant risks identified in the audit plan:
 - there was no evidence of management override of controls,
 - two issues in relation to revenue recognition,
 - no issues in respect of the risk of fraud,
 - a minor issue in relation to the valuation of the pension fund,
 - the Council has correctly applied the legislative and CIPFA Code of Practice requirements for infrastructure assets, and
 - no issues in respect of the completeness of non-pay operating expenditure.
40. Overall, there were two material issues identified during the audit of the financial statements. These have been corrected and the external auditor anticipates issuing an unqualified opinion on the County Council accounts.
41. There were also some smaller potential issues raised that are not material. All but one have not been adjusted for in the financial statements as agreed with the external auditor.

42. The detailed explanations of the differences will be reported to the Corporate Governance Committee on 16 March 2023, and are included below for information.

Material Items

43. Academy Land Valuations – when schools convert to Academy status the Council provides the academies with a 125-year lease but retains legal title to the land. During the 2021/22 audit the Council and the external auditor reviewed the valuation method used for school land. Following this review the Council and the auditor have now concluded that the previously agreed valuation method (to use current market value is no longer appropriate) and to instead revalue the land assets to £1 to reflect the restricted use to the authority. As a result, a prior period adjustment to the accounts has been made and a reduction of £211m to the value of land and buildings in the balance sheet as at 31 March 2022.
44. Incorrect netting off of debtor and creditor balances – the accounting records contain certain codes that are managed on a gross basis to assist with reconciliations. An example is with VAT – input tax is debited to one code and output tax is credited to a separate code. However, the net balance is what is due from or to the Council. As part of the preparation of the balance sheet an exercise is undertaken to net down these codes. On one code an error occurred and the code was incorrectly netted down. The total correction required was £43m, requiring an adjustment to gross back up debtors and creditors. This correction has been made in the accounts.

Other Items

45. Valuation of school buildings – the basis of the valuations provided by the external valuer did not correctly include the requirements of the Department for Education (DfE) guidance in respect of school areas resulting in an understatement of the value. The valuations have now been amended and the accounts updated. The adjustment required was £4.8m as at 31 March 2021, and £5.3m cumulative as at 31 March 2022. The accounts have been adjusted for this item.
46. The following have been reviewed with the auditor and agreed to not be material and have therefore not been adjusted for in the accounts.
47. Understatement of Pension assets – in order to produce the draft accounts within the timescales required by the Accounts and Audit Regulations it is sometimes necessary to use estimates for certain entries in the draft accounts – particularly when the data is dependent on a third party. Once the actual figures are eventually reported (sometimes many months later), these can differ from the estimates used. An example is the value of pension fund assets as part of the estimate of the net pension liability as assessed by accounting standard IAS19. As at 31 March 2022 the difference relating to the Council was a reduction in the net pension liability of £2.3m
48. Potential understatement of the debtors credit loss allowance – the Council uses a combination of individual review of larger debts and estimates for smaller debts when making a provision for potential unrecoverable debts as at year end. The auditor has challenged some of the percentages used and has calculated a potential understatement of the allowance (of £2m) if higher percentages were used. However, the Council has a low historical experience of bad debt write offs and does not

calculate the required provision on that basis, but it has agreed to review the percentages used.

49. Delay to the de-recognition of academy schools - there were two schools de-recognised in 2021/22 instead of 2020/21. Both schools converted to academy status during 2020/21 and should have been derecognised in that year. Processes have been updated to avoid this delay in writing out the values.
50. Movement of valuations on assets not revalued in 2021/22 – in line with the CIPFA accounting Code of Practice the Council values land and building assets on a rolling programme at least once every five years. In addition there is a requirement to ensure that values are not materially misstated as at the balance sheet. It is impractical and expensive to value every asset every year and so high value assets are subject to more frequent valuations. As at 31 March 2022 the Council revalued almost £300m of its total £450m of land and building assets. For assets not subject to valuation as at the 31 March 2022 an accounting estimate shows that there could be a potential £2.8m increase in valuations had all assets been valued.
51. Potential overstatement of debtors balances – within a sample of invoices outstanding as at year end there was one invoice that had subsequently been credited and cancelled after year end, and one invoice that has not yet been paid while a dispute on an element of the overall charge is being resolved. This is normal in the course of business where invoices can be disputed and clarifications and corrections made. Extrapolating these examples for the overall population of debtors shows a potential overstatement of income of £1m as at 31 March 2022.

New Issues and Risks

52. There was a new audit engagement lead and mostly new audit team in place for the audit of the 2021/22 accounts, both on the County Council and the Pension Fund. This, together with enhanced levels of testing now required from auditors', has resulted in the identification of some areas of the accounts that could be improved and may assist the audit team in future audits. These issues are listed below and will be reviewed during summer 2023, after the 2022/23 accounts have been completed:
 - General ledger code structure – number of codes used.
 - Journal postings below £20,000 – auto approved, although segregation is in place .
 - Grossing up of control codes – journals then required to net down.
 - Monthly allocations (journal postings) – process to allocate the income and expenditure net totals to the balance sheet (to balance the balance sheet).
 - Reallocation of costs – internal recharges net off on fixed codes.
 - Reconciliation of code balances – example of one code not fully reconciled.
 - Derecognition of plant and equipment disposal – fully depreciated assets, the net position is correct but the gross balances are incorrect. Housekeeping exercise required in the fixed asset register.

Audit Fees

53. The auditor has confirmed their final audit fee for 2021/22 as £139,777 compared with the proposed fee of £114,715 in the audit plan. The increase in the fee is due mainly to the additional work required for the corrections necessary to the accounts.

Audit Findings Report – Leicestershire County Council Pension Fund 2021/22

54. The auditor's work is substantially complete and they anticipate issuing an unqualified opinion for the pension fund.
55. During the audit there was one adjustment identified totalling £7.95m relating to the valuation of hard to value pooled assets, which was not available when the accounts needed to be prepared. For these assets estimates have to be made as the valuations are not known for many months after the year end date. The amount was not material overall and this was not adjusted for in the accounts. This was agreed with the external auditor.
56. There were two control issues reported relating to; journal postings below £20,000 – auto approved (without separate approval), and senior finance officer's ability to enter journals. No irregularities were identified and management have agreed to make changes to remove the risks.
57. There were two inconsistencies identified following a review of the accounts to the pension fund annual report. These were rounding and timing differences. The annual report has been updated to agree with the Pension Fund final accounts.
58. Other recommendations made in the appendix to the auditor's report around the observations below – these were all accepted:
 - No evidence of review of assumptions used in the valuation of the pension fund's direct property portfolio;
 - Internal control reports and bridging letters, two fund manager reports were unavailable;
 - Bodies joining the Pension Fund not accounted for (as at the year-end date) – details not available at the time the draft accounts had to be prepared.
 - IT system – access to Oracle Fusion, password configuration, and batch job management.
59. Updates were also made to some disclosure notes within the Pension Fund accounts to ensure that they fully meet the requirements of the CIPFA accounting code of practice. These are listed in the appendix to the auditor's report.
60. The auditor has confirmed their final fee for audit of the pension fund is £33,193, and £17,000 for the IAS19 assurance work (for the County Council and the auditors of the scheduled admitted bodies with a 31st March year-end). Both final fees are in line with the proposed fees in the audit plan for 2021/22.

Value for Money Arrangements

61. The Auditor's Annual Report (AAR) was received in February 2023 and will be reported to the Corporate Governance Committee on 16 March 2023. A copy is attached for information, Appendix F.
62. The AAR is a detailed review of the value for money (VfM) arrangements at the Council. The AAR is a relatively new report, required by the National Audit Office. The first AAR, for 2020/21, was reported in January 2022. The report covers five areas. These are:

- Financial sustainability;
- Governance;
- Improving economy, efficiency and effectiveness;
- The opinion on the financial statements; and
- Pension Fund arrangements.

63. Overall, the auditor's report is very positive. The external auditor has concluded that the Council has a good track record of sound financial management, had appropriate arrangements in place to manage the financial resilience risks, has a clear and documented governance framework in place and a well-developed performance management framework. No significant weaknesses have been reported.

RECOMMENDATION

64. The Committee is recommended to approve the financial statements for 2021/22.

BACKGROUND PAPERS

Provisional revenue and capital outturn, Cabinet – 27 May 2022

<https://politics.leics.gov.uk/documents/s169173/Provisional%20Outturn%20Report%20-%20FINAL.pdf>

Report to Corporate Governance Committee – 16 May 2023

<https://politics.leics.gov.uk/documents/s175377/External%20Audit%20of%20the%2021-22%20Statement%20of%20Accounts.pdf>

CIRCULATION UNDER THE LOCAL ISSUES ALERT PROCEDURE

None.

EQUAL OPPORTUNITIES IMPLICATIONS

None.

APPENDICES

Appendix A – Financial Statements 2021/22

Appendix B – External Auditors Report - County Council

Appendix C – External Auditors Report - Pension Fund

Appendix D – Letter of Representation – County Council

Appendix E – Letter of Representation – Pension Fund

Appendix F - Auditor's Annual Report 21/22

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