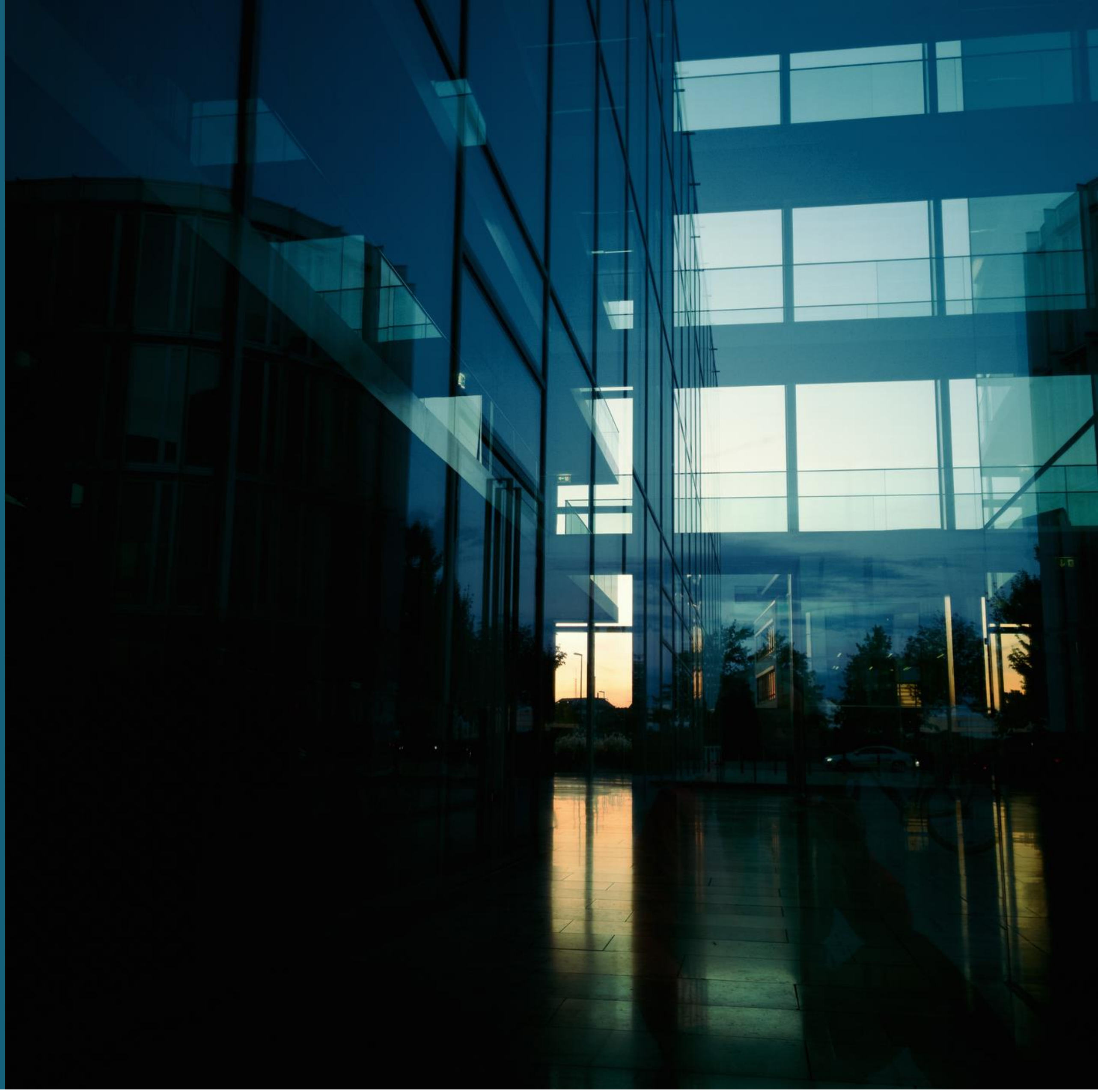
Audit Update Report

London Borough of Hackney – Accounts year ending 31 March 2021 & 31 March 2022

April 2023



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11 April 2023

Dear Committee Members

Audit Update Report – Hackney's accounts year ending 31 March 2021 & 31 March 2022

We are pleased to present our latest Audit Progress Report on the audit of the Council's statements of account, including the Pension Fund accounts, for the years ending 31 March 2021 and 2022. This follows previous reports we have issued and verbal updates we have provided to previous Audit Committee meetings.

At the date of this report our audit of the 2020/21 statement of accounts (including the Pension Fund) is complete subject to finalising procedures on the infrastructure assets matter and completing our concluding procedures. We anticipate issuing an unqualified audit opinion and further to the draft VFM commentary we issued in January 2023 we will have no VFM matters to report. We will issue our Auditor's Annual Report soon after the audit opinion.

Further to the update we provided to the January 2023 meeting, the audit of the 2021/22 accounts remains in progress, and we anticipate completing audit testing (subject to the Council resolving all outstanding queries promptly) by the end of April 2023. However, a new national issue has arisen relating to the pension liabilities reported in the 31 March 2022 Council accounts and the impact of the recent triennial valuation. We will provide a verbal update to the Committee.

If you would like to discuss any matters in more detail, then please do not hesitate to contact me on 07977 261873.

Yours faithfully

Suresh Patel, Partner - Mazars LLP

01

Section 01:

Status of the audit

Section 01: Status of the audits

Year ending 31 March 2021

Following the January 2023 Audit Committee meeting, in February the Council provided their response to the infrastructure issue. Following our initial review and queries, the Council provided further information and evidence to support their response in March. We are in the process of completing our audit procedures and at this stage are satisfied with the Council's response and the expected changes made to the 31 March 2021 accounts in respect of accounting policies and Note 5 – Property, Plant and equipment. Subject to receiving a final version of the accounts, requesting and obtaining management representation and then completing final procedures we will be able to issue our final audit completion letter and the audit opinion. This includes the pension fund accounts. Having issued the draft VFM commentary to the January 2023 meeting, we can then also issue the Auditor's Annual Report for 2020/21.

Year ending 31 March 2022

At the January 2023 Audit Committee, officers provided an update on the 2021/22 statement of accounts and audit. We have now substantially completed the audit of the 2021/22 Pension Fund accounts and we have no matters to report to the Committee.

At the date of this report, for the audit of the 2021/22 Council accounts, there remain a small number of audit procedures that are in progress and where we are continuing to work with officers to resolve audit queries. Subject to the prompt resolution of these queries we anticipate completing all audit testing by the end of April.

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However, due to the protracted nature of the 2021/22 audit, a new national issue has arisen that may impact the timing of concluding the audit. The issue relates to the Council's reporting of its assets and liabilities associated to its membership of the Hackney Pension Fund. The draft Councul accounts include values based on actuarial reports which use estimates as at 31 March 2022 based on roll forward of information (e.g. membership data) since the last triennial review at 31 March 2019. However, on 1 April 2023 the Council received the latest triennial review from its actuaries, which provides actuals for 31 March 2022. These values are likely to be materially different to the estimated values used for the draft accounts. Auditors cannot place any reliance on the new triennial valuation until the Pension Fund auditor has carried out audit procedures on the membership data that supports the valuation. This is unlikely to commence until July 2023. This matter is currently being discussed at a national level and a resolution is being sought. We will provide the Committee a verbal update.

We include a summary of the status of the audit to date on page 6 of this report and we will issue comprehensive Audit Completion Reports on completion of the Pension Fund and Council audit.

We are currently drafting the VFM commentary for 2021/22 and aim to provide a draft to management by the end of April. As we have reported previously, we have not identified any risks of significant weakness.

Section 01: Status of the audit

Summary

Audit area	Status	Description of the outstanding matters
Property, plant and equipment and Investment Property valuation testing		Our work on land and building valuations, in particular completing our review of the information being provided by the Council's valuer is in progress.
Revenue grants, income and creditors		Following internal review we have very recently made some final requests for supporting evidence from management.
Provisions		We are continuing to review and internally evaluate the available data to conclude on our assessment of the Council's year end provisions.
IAS19 - defined benefit liability valuation		As outlined on page 5 there is a national issue impacting pensions.
Events after the reporting period		Review of events after the reporting period, up to the point at which we sign our audit report.
Final review procedures		We are currently completing our file review. We cannot complete our closure procedures until all outstanding points are resolved and the revised accounts are received.
File closure procedures		Following completion of our review process , we will need to complete our file closedown procedures, including receipt of communications from management and consideration of post balance sheet events up to the date of final sign-off.
Whole of Government Accounts (WGA)		Our work on the WGA return will take place later in the year once we have received the appropriate guidance from the NAO.

Auditor assessment of potential impact

Likely to result in material adjustment or significant change to disclosures within the financial statements.

Potential to result in material adjustment or significant change to disclosures within the financial statements.

Not considered likely to result in material adjustment or change to disclosures within the financial statements.

Section 01: Status of the audits

Wider responsibilities

Our powers and responsibilities under the Local Audit and Accountability Act 2014 (the 2014 Act) are broad and include the ability to:

- issue a report in the public interest;
- make statutory recommendations that must be considered and responded to publicly;
- apply to the court for a declaration that an item of account is contrary to law; and
- issue an advisory notice under schedule 8 of the 2014 Act.

To date we have not exercised any of these powers as part of our 2020/21 audit.

The 2014 Act also gives rights to local electors and other parties, such as the right to ask questions of the auditor and the right to make an objection to an item of account.

We received one objection for 2021/22 relating to the Council issuing Penalty Charge Notices (PCNs) in the Mount Pleasant Lane area using the Hackney (Mount Pleasant Lane Area – Mount Pleasant Lane, Southwold Road and Springfield Gardens) (Traffic Management and Parking) (Experimental) Order 2020 ("the Springfield ETO"). The objector requested us to make an application to the Court for a declaration that the income generated by the PCNs was contrary to law because the ETO did not prohibit the movement of vehicles along Mount Pleasant Lane as intended and as a result, the PCNs issued for driving through the road closure were ultra vires. They also asked us to issue a public interest report in relation to the same matter.

Audit considerations

We have carefully considered each of the points raised by the objector and carried out specific procedures to compile sufficient, appropriate audit evidence to form a view on the matter. Our work has involved discussions with senior Council officers, reviewing relevant Council documents and considering the relevant Regulations. We have also obtained our own legal advice on the statutory provisions related to PCNs, Traffic Management Orders (TMOs) and ETOs.

Audit Findings

We found that the wording of the Springfield ETO (effective from November 2020) contained an error and, instead of creating the intended road closure, created a road closure which was not possible to implement. The Council correct the error in March 2022. Our view is that the PCNs issued by the Council were ultra vires as the ETO did not prohibit the movement of vehicles along Mount Pleasant Lane as intended. The income received as a result of those PCNs from November 2020 to March 2022 was also ultra vires and are, therefore, items of account that are contrary to law.

Conclusion

We made a recommendation to the Council under section 27(6) of the LAAA that it considers (i) whether to apologise for issuing PCNs unlawfully and (ii) whether to set up a voluntary scheme whereby members of the public can claim a refund for PCNs issued for breaching the Mount Pleasant Lane road closure.

The Council has agreed to refund all PCNs for the location during the period that the Springfield ETO contained the error.

02

Section 02:

Significant findings to date

Section 02: Significant findings to date

In this section we outline the significant findings from our audit. These findings include:

- our audit conclusions regarding other significant risks and key areas of management judgement outlined in the Audit Strategy Memorandum;
- Our audit conclusion regarding they key areas of management judgment related to infrastructure asset useful expected life, and depreciation charge, which were identified during the audit, and not outlined in the Audit Strategy Memorandum;
- our comments in respect of the accounting policies and disclosures that you have adopted in the financial statements. On page 14 we have concluded whether the financial statements have been prepared in accordance with the financial reporting framework and commented on any significant accounting policy changes that have been made during the year;
- any further significant matters discussed with management;
- any significant difficulties we experienced during the audit

Significant risks

Management override of controls	**Description of the risk** In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Due to the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.
	How we addressed this risk We addressed this risk through performing audit work over: • Accounting estimates impacting amounts included in the financial statements; • Consideration of identified significant transactions outside the normal course of business; and • Journals recorded in the general ledger and other adjustments made in preparation of the financial statements.
	Audit conclusion We have no significant findings to report as a result of our work on areas subject to potential management override of controls.

Section 02: Significant findings to date

Valuation of Property, Plant and Equipment (PPE)	
	Description of the risk The CIPFA Code requires that the carrying value of PPE should reflect the appropriate current value as at the year end. The Council has adopted a rolling revaluation model which sees other land and buildings revalued over a five year cycle, and may result in individual assets not being revalued for several years. This creates a risk that the carrying value of those assets that have not been revalued in year is materially different from the year end fair value. Land and buildings including Council dwellings are the Council's most valuable assets accounting for £3.9 billion of the Council's £4.2 billion Property, Plant and Equipment balance at 31 March 2022. In respect of Council dwellings, these are reviewed using a beacon valuation methodology, which values Council stock by grouping assets into type and using a nominated beacon asset for each group. The assessed value is uplifted based on an open market assessment then amended for an adjustment factor provided by government. Due to the high degree of estimation uncertainty associated with valuations and the fact that there were significant findings in the prior year we have determined there is a significant risk in this area
	How we addressed this risk We addressed this risk by reviewing the approach adopted by the Council to assess the risk that assets not subject to valuation at year end are not materially misstated, and considered the robustness of that approach. We also assessed the risk of the valuation changing materially in year, considering the movement in market indices between revaluation dates and the year end, in order to determine whether these indicate that fair values have moved materially.

Valuation of Property, Plant and Equipment (continued)	
	In addition, for those assets which have been revalued during the year we: • assessed the valuer's qualifications; • assessed the valuer's objectivity and independence; • reviewed the methodology used; and • performed testing of the associated underlying data and assumptions.
	Audit conclusion Audit work is substantially complete, with no material findings so far. We are currently assessing the results of the valuation review performed by our internal valuations team on the revaluations of assets to enable us to conclude on this work.

Section 02: Significant findings to date

Investment property valuation

Description of the risk

The CIPFA Code requires that the carrying value of investment properties should reflect fair value. For the Council's £199m of investment properties this is using fair value.

Due to the high degree of estimation uncertainty associated with market valuations and the issues we reported in the prior year, we have determined there is a significant risk in this area.

How we addressed this risk

We reviewed the Council's approach to revaluing its investment property portfolio as at 31 March 2022. For a sample of those assets which had been revalued during the year we engaged our own expert to :

- assess the valuer's qualifications;
- assess the valuer's objectivity and independence;
- review the methodology used; and
- perform testing of the associated underlying data and assumptions.

Audit conclusion

Audit work is substantially complete, with no material findings so far. We are currently assessing the results of the valuation review performed by our internal valuations team on the revaluations of assets to enable us to conclude on this work.

Net Defined Benefit Pension Scheme liability Valuation

Description of the risk

The valuation of the Council's net liabilities (£700.7m as at 31 March 2022) includes use of discount rates, inflation rates, mortality rates etc., all of which should reflect the profile of the Council's employees and other appropriate data. Due to the high degree of estimation uncertainty associated with the valuations, we have determined there is a significant risk in this area

How we addressed this risk

As the Council is the Fund administrator, we have addressed this risk by reviewing the controls that the Council has in place over the information sent to the Scheme Actuary, Hymans Robertson. We have also:

- assessed the skill, competence and experience of the Fund's actuary;
- challenged the reasonableness of the assumptions used by the actuary as part of Technical Actuarial Standards;
- carried out a range of substantive procedures on relevant information and cash flows used by the actuary as part of the annual IAS 19 valuation.

Audit conclusion

There have been no significant findings arising from our review of the defined benefit pension scheme liability valuation.

However, as reported on page 5 there is a new national issue and ongoing discussions seeking a resolution.

Section 02: Significant findings to date

Infrastructure assets

Description of the risk

The government has put in place a statutory accounting override to allow local authorities to treat the value of any replaced component of infrastructure assets as nil, without the need to further evidence that this is the case. The override also removes the requirement for authorities to make prior period adjustments to infrastructure asset balances. The override does not include any provision for matters relating to gross cost or accumulated depreciation, as these matters are anticipated to be addressed through the Code.

The statutory override does not apply to the depreciation charged in year. CIPFA bulletin 12 Accounting for Infrastructure Assets Temporary Solution specifically considers depreciation and useful lives of assets stating that depreciation is an estimate of economic consumption of economic benefits and cannot be a precise measurement.

Given that Infrastructure Assets are highly material, we have identified useful expected lives and the depreciation estimate as a key area of management judgement with a risk of material misstatement.

How we addressed this risk

We addressed this area of management judgement by:

- Reviewing management's review of asset life, residual value and depreciation methodology for infrastructure assets;
- Assessing the expertise of the engineers management use to inform their estimate of useful expected lives;
- Reviewing the accounting policies for derecognition of infrastructure assets to ensure they reflect the accounting treatment applied;

Infrastructure assets (continued)

How we addressed this risk

- Obtaining assurance that the apportionment of NBV and in-year expenditure across classes of infrastructure assets are reasonable;
- Challenging the asset lives determined by the Council where they fall outside of the ranges in the CIPFA bulletin; and
- Ensuring management have included the disclosures required by the Code Update and Amended Regulations.

Audit conclusion

We are satisfied the balances and associated disclosures are materially accurate and appropriately accounted for within the financial statements. We will be making a recommendation to management in respect of record keeping of expenditure on infrastructure assets, to ensure gross book values, and the associated accumulated depreciation, do not become materially misstated following removal of the statutory override.

Section 02: Significant findings to date

Key areas of management judgement

Cyber attack estimates	**Description of the risk** The cyber attack in October 2020 significantly impacted the Academy and Universal Housing systems which provide the Council with information to prepare the Comprehensive Income and Expenditure statement, the Housing revenue Accounts and the Collection Fund. Although the method and principles remain consistent with prior years, the loss of data from the systems, and the continued recovery actions that the Council has been required to make to ensure records are completely updated, has resulted in an increase in the estimates within the core statements. The Council has continued to make progress to ensure systems are up to date, but there remain a number of updates to completed, and as a result we have determined that the estimations within the core statements represent an area of enhanced audit risk.
	How we addressed this area of management judgement We have reviewed the estimation techniques used by officers to derive the material estimates within the core statements and have: • Understood and documented the estimation methods applied; • Considered and challenged the appropriateness of the data used; • Considered and challenged the reasonableness of assumptions made; and • Applied professional scepticism to the above.
	Audit conclusion The estimates impacted by the cyber attack have been formed using a reasonable methodology and the underlying data is appropriate.

Section 02: Significant findings to date

Qualitative aspects of the Authority's accounting practices

We have reviewed the Authority's accounting policies and disclosures and concluded they comply with the Code of Practice on Local Authority Accounting, appropriately tailored to the Authority's circumstances. The accounts have been prepared on a going concern basis and we have not identified any reasons why this would not be appropriate or any material uncertainties that the Council would be required to disclose.

Draft accounts for 2020/21 were provided by the Authority on 6 December 2021 and 2021/22 on 27 July 2022. Both sets of accounts were of a good quality and supporting working papers were made available prior to the commencement of the audit. Staff members were generally timely in response to evidence requests and audit enquiries.

Internal control matters

To date we have identified one matter that we wish to bring to the Committee's attention. During our review of the Council's response to the national infrastructure issue within the financial statements, we noted a required development in the record keeping of expenditure on infrastructure assets, to ensure gross book values, and the associated accumulated depreciation, do not become materially misstated following removal of the statutory override.

Significant matters discussed with management

We have discussed the following significant matters with management:

- The further impact of covid-19 on the council and the associated impacts this may have on items within the Council's financial statements;
- The Council's response to the national infrastructure issue and its proposed amendments to the financial statements to comply with the detailed statutory override; and
- The remaining impact of the cyber attack suffered by the Council on its operations and ability to provide support for figures within the financial statements.

Significant difficulties during the audit

During the course of the audit, we did not encounter any significant difficulties and we have had the full co-operation of management.

Modifications required to our audit report

To date we have not identified any issues which would result in us proposing to issue a modified audit opinion.

03

Section 03:

Value for money

Section 03: Value for Money

Approach to Value for Money (VFM)

We are required to consider whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out and sets out the reporting criteria that we are required to consider. The reporting criteria are:

- **Financial sustainability** - How the Council plans and manages its resources to ensure it can continue to deliver its services
- **Governance** - How the Council ensures that it makes informed decisions and properly manages its risks
- **Improving economy, efficiency and effectiveness** - How the Council uses information about its costs and performance to improve the way it manages and delivers its services

At the planning stage of the audit, we undertake work to understand the arrangements that the Council has in place under each of the reporting criteria and we identify risks of significant weaknesses in those arrangements.

Although we describe this work as planning work, we keep our understanding of arrangements under review and update our risk assessment throughout the audit to reflect emerging issues that may suggest significant weaknesses in arrangements exist.

VFM risk assessment

We have now completed our VFM risk assessment. We have drawn on our understanding of the Council's VFM arrangements from prior year work, updated based on discussions with officers and review of updated policies and procedures. We have also reviewed papers from the Council's Cabinet and other relevant committees. We have not identified a risk of significant weakness for 2020/21.

Consideration of the Cyber Attack

We have considered the impact of the October 2020 cyber attack on our VFM risk assessment. We have reviewed our December 2021 Cyber Impact Assessment report and considered the findings and conclusions. On this basis, we are satisfied that there are no risks of significant weakness in the Council's VFM arrangements arising from the cyber attack.

Reporting

Our work remains in progress and to date we have not identified any significant weaknesses in the arrangements that have required us to make a recommendation.

As noted above, our commentary on the Council's arrangements will be provided in the Auditor's Annual Report in June.

04

Section 04:

Independence and fees

Section 04: Independence & fees

As part of our ongoing risk assessment we monitor our relationships with you to identify any new actual or perceived threats to our independence within the regulatory or professional requirements governing us as your auditors. We can confirm that no new threats to independence have been identified since issuing the Audit Strategy Memorandum and therefore we remain independent.

Audit fees

We have reflected in the table below our estimate of the impact on scale fees set by PSAA of changes in the scope of our work arising from the new NAO Code, revisions to auditing standards and increased regulatory requirements. We will quantify our final fees on conclusion of the audit, provide supporting information and seek agreement with the Group Director Finance and Corporate Resources and then approval by PSAA.

Notes

1. The 2020 NAO Code has increased the work required to understand the Council's VFM arrangements, assess the risk of significant weaknesses and prepare a VFM commentary. This work is in progress and the additional fee will fall within the range established by PSAA.
2. The auditing standard in respect of auditing accounting estimates (ISA 540) was revised requiring auditors to carry out enhanced risk assessment procedures and increasing the focus on professional scepticism. We have used the minimum additional fee published by PSAA for the bottom of our range and the upper end takes into account the risks we have identified.
3. The additional time taken to deal with correspondence from the public and responding to objections results in additional fees. When we have completed our work on certifying outstanding audit years we will quantify the additional time and audit fee.

Area of work	2021/22 Proposed Fee	2020/21 Proposed Fee
Code Audit Work (Scale fee)	£174,266	£174,266
Fee variations:	-	-
- VFM Code requirements (note 1)	£11,000-15,000	£11,500
- ISA 540 (revised) accounting estimates (note 2)	£10,000-18,000	£10,000-18,000
- Correspondence / objections (note 3)	£5,000-7,000	TBC
- Regulatory requirements	£6,000-7,000	£5,225
- Group accounts	£5,000-7,000	£5,200
- Valuation expert	£4,000-6,000	£3,600
- Infrastructure review	n/a	£9,000-11,000
TOTALS	TBC	TBC

Suresh Patel, Partner

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