

Audit update report

Warwick District Council

Year ended 31 March 2022

18 January 2023



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1. Headlines

Financial Statements

Our audit of the Council's financial statements has been challenging and time consuming for officers and auditors. There is more of the audit still to be completed than any of us would have wished. This is primarily owing to delays, significant in some cases, in obtaining working papers and reports – often exacerbated as officers learn how to get the best out of the new ledger system.

Initial delay in publication

Officers notified the audit team well in advance that they would not be able to publish draft accounts by 30 July, as required by the relevant legislation. We agreed an expected date of early September, which Officers were able to meet. While they are to be commended for sticking to the revised timetable, on receipt of the draft financial statements it immediately became clear that there had not been a robust quality assurance process to ensure that the financial statements were as free from error as possible.

A need to enhance Quality Assurance processes

Our initial review of the financial statements, before any testing had begun, identified very significant increases in both income and expenditure for portfolios within the Comprehensive Income and Expenditure Statement (CIES) compared to the previous year, which were not expected. Officers subsequently identified that reports used to prepare the CIES had been set up incorrectly. The effect was to reduce reported Gross Expenditure from £138,857k to £95,355k and Gross Income from £116,906k to £73,404k. As the difference of £43,502k affected both expenditure and income equally, Net Expenditure was unchanged at £21,951k.

Based on our audit work completed to date, we expect highly material changes to all four primary statements – the CIES, Balance Sheet, Movement in Reserves Statement (MiRS) and the Cash Flow Statement.

Other significant disclosure errors that the audit team identified on initial review included Note 14 – Property, Plant and Equipment showing vehicles, plant & equipment, infrastructure and community assets being revalued when they weren't; and Note 19 – Debtors – including a line showing a negative prepayment of £3,265k, which should have been included in Creditors.

Difficulties in providing appropriate reports for audit sampling

Officers and auditors spent significant amounts of time working together to produce and agree suitable reports for audit testing in a number of areas. In particular journals, debtors and creditors. Our work on journals has been made more complicated owing to the change in financial accounting system part way through the year. Management override of controls, which includes the potential misuse of journals, is a significant risk for all audits, and is an area of particular audit focus. Our work is supported through of specialized software which allows for the identification of journals which meet specific characteristics. This approach provides higher levels of assurance to both auditors and Those Charged with Governance than a purely manual approach would. However, auditors need certain information to be able to use the software, and this proved problematic on both systems. With the new ledger system it took a significant amount of time for us to be provided with a journals report which showed all of the officers who had been involved in the journal, rather than just the last individual involved. This is a key area for us to be able to test for appropriate segregation of duty. We were provided with this information in early December.

1. Headlines

Financial Statements (continued)

Our work on trade receivables and trade payables has also been far more challenging this year. Due to the continuous drive to improve the quality of the audit work that we do, combined with the number and scale of the errors that we have identified during our audit work to date, we asked officers to provide supporting reports for receivables and payables in a different format to those provided in previous years. The Council's finance team were not expecting to have to do this, and as a result, we have experienced considerable delays in obtaining suitable reports for audit in both of these areas

Included in Note 19 – Debtors – is an amount of £5,988k for “trade receivables”. These are amounts owed to the Council, usually by trade customers. In most councils officers are easily able to run reports analysing this balance, usually on an aged basis, which is then used for debt collection and credit control. Officers were unable to do this, and provided us with a transaction listing covering thousands of lines, on both debit and credit sides. These original reports were not in a format that was appropriate for audit testing because they included hugely material control account balances brought forward from prior years with no clear way to determine what amounts were owed to/from the Council as at 31 March 2022.

The first listing was provided to audit on 7 September 2022. Officers and auditors spent considerable time in trying to identify transactions that netted off or may have been tested elsewhere. After many weeks the final transaction report that was provided for audit included debit items totalling £147,831k and credit items totalling £141,844k. These two items total £289,675k, to support a balance of £5,988k. It took until 6 December for us to be provided with a debtors report in a suitable format for testing some of the balance – with Officers still working on providing a report supporting the remaining categories.

The position on trade payables of £5,454k within Note 22 – Creditors – is very similar. The report presented for audit had debit items of £114,296k and credit items of £119,750k, totalling £230,046k. Again, we would expect the Council to be able to easily produce reports which support this amount, and use them to ensure suppliers are paid on time.

Additional audit resource required

We have added to the strength and depth of our audit team, including a further two Assistant Managers, in an attempt to complete as much of our audit work as possible before the Christmas break. Despite this, the audit has run over into 2023 and it has been necessary to delay the issue of our final Audit Findings Report to the Audit & Standards Committee.

Material decrease in valuation of Property, Plant and Equipment

The Balance Sheet presented for audit, supported by the detailed Note 14, shows a Net Book Value for Property, Plant and Equipment as at 31 March 2022 of £604,839k. As set out in more detail on page 10, this figure is overstated by £12,772k and will be amended to £592,066k.

Uncorrected items

The audit of the Warwickshire Pension Fund has identified that gross assets are understated by £13.6m owing to the valuation being received in arrears and the Pension Fund not being able to capture the movement in the value of the investment in the final quarter of 2021/22. Warwick District Council's share of this is £0.81m, meaning that net assets are understated by this amount. Were management to adjust for this the net LGPS liability would be reduced by the same amount, from £33.7m. However, management have declined to amend on the basis that it is immaterial and will be corrected in the next valuation. Members are asked to agree Officers' approach, and this is included in the Letter of Representation requested.

1. Headlines

Financial Statements (continued)

As we have stated, our audit is ongoing, and there is still a considerable amount of audit work to complete. This includes:

- journals testing;
- fees, charges and other service income testing;
- debtors testing;
- property revaluations;
- audit of capital disclosures;
- other service expenses testing;
- creditors testing;
- testing of reliefs awarded to council tax and business rates payers;
- testing of the Housing Revenue Account disclosures;
- audit of the Group Financial Statements;
- Movement in Reserves Statement;
- Narrative Report; and
- Cash Flow Statement.

Owing to the amount of work still outstanding, we are unable to provide an audit findings report at this stage. On completion of our audit work we will also need to complete the following:

- receipt and review of management representation letter; and
- review of the final set of financial statements.

We are currently unable to conclude that the other information to be published with the financial statements, primarily in your Narrative Report, is consistent with our knowledge of your organisation and the financial statements we have audited. This is owing to a number of queries on the Narrative Report itself still being outstanding and the amount of audit work remaining, as set out above.

1. Headlines

Value for Money (VFM) arrangements

Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to consider whether the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. Auditors are now required to report in more detail on the Council's overall arrangements, as well as key recommendations on any significant weaknesses in arrangements identified during the audit.

Auditors are required to report their commentary on the Council's arrangements under the following specified criteria:

- Improving economy, efficiency and effectiveness;
- Financial sustainability; and
- Governance

We have not yet completed our VFM work. Our detailed commentary will be set out in the separate Auditor's Annual Report, which will follow once our work is complete.

Events since February 2022 have had a significant negative impact on the Council's medium to long term financial sustainability. Recurrent savings of £3m need to be secured to enable the Council to be able to set a balanced budget from 2023/24 onwards. The Council needs to ensure that only fully worked up, realistic savings or income generation schemes are included in the medium term financial strategy. Recommendations made as part of our 2020/21 work still need to be addressed.

We will also need to consider whether the significant challenges we have encountered in our audit work, and the number and magnitude of adjustments to the financial statements, constitutes a significant weakness.

Our findings to date are set out in the value for money arrangements section of this report.

Statutory duties

The Local Audit and Accountability Act 2014 ('the Act') also requires us to:

- report to you if we have applied any of the additional powers and duties ascribed to us under the Act; and
- to certify the closure of the audit.

We have not exercised any of our additional statutory powers or duties.

We expect to certify the completion of the audit upon completion of our work on the Council's Whole of Government Accounts submission. The guidance for this has yet to be issued by the government department, but we expect the Council to be below the threshold for detailed testing.

Significant Matters

We have encountered significant difficulties in the course of our audit work. These are set out on pages 3 to 6.

2. Financial Statements – key messages

Key messages arising from our financial statements work to date

- The financial statements were submitted after the deadline.
- The audit of the Warwickshire Pension Fund has identified that gross assets are understated by £13.6m owing to the valuation being received in arrears and the Pension Fund not being able to capture the movement in the value of the investment in the final quarter of 2021/22. Warwick District Council's share of this is £0.81m, meaning that net assets are understated by this amount. Were management to adjust for this the net LGPS liability would be reduced by the same amount, from £33.7m. However, management have declined to amend on the basis that it is immaterial and will be corrected in the next valuation. Members are asked to agree Officers' approach, and this will be included in the Letter of Representation requested.
- Our work on Note 35 - Related Party Transaction identified two undeclared Member interests with organisations with which the Council had transactions during the year. This resulted in an increase in the disclosure note of £47k. While this is below our trivial level, it is very important that Members (and Officers) declare all organisations in which they have an interest so that they can be protected from any allegations of impropriety. In this instance the interests were identified by the audit team undertaking Companies House searches of publicly available information. We consider this to be a control weakness, and will raise a recommendation in our final report.
- Note 21 - Cash & Cash Equivalents totals £50,727k and includes £1,023k in respect of "Bank Current Accounts". Our audit work identified there are amounts totalling £735k which are historic cash balances that have been rolled forward for a number of years, some with little or no change from their values as at year end in 2020-21. From discussions held with Officers these amounts are not expected to be received and therefore these amounts will be written off and removed from Note 21. This will reduce the amount per Note 21 from £1,023k to £288k. This will in turn affect the Financial Instruments Note, the Cash Flow Statement and the Balance Sheet.
- Note 17 - Financial Instruments for Current Investments totals £77,179k. Included in this figure is "Bank Current Accounts" totalling £1,977k. This relates to historic bank balances which have been carried forward for a number of years and recorded incorrectly as a Short Term Investment. These amounts are not expected to be collectable given the time that has passed and will be written off. There is also an issue of some amounts being double counted in both the Short Term Investments breakdown and the Cash & Cash Equivalents breakdown. For example, the £411k Bank Current account, which has been agreed to the appropriate Bank Statement and Bank Letter, should be recorded as Cash and Cash Equivalents but it is included within the £1,977k and therefore this would be double counted on the Balance Sheet as the amount is included in both the Short Term Investment line and the Cash & Cash Equivalents line on the Balance Sheet. We consider the write off of £1,977k of "Bank Current Accounts" and the write off of £735k from the cash and Cash Equivalent balance, to be a control weakness, and have raised a recommendation.
- Note 14 – Property, Plant & Equipment – was amended to correct two errors. The first error is around double counting of asset valuations. This saw the Cost / Valuation of assets decrease by £18,275k from £628,325k to £610,050k. The second error is incorrect disclosure of depreciation. This saw depreciation decrease by £5,503k from £23,487k to £17,984k. This had the total effect of reducing the Net Book Value of assets as at 31 March 2022 by £12,772k from £604,838k to £592,066k. This will be reflected in the Balance Sheet.
- Note 19 – Debtors – includes a negative line for "Prepayments" in the amount of (£3,265k). This is a creditor balance will be removed from Short Term Debtors and shown as a positive Creditor of £3,265k in the Short Term Creditors Note. This will be updated on the Balance Sheet but will not affect the net position as the amounts being amended are equal and opposite.

2. Financial Statements – key messages

- The Council's accounting policy for measurement of property states "Assets included in the Balance Sheet at current value are revalued sufficiently regularly to ensure that their carrying amount is not materially different from their fair value at year-end, but as a minimum every five years." This policy is consistent with the CIPFA Code. However, Note 14 – Revaluations – shows that assets included in the Balance Sheet with a value of £498k were last valued in 2015/16. The Council is therefore not complying with its own policy or the CIPFA Code. We consider this to be a control weakness, and will raise a recommendation in our final report.
- The Annual Governance Statement was amended following audit to fully comply with the Code. In the version of the accounts provided for audit, there was no:
 - discussion of group activities and applicable internal control.
 - action plan.
 - conclusion.
 - update relating to the two significant governance issues included in the previous year's AGS.
- Our work on the Narrative Report is ongoing. However, we have already agreed a number of amendments with Officers to ensure that the Report correctly reflects the financial statements and is factually correct.
- Note 36 – Capital Expenditure and Capital Financing – initially included a value of £244k in respect of Minimum Revenue provision (MRP). The correct figure, as supported by the Council's working paper, is £344k. Officers have updated the note.
- Officers have made a number of minor changes to the financial statements to correct typographical errors.
- Officers made adjustments to a number of notes in order to improve clarity and to better comply with the CIPFA Code. None of these adjustments impacted the Council's financial performance.

3. Value for Money arrangements

Approach to Value for Money work for 2021/22

The National Audit Office (NAO) issued its guidance for auditors in April 2020. The Code requires auditors to consider whether the body has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

When reporting on these arrangements, the Code requires auditors to structure their commentary on arrangements under the three specified reporting criteria.



Improving economy, efficiency and effectiveness

Arrangements for improving the way the body delivers its services. This includes arrangements for understanding costs and delivering efficiencies and improving outcomes for service users.



Financial Sustainability

Arrangements for ensuring the body can continue to deliver services. This includes planning resources to ensure adequate finances and maintain sustainable levels of spending over the medium term (3-5 years)



Governance

Arrangements for ensuring that the body makes appropriate decisions in the right way. This includes arrangements for budget setting and management, risk management, and ensuring the body makes decisions based on appropriate information



Potential types of recommendations

A range of different recommendations could be made following the completion of work on the body's arrangements to secure economy, efficiency and effectiveness in its use of resources, which are as follows:



Statutory recommendation

Written recommendations to the body under Section 24 (Schedule 7) of the Local Audit and Accountability Act 2014. A recommendation under schedule 7 requires the body to discuss and respond publicly to the report.



Key recommendation

The Code of Audit Practice requires that where auditors identify significant weaknesses in arrangements to secure value for money they should make recommendations setting out the actions that should be taken by the body. We have defined these recommendations as 'key recommendations'.



Improvement recommendation

These recommendations, if implemented should improve the arrangements in place at the body, but are not made as a result of identifying significant weaknesses in the body's arrangements

3. VFM - our procedures to date

We have not yet completed our VFM work. Our detailed commentary will be set out in a separate Auditor's Annual Report.

As part of our work, we considered whether there were any risks of significant weakness in the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources. The risks we have identified are detailed in the table below, along with the further procedures we have performed to date.

Risk of significant weakness	Procedures undertaken	Auditor view
<p>The Medium Term Financial Strategy (MTFS), presented to Council on 23 February 2022, includes cumulative savings / income generation schemes of around £6.0m. In addition to these there is a further £1.2m of recurrent savings that still need to be identified by 2026/27.</p> <p>There is a risk around financial sustainability, and whether the Council has realistic, robust plans to move to a balanced financial position in the longer term. This risk is heightened as the cancelling of the proposed merger with Stratford on Avon District Council will mean that some of the anticipated savings are unlikely to be achieved.</p>	<p>To address this risk we have looked at the arrangements in place to identify savings or income generation schemes, and how robust and realistic these are.</p>	<p>The Quarter 1 2022/23 Budget Report, presented to Cabinet in September 2022 states "Recurrent savings of £3m need to be secured to enable the Council to be able to set a balanced budget from 2023/24 onwards. Officers are currently reviewing ways of reducing the deficit, including income generation, service efficiency and cost saving schemes. This work and its outcomes will be reported to Cabinet as part of the Q2 Budget Report in December."</p> <p>The Council MTFS therefore required the use of reserves while longer term plans were worked up. We are considering whether, in accordance with the NAO guidance, this represents a significant weakness in the Council's arrangements.</p>
<p>The Council will need to develop and embed appropriate governance arrangements for the newly formed housing company, Milverton Homes Limited, and also establish arrangements to assess whether the expected benefits are realised.</p>	<p>To address this risk we have gained an understanding of the arrangements that the Council has put in place, and how governance works in practice. This includes how the Council satisfies itself regarding progress and benefits realisation.</p>	<p>While there has been limited reporting to Members, we do not consider this to be inappropriate as there has been little activity that Members need to be aware of. Key reports such as loan approvals and business plans have been presented to Cabinet for discussion and approval.</p> <p>From the work that we have completed to date, it appears that appropriate governance arrangements are in place. The Council has put in place an independent project monitor and commissioned an internal audit report which has highlighted areas where the Council governance and oversight arrangements needed to be enhanced. At this stage it is too early to consider whether anticipated benefits have been realised.</p> <p>Our work on the audit of the group financial statements is ongoing. We are therefore unable to fully conclude on whether the arrangements, and the related accounting, are appropriate.</p>
<p>Upon receipt of the draft financial statements for audit, we identified significant issues in the financial statements before our testing began. Based on our audit work completed to date, we expect highly material changes to all four primary statements.</p> <p>We therefore consider that this is indicative of an additional risk of significant weakness in the Council's arrangements.</p>	<p>Our audit of the financial statements is ongoing at the time of writing this report.</p>	<p>We will need to consider whether the significant challenges we have encountered in our audit work, and the number and magnitude of adjustments to the financial statements, constitutes a significant weakness.</p>

