GOVERNANCE AND AUDIT COMMITTEE

Minutes of the hybrid meeting held on 27 July, 2023

PRESENT:	Mr Dilwyn Evans (Lay Member) (Chair) Councillor Euryn Morris (Deputy Chair) Councillors Geraint Bebb, Trefor Lloyd Hughes, MBE, Keith Roberts, Margaret M. Roberts, Ieuan Williams Lay Members: Sharon Warnes, William Parry, Michael Wilson
IN ATTENDANCE:	Director of Function (Resources) and Section 151 Officer Programme, Business Planning and Performance Manager (GM) Principal Auditor (NW) Committee Officer (ATH) Webcasting Officer (FT)
APOLOGIES:	Councillor Dyfed Wyn Jones
ALSO PRESENT:	Councillor Robin Williams (Deputy Leader & Portfolio Member for Finance), Mr Derwyn Owen (Engagement and Audit Director – Audit Wales), Bethan H. Owen (Accountancy Services Manager)

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1. DECLARATION OF INTEREST

No declaration of interest was received

2. MINUTES OF THE PREVIOUS MEETING

The minutes of the previous meeting of the Governance and Audit Committee held on 29 June, 2023 were presented and were confirmed as correct.

3. EXTERNAL AUDIT :ISLE OF ANGLESEY COUNTY COUNCIL DETAILED AUDIT PLAN 2023

The report of Audit Wales setting out the detailed audit plan for the Isle of Anglesey County Council for the 2022/23 audit year was presented for the Committee's consideration. The Plan set out the work proposed to be undertaken in relation to the financial audit, the performance audit programme for the year along with the programme of grant certification work and audit reporting timetable and fees. The document was presented in draft version pending further discussions with the audited and inspected body.

Mr Derwyn Owen, Engagement and Audit Director for Audit Wales presented the report and provided an overview of the contents. Since the outline audit plan was presented to the Committee in June, 2023 the more detailed risk assessment work in relation to the accounts has been undertaken. Mindful that the auditors do not seek to obtain absolute assurance on the truth and fairness of the financial statements and related notes but adopt a concept of materiality, the level of materiality for the 2022/23 audit of the financial statements has been set at £2.845m. The audit planning and risk assessment work to date has identified the risk of manangement override of controls as the most significant financial statements risk as per Exhibit 1 of the plan. This risk is present in all entities and is not unique to Anglesey. No significant risks specific to the Isle of Anglesey County Council's accounts were identified during the planning stage. Exhibit 2 outlines the other areas of audit focus along with the auditors' planned response; these relate to the valuation of land and buildings, the valuation of pension fund net liability, pension scheme surpluses and issues reported in the 2021/22 audit of accounts report and how they have been addressed to minimise reoccurrence. The audit team is yet to conclude all areas of the risk assessment and should any further significant financial risks arise on completion of this work then the Section 151 Officer will be updated as will the Governance and Audit Committee via its Chair. The detailed Audit Plan will be re-issued if necessary. The programme of performance audit work remains unchanged from that set out in the outline Audit Plan in June. The Audit of Financial Statements Report 2022/23 is scheduled to be finalised and delivered by November, 2023. The proposed audit fee is set out in Exhibit 5 of the plan. Fee rates for 2023/24 have increased by 4.8% for inflationary pressures and the financial audit fee reflects a further increase of 10.2% for the impact of the revised auditing standard ISA 315 on the financial audit approach. This is in line with the industry standards nationally in the private and public sectors. Any fees not required/used will be refunded.

In considering the Plan contents, the Committee highlighted the following –

- A discrepancy between the Welsh and English versions of the Plan with the omission from the Welsh version of the schedule of audit fees.
- The increased audit costs, specifically the nature of the additional requirements imposed by ISA 315 that makes a rise of 10.2% necessary.

  Mr Derwyn Owen referred to Appendix 1 of the Plan which sets out the key changes to ISA 315 and the additional work to the annual audit which these entailed. These include more detailed and extensive risk identification and assement pocedures, a requirement for the auditors to obtain a wider and enhanced understanding of the Council's IT environment, a focus on exercising professional scepticism, the introduction of risk assessments that are scaleable depending on the nature and complexity of the organisation to be audited and a potentially greater use of technology in the performance of the audit.

- The nature and occurence of management override of controls and whether there are measures that can be taken to prevent this from happening rather than detecting it after the event as appears to be the approach as outlined in the auditors' planned response.

  Mr Derwyn Owen confirmed that management override of controls has been identified as a risk in the audit plan in the past few years and is a risk that is common to all entities. Whilst there have been no instances of it happening within the Council there have been several such occurrences across both private and public sector organisations in the UK. It is viewed as a significant risk and as such the auditors must carry out procedures to test the reliability of the financial information and statements presented. As regards prevention, the external auditor assesses the effectiveness of the Council's controls at the end of the financial year while it is internal audit's role to carry out that assessment on on ongoing basis throughout the year in accordance with its programme of work to ensure that the controls in place are operating as they should.

- The implications of ISA 315 for the Council in terms of additional work pressures on Finance Service personnel and whether those have been recognised via the standards or otherwise.

Mr Derwyn Owen advised that the requirements of ISA 315 may result in a greater number of enquiries for the Council. Audit Wales will work with the Finance Service team to expedite the audit and will discuss any increase in workload with the Section 151 Officer.

The Director of Function (Resources)/Section 151 Officer advised that the workload depends on issues identified in the course of the audit as well as the quality of the financial statements and supporting documentation submitted to the auditors. The Finance Service has endeavoured to work with Audit Wales over the past two years to improve the quality of the process and to ensure that its working papers are of a high standard and that the evidence provided to the auditors is sufficient to reduce the number of queries and/or incidence of errors and consequently, the resulting workload on staff.

- The likelihood that in the course of identifying and assessing the risks of material misstatements as required by ISA 315 the auditors will uncover a number of immaterial misstatements which will have to be recorded and which add to the workload and possibly the cost, but may not prove significant in the context of the overall accounts. It was asked whether any course of action can be taken to avoid this happening.

  Mr Derwyn Owen advised that the audit testing strategy is based on the reasonable expectation of identifying material misstatements. Whilst the nature and type of misstatement uncovered as the audit progresses is not something that the auditors have any control over it can determine the level of response as in the case of a material error the potential impact it has on the accounts or with a trivial error whether or not it can be disregarded. However, these are not matters that can be foreseen at the outset of the audit.

It was resolved to note the Detailed Audit Plan 2023.

4. DRAFT ANNUAL GOVERNANCE STATEMENT 2022/23

The report of the Head of Profession (HR) and Transformation incorporating the draft Annual Governance Statement (AGS) for 2022/23 was presented for the Committee's consideration.

The report was presented by the Programme, Business Planning and Performance Manager. To demonstrate good governacne the Council must show that it is complying with the core (and supporting) principles contained within the CIPFA/SOLACE Framework for Delivering Good Governance in Local Government. The draft Annual Governance Statement has been prepared in accordance with those principles.The Annual Govemance Statement for 2022/23 has been streamlined in form and content following the presentation of the Local Code of Governance to the Committee in December, 2022. The Statement sets out the Council's scope of responsibility and expectations regarding how it conducts its business, the Governance Framework and the elements contained thererin, how the effectiveness of the governance framework is evaluated and the assessment of performance against the core principles along with a progress update on issues identified in last year's Statement. Although no significant governance matters were identfied for the year ending 31 March, 2023, the assessment process did identify a number of governance issues that will be addressed in 2023/24 as noted within the Statement. The Statement seeks to provide assurance about the Council's arrangements for the governance of its affairs including its ability to identify opportunities for further improving governance and the management of risk and resources. The Statement has been through an internal process having been considered by the Leadership Team and by the Head of Audit and Risk.

In considering the Annual Governance Statement the Committee raised the following points –

- The meaning of “significant” as it applies in the context of no significant governance matters having been identified for the year ending 31 March 2023.

  The Committee was advised that in relation to the Governance Statement a significant matter would be any matter that affects the Council’s ability to fulfil its statutory duties and to deliver the strategic objectives as set out in the Council Plan for 2023-28. No such matter has arisen as evidenced by the regular update reports and regulatory review reports presented to the Committee during the year. Additionally, the annual report of the Head of Audit and Risk setting out the chief audit executive’s formal audit opinion for the year ending 31 March, 2023 did not find any areas of significant corporate concern.

- The ways in which the corporate scorecard as an effective performance management tool might be further enhanced and whether the process for reviewing the indicators for inclusion on the scorecard should be expanded to include members of the Governance and Audit Committee to provide an additional perspective.

  The Committee was advised that the Corporate Scorecard is in the process of being reviewed to ensure that it aligns with the newly approved Council Plan for 2023-28. The Council’s governance framework of which the Corporate Scorecard is a component is reviewed and refined annually to ensure it remains effective and while it would be impractical to bring the Governance and Audit Committee into the review of the scorecard for 2023/24 mid-process, the suggestion will be considered when reviewing the scorecard for 2024/25.

- Whether the monitoring of the Council’s capital project activity would benefit from the establishment of a dedicated programme management office to provide oversight and scrutiny of the delivery of the Council’s capital projects.

  The Committee was advised that the suggestion for a programme management office for capital projects would be taken back to the Leadership Team for consideration.

Having reviewed the document, the Governance and Audit Committee resolved to approve the draft Annual Governance Statement 2022/23 that will form part of the 2022/23 Statement of the Accounts.

5. DRAFT STATEMENT OF THE ACCOUNTS 2022/23

The report of the Director of Function (Resources)/Section 151 Officer incorporating the draft Statement of the Accounts for 2022/23 was presented for the Committee’s consideration. It was noted that the figures contained within the report are unaudited and may therefore be subject to change.

The report was presented by the Director of Function (Resources)/Section 151 Officer. The draft accounts were signed by the Council’s Responsible Financial Officer i.e. the Director of Function (Resources)/Section 151 Officer on 30 June, 2023 with the audit of the accounts due to commence in August 2023. A correction was made to Table 1 in the report in that the figure of £3,258m in being a contribution from useable reserves and balances should not therefore appear in brackets. Although efforts have been made in recent years to streamline and simplify the accounts by removing notes that are considered nonmaterial, the Statement remains a technical and complicated document. The accounts including the Comprehensive Income and Expenditure Statement are presented in accordance with statutory accounting requirements rather than on the basis of how the Council is funded and as such they contain a number of items which are not charged against Council Tax and which are then reversed out to arrive at the Council's final financial position in respect of reserves and balances.

The following elements of the Statement of Accounts were highlighted –

- The Narrative Report which provides an overview of the Council's financial performance for the year in question covering both revenue and capital expenditure and refers to the Council's vision, priorities and strategies and the challenges it has faced. It also lists the core financial statements that are to follow. The narrative report provides a commentary on how the Council has used its resources during the year to achieve its stated objectives.
- The draft Comprehensive Income and Expenditure Statement (CIES) shows the cost of providing services in the year in accordance with statutory accounting requirements and covers both the Council Fund and the Housing Revenue Account. It includes accounting adjustments such as depreciation and pensions adjustments which are not funded by Council Tax payers so the impact of these are excluded in the note called Adjustments between Accounting Basis and Funding Basis (Note 6 in the Statement of Accounts). The CIES shows that the net cost of services was £179.355m with a deficit of £15.993m on the provision of servces. Adjustments are made as per Table 1 of the introductory report to determine the movement in reserves and balances (Note 6). The CIES and adjustment Note 6 are then brought together in the Movement of Reserves Statement to show the Council balances as at 31 March, 2023 which is a true reflection of the Council's financial position.
- The Movement in Reserves Statement shows the changes in the year in the different reserves held by the Council. The Council had total usable reserves of £54.742m distributed between the General Reserve, Earmarked Reserves, the Housing Revenue Account, School reserves, Capital Receipt Reserves and Capital Grants Unapplied Reserve as at 31 March 2023. This is a reduction from the £58m of the previous year. These are resources which the Council has available to spend. The Council's draft General Fund balance stood at £13.967m which is equivalent to 8.8% of the net revenue budget for 2022/23 and is £6.067m above the minimum threshold for the General Fund Balance set by the Executive which is 5% of the net revenue budget or £7.9m.
- The Exepnditure and Funding Analysis aims to show the real impact of the year's financial performance on the Council's balances. Although it is difficult to reconcile the CIES to the information presented in the tables within the report the Expenditure and Funding Analysis fulfils this function in part. The CIES includes many accounting adjustments which are not true costs which affect the Council's usable balances.To ensure that these accounting costs do not affect Council taxpayers and Council funds, they are cancelled out in the Expenditure and Funding Analysis.
- The Balance Sheet shows the value of the Council's assets and liabilities as at 31 March 2023. The value of the Council's net assets increased by £132.769m from £272.233m in 2021/22 to £405.002m at 31 March 2023. The value of the Council's long-term assets increased by £20.918m due to capital expenditure on the Council's property, plant and equipment and the revaluation of existing assets.The most significant change relates to the accounting valuation of the Pension Fund which for 2022/23 is shown to be in a net asset position of £19.815m which is an improvemnt of £141.014m on the previous year. This is due to the impact of interest rate and bond rate increases upon which the discount factor is based and the Actuary is required to use when discounting the future olbligations of the pension fund with the current value of the pension fund assets. However, as accounting standards do not allow this to be reported as an asset in the Balance Sheet because the Council cannot realise the value of the asset at this point, it is shown as nil on the Balance Sheet. The results of the accounting valuation are explained in the Local Government Pensions note 34 to the accounts.

- The Cashflow Statement shows the changes in cash and cash equivalents of the Council during the financial year and shows how the Council generates and uses cash and cash equivalents by classifying cash flows as operating, investing and financial activities.
- The notes to the accounts provide further information and context to the figures contained in the core financial statements.

In the ensuing discussion on the contents of the Statement of the Accounts the Committee raised the following matters –

- Whether the accounts for 2022/23 show any significant changes or adverse trends compared to previous years' accounts.

  The Committee was advised that a point of focus are the Council's balances which have increased over the past two years due to the provision by Welsh Government of additional funding to meet the cost of the Covid-19 pandemic response but which are now beginning to decrease. The Council has a planned use for elements of its reserves particularly the earmarked reserves and the Housing Revenue Account reserves because those have been set aside for specific purposes. School balances are also expected to reduce as schools fully utilise the Covid catch up funding which was provided by Welsh Government to help pupils make up for missed learning during the pandemic. The £1.212m underspend on the 2022/23 revenue budget has contributed to the Council's General Balances bringing the total to £13.967m although £3.8m of this sum has been committed to fund the 2023/24 budget and the reserves will likely be drawn down again to balance the 2024/25 budget. Any overspend on the 2023/24 budget will also have to be funded from reserves. While there are no changes/movements in the accounts that are a cause of concern at the present time it is foreseen that the Council will face challenges in the future particularly in setting a balanced budget for 2024/25, and a downward trend in the Council's balances is predicted as a result. The position will be reviewed in setting the 2024/25 budget and the Medium Term Financial Plan.

- The lack of specific reference in the accounts to provision for climate change and carbon reduction projects.

  The Committee was advised that a new Capital Strategy is in development which will consider the Council's capital requirements and priorities and how those will be funded. However, addressing all the Council's capital needs and aspirations would require a significant amount of funding which in terms of borrowing is unrealistic and unaffordable. Needs therefore have to be prioritised and balanced against affordability so that the Council does not become financially overstretched to the extent as in some councils where servicing debt costs is putting pressure on revenue resources. The level of borrowing to support capital expenditure has to be carefully considered and the strategy endorsed by the Executive and Council mindful also that the residents of Anglesey may have to pay more annually for investment in assets and for making progress towards net zero targets. Whilst achieving net zero status is among the Council's priorities no specific provision has been made in that regard to date.

- Clarification of the debtors figures, the relationship with the bad debt provision totalling £8.149m and debt collection.

The Committee was advised that the Council's debts are assessed for the value and age of the debt as well as the likelihood of its being successfully recovered. The older a debt the less likely it will be recovered. A bad debt provision is made annually and a charge is made to the revenue budget accordingly which funds the provision. Debts that are authorised to be writen off because they are assessed as unrecoverable are removed from the system and are then charged against the bad debt provision. Some types of debt are more difficult to collect than others e.g. home/residential care debts where vulnerable individuals are involved and the service cannot be withdrawn or where hardship is a factor and these are reflected in the annual assessment. In the case of Council Tax, the tax base when determined annually is not set at 100% to allow for an element of non-collection (the current Council Tax collection rate is aproximately 99.3%). The sum of £8.149m noted in the accounts reflects what the Council taking a prudent approach, has assessed as an amount that may have to be written off (having considered the types of debt outstanding and having exhausted recovery processes) which in the context of the total amount of income collected by the Council annually is not an exceptional sum.

- The impact of interest rate rises on the Council's borrowings taking account of the fact that while the Council will receive a higher return on its investment it will conversely be paying more for borrowing.

The Committee was advised that the Council routinely borrows from the PWLB for a fixed term ranging from one to fifty years and that the interest rate varies according to the length of the loan term with more favouable rates for longer loan terms. Whilst interest rates were low the Council has been using its cash balances to fund capital expenditure as the return on investment was poor. As interest rates have increased the returns on investment are now such that they have surpassed PWLB's long term interest rate thereby raising the question of whether it is now timely for the Council to be taking out borrowing given that it has the capacity to do so having previously used internal borrowing instead of borrowing externally and because any cash surplus would now be better invested than used to fund capital activity. The risk in borrowing long-term at this point in time is that interest rates may reduce and the Council could find itself locked into a higher rate for a length of time when it could have borrowed more cheaply had it waited. In determining whether or not to borrow therefore the Council will consider a number of factors including timing as part of its treasury management strategy. Lending between authorities is also an option albeit on a smaller scale and subject to due diligence checks.

- The increase in the valuation of the Council's assets and the basis for the increase, what it means in practical terms if the value of the assets cannot be realised and whether assets have a part in borrowing.

The Committee was advised that Council borrowing is not secured against any of its assets as the PWLB lending facility is operated by the Government with Government funds. The valuation of assets fulfils accounting requirements. However, the Council will sell assets that are considered surplus to requirements because they no longer have any operational use e.g. schools that have been closed as part of the schools' modernisation programme and the capital receipts have been used to fund new schools. The Council's assets include its housing stock which because the properties are tenanted are valued at Social Housing existing use value rather than market value. In terms of funding capital activity , the Council seeks to maximise grant funding in the first place including the General Capital Grant and supported borrowing from Welsh Government (where the costs of borrowing are met by Welsh Government) in order to reduce the need to borrow externally. The Council will consider undertaking unsupported borrowing if the investment brings in income, generates savings e.g. in running costs or increases the value of an asset but it would have to meet the costs of so doing from its revenue budget in the form of interest payments and the Minimum Revenue Provision which is a charge made to the revenue budget annually to set aside a sum to pay back the loan. These are factors in considering whether to borrow to ensure that borrowing remains affordable. Councils that are experiencing difficulties in servicing their debts have borrowed to invest in commercial properties for income which due to factors including the pandemic have not provided the revenue returns expected.

- Whether the increase in the cost of providing services from £147.569m in 2021/22 to £179.355m in 2022/23 as shown in the CIES is an actual increase and is a year on year increase and if so whether it is a cause for concern.

  The Committee was advised that the increase does in part represent a real increase in the cost of providing services due to inflation and pay rises as borne out by the Council's revenue budget for 2023/24 which at £175m net is an increase in the region of £17m on the previous year's budget. However, the figure for the cost of services in the CIES also includes items such as depreciation and pension current service costs which are included for accounting purposes rather than as a reflection of how the Council is funded. A more accurate comparison on a funding basis is made in the Expenditure and Funding Analysis where the net expenditure has increased from £123.596m in 2021/22 to £148.068m in 2022/23 but having regard to the fact that this figure also includes the HRA which is separate and is not funded by Council Tax. The cost of living crisis is having an impact on the Council in the form of inflation and rising costs and is a challenge going forwards.

- The valuation of the Pension Fund which has changed from a liability of £121.199m in 2021/22 to an asset of £19.815m in 2022/23 due to the impact of interest rate and bond rate increases. If rising interest rates and therefore the impact are seen as potentially short-term it was asked whether the accounts should be restated on the liability and whether it is possible to prevent the distortion in the Balance Sheet which significant variations in the valuation of the Pension Fund can create.

  The Committee was advised that the valuation of the Pension Fund by the Actuary for the purpose of the accounts is theoretical and projects what the Council's liability or asset would be if the fund ceased to exist. It is carried out on an accounting basis and the results do not affect the Council's actual funds.The funding valuation completed every three years for the purpose of calculating the contributions and level of funding required is a more accurate measurement of the true value of the Fund as it considers the actual assets that the fund is invested in at the valuation date and assesses whether the returns on those assets are likely to meet all future payments to members based on all the benefits earned up to the valuation date. For this valuation a different set of assumptions is used. If the value of the assets and future returns are lower than the estimated future liability then the Council's contribution rates will increase to make up the difference over an agreed period of time. At the last funding valuation the Pension Fund was 110% funded.

- With regard to the £40.690m total capital spend for 2022/23 it was noted that whilst £26.595m was capitalised and added to the value of assets in the Council's Balance Sheet, the remainder was charged to the CIES of which £11.881m did not increase the value of capital assets. It was queried whether this could have been predicted.

  The Committee was advised that accounting rules mean that the capital expenditure to which the sum refers is treated as revenue in the accounts because it has not been spent on or increased the value of a Council owned asset. This is the case for example with Disabled Facilities Grant expenditure which for the purpose of the Council's budget and funding is treated as capital expenditure as it is funded from capital resources but because it involves improvements to a private property rather than to an asset owned by the Council is treated as revenue in the accounts.

- Given the complexity of the Statement of Accounts, its value in providing the public readership with a true representation of the Council's financial performance and position was questioned especially as the figures in the financial statements can be misconstrued and are difficult to relate to the Council's actual budget outturn figures. It was suggested that a short and simplified summary of accounts information that is easily accessible to the public could be published and that it be highlighted on the Council's website perhaps alongside the Council Budget Book which provides detailed information about service budgets.

The Committee was advised that the budget monitoring and outturn reports to the Executive provide information about the actual performance of the Council's services against budgets in the year as well as the progress of capital expenditure and activity and that these are available under the committees and meetings section of the website.

The Director of Function (Resources)/Section 151 Officer confirmed that he would consider drafting a one page summary of headline accounts figures for the Council's website.

Having scrutinised the draft Statement of the Accounts for 2022/23 the Governance and Audit Committee resolved to note the draft unaudited main financial statements for 2022/23.

Action: A summary of headline accounts information be produced and along with the Council Budget Book be signposted on the Council's website to be more easily accessed by the public.

6. REVIEW OF FORWARD WORK PROGRAMME

The report of the Head of Audit and Risk incorporating the Committee's updated Forward Work Programme and Training Programme for 2023/24 was presented for the Committee's consideration.

The Principal Auditor highlighted the following –

- The redistribution of items between the September meeting and the subsequent three meetings in December 2023 and February and April 2024 to accommodate a session at the end of the 21 September meeting with the CIPFA Facilitator in relation to the Committee's sef-assessment.
- The withdrawal from the work programme of the item on the Local Code of Governance as it is only required to be considered once in an electoral cycle and was last considered by the Committee in December 2022.
- The withdrawal from the work programme of the Partnerships and Regeneration Scrutiny Committee Annual Report following consultation with the Scrutiny Manager as previously reported. Consequently, partnerships and collaborations as an area will be addressed as part of the Internal Audit Strategy for 2023/24.

It was resolved –

- **To accept the updated Forward Work Programme proposed for 2023/24 as meeting the Committee's responsibilities in accordance with its terms of reference.**
- **To note the changes to the dates on which reports will be submitted.**

Mr Dilwyn Evans
(Chair)