Minutes of the Audit Committee
23 March 2023

Present:

Councillor H. Harvey (Chairman)
Councillor J. Button (Vice-Chairman)

Councillors:

S. Buttar	K. Howkins	P. Briggs (Independent Member)
I.T.E. Harvey	L. E. Nichols	

Substitutions: Councillors C. Bateson (In place of T. Fidler)

Apologies: Councillor T. Fidler

In Attendance: Councillors M. Beecher

1/23 Apologies, Substitutes and Welcome

Apologies for absence were received from Councillor Fidler. Councillor Bateson attended in his place.

The Chair welcomed Philip Briggs, Independent Member, to his first Audit Committee meeting.

2/23 Minutes

The minutes of the meeting held on 24 November 2022 were approved as a correct record, subject to the addition of the text below in relation to the item on the forward plan:

“There was also discussion regarding concerns and risk to the authority from hybrid working and it was agreed that this be covered at the next committee meeting”.

3/23 Disclosures of Interest

There were none.

4/23 KPMG 2017/18 Audit Opinion

Joanne Lees and Philip Johnstone from KPMG, the Council's external auditors, attended for this item.

The Chair introduced this item noting the 5-year delay in receiving the final report from the Council's outgoing external auditors.

KPMG presented the final 2017/18 ISA 260 report which included the ISA 260 report, the auditor's opinion on the Statement of Accounts and Value for Money, the financial statements for 2017/18, and a management representation letter. A draft ISA 260 report for 2017/18 had been presented to this Committee in February 2019. The final ISA 260 report concluded an adverse Value for Money (VFM) opinion which was set out in the Auditor's 2022 Public Interest Report (PIR). The PIR had been presented to Council on 8 December 2022. The Committee noted that all of the follow up recommendations in Appendix 1 of the ISA report had been addressed.

Joanne Lees, for KPMG, explained that KPMG had completed the financial statements, issued an unqualified opinion on the financial statements, and provided commentary on each valuation risk. She restated KPMG's adverse opinion in relation to the Value for Money (VFM) opinion. The report included significant risks, recommendations raised and followed up, audit differences and the issuance of a Public Interest Report (PIR) which would be discussed in the item below.

Philip Johnstone, for KPMG, confirmed that the Public Interest Report had been issued to the Council on 12 October 2022, but not published until 30 November 2022 due to the death of a councillor and a subsequent by-election. The pre-election period had ended on 30 November 2022 and the PIR had been published on that date.

The Independent Member noted the important control recommendations in the report and asked if these would be carried forward by the new auditors. The Chief Finance Officer reported that they had been addressed and would be kept under review.

The Committee **resolved**

1. to accept the ISA 260 report from KPMG and to accept the opinions on the Statement of Accounts and Value for Money, and
2. that the Chair of the Audit Committee and Chief Finance Officer would sign the accounts and the letter of representation.

Councillors Bateson and Nichols voted against the resolution**.**

5/23 Public Interest Report Recommendations Follow Up

The Committee considered a Public Interest Report (PIR) Recommendations Follow Up report which was presented by the Chief Finance Officer. The PIR Recommendations Action Plan set out the Council's responses to the five recommendations made in KPMG's Public Interest Report. One of the recommendations was to develop an action plan to address weaknesses identified in the report.

The Chief Executive, the Monitoring Officer and the Chief Finance Officer addressed the Committee.

Statement from the Chief Executive Officer:
"At 8pm on the 12th October 2022, KPMG released their 2017/18 Public Interest report, concluding their Value for Money process. Despite being in close communication with KPMG for several months prior, the report literally came out of the blue without any prior indication of its intended release.

The very next day, on the 13th October, the KPMG Working Group, comprising of the Leader and the Deputy Leader, who are also the Chair and Vice-Chair of the Corporate Policy and Resource Committee, as well as the Chair and Vice-Chair of the Audit Committee supported by senior and statutory officers, met and assessed the legal practicability of complying with our statutory obligations in setting the necessary course of action.

Urgent communications with KPMG and the Secretary of State and DLUHC ensued immediately thereafter. As the timing coincided with the pre-election period for Spelthorne's most recent by-election and, as the Committee will know we had 4 of those last year, the report's release was delayed until immediately after the polls were closed on the 30th November.

The audit report presented to this Committee in the previous item, has thus taken our auditors 5 years to produce - though to be fair to KPMG, the best part of a year's delay can be directly attributed to the actions of one individual Spelthorne Councillor which is currently being investigated under the Members' Code of Conduct.

Audit congestion and lengthy tailbacks are endemic in the sector and now only 12% of local authority audits are currently being completed within the 6 months statutory deadline.

This is by far the lowest percentage on record since the introduction of the Local Audit and Accountability Act 2014 which saw the abolition of the Audit Commission and the transfer of all audit work to private sector companies.

In fact as recently as last week, the Director General, Local Government, Resilience and Communities at the Department for Levelling Up, Housing and Communities wrote to me and other Chief Executives to update us on the Department's continued work to respond to Sir Tony Redmond's *Local Authority Financial Reporting and external audit: independent review* (the

Redmond Review) and to reaffirm the Department's continued resolve to work with us and others across the sector to ensure a system wide approach to reducing the continued delays to local audits.

However, by any measure the release of our Audit Report, virtually half a decade after the audit year in question, in itself is a remarkably poor turnaround, posing significant concerns in both the 'timely value' of such audits and their associated 'cost value'.

The Public Sector Audit Appointments company believes that such delays in audit opinions have a real public-facing impact, undermining the ability of local authorities to account effectively for their stewardship of public money to taxpayers.

Notwithstanding the contextual factors, the Extraordinary Full Council Meeting was called to formally note and respond to the Public Interest Report with the ensuing Auditors' Recommendations fully accepted – hence the relevance of tonight's focus on the ensuing Action Plan. Thank you Chair."

Statement from the Monitoring Officer:
"Thank you Madam Chair, In dealing with the Public Interest Report, I consider that given the unfortunate circumstances that the Council had to administer a by-election in November 2022, the Council has met its statutory obligations under Schedule 7 of the Local Audit and Accountability Act 2014 in that:-

a) As soon as practicable, the PIR was published on the Council's website
b) As soon as practicable, a copy of the PIR was provided to each of the Council's Members
c) Ensured that any member of the public could inspect the report at all reasonable times without payment
d) A Council meeting was held on 8th December to consider the PIR and made a decision to accept the Recommendations of the Auditor.

As soon as the Council became aware that there would be a delay to publishing the PIR and corresponding notice, KPMG and DLHUC were consulted and they did not object to the timescales that we proposed.

Now turning to the report itself, you will note that it provides a conclusion based on legal opinion together with five recommendations.

I will briefly comment on the legal opinion.

The Auditors assert that the Council did not seek proper legal advice prior to borrowing and purchasing the properties. This is incorrect. The Council sought legal advice on 19th July 2016 and 21st March 2017 and on four further occasions, the latest being November 2022 all from James Goudie KC, a **leading** local government counsel and experienced head of chambers.

The Auditors also conclude that the Council firstly did not, in the circumstances, have the necessary legal powers to borrow and then purchase the properties; and
secondly even if it did have the power, it exercised the power unlawfully, by failing to “have regard” to relevant statutory guidance at the time.

James Goudie, the Council’s KC, is of the opinion that the Council **did possess** the necessary powers and **could rely** on the general power of competence conferred by the Localism Act 2011 as it was not trading or acting for a commercial purpose but was investing. **That does not entail the use of a company.**

The Auditors took issue with the 2017/18 purchases being outside of the borough stating that section 120 LGA 1972 could not be relied upon as the acquisitions were not directly “for the purposes of any of the local authority’s functions, any enactment, or for the benefit, improvement or development of their area”.

However that is not agreed by James Goudie, the Council’s KC, as he advises “there can be no greater benefit for an authority and its residents than an improvement in its general financial position and ability to fund services, at any rate if there is an identified and reasonably well-defined outcome in terms of benefit”.

In essence the authority’s KC strongly maintains his previous advice and is unpersuaded by the Auditors’ legal findings. Taking into account that the Council’s KC is one of UK’s top legal advisors in the arena of local government law, the Council I believe acted absolutely reasonably in accepting his advice as an accurate interpretation of the law, which has not been tested in any court, so far.

As the Council has accepted the Auditors’ recommendations it is now imperative for the Committee to consider that an Action Plan is put in place to set out how the Council seeks to comply with the Recommendations of the Auditor and move forward. Thank you. Thank you, Madam Chair.”

Statement from the Chief Finance Officer:
“Thank you Madam Chair, the Public Interest Report set out KPMG’s conclusions to their Value for Money opinion for 2017/18 and made 5 recommendations which the Council accepted at its Extraordinary Council Meeting on the 8th December 2022, as we have always been either applying the best practice suggested, or due to the time which has elapsed since KPMG published their report we have had in place for some while. Whilst we appreciate that external auditors have to be rightly careful to ensure that their work satisfies the Financial Reporting Council and that does slow down the audit process, it is very frustrating that KPMG have taken so long to reach their conclusions. In the last four and half years since the VFM Opinion was originally due the Council has ceased to acquire investment assets and its portfolio has weathered remarkably well the most extreme economic stress test in more than 300 years as a result of the economic impacts of the

Pandemic. Having said that we are of course always open to looking at how we improve the way we do things. So we will review the points made relating to recommendations, particularly recommendations 4 and 5 of the Auditors' Report. As Madam Chair has already commented, Coralie Holman, the new Group Head for Assets, only started in that role last week and we are suggesting that we allow time for her to bring a fresh perspective to reviewing our approach and that officers bring back a fully worked up Action Plan to the July Audit Committee.

Within the portfolio we do have some challenges with some churn of tenants but that is why we have been building up our sinking funds reserves balances by setting aside each year part of the income from the rental income, to ensure we have a safety net to cover dips in rental income. This enables us to manage those challenges without impacting on the Revenue Budget of the Council. As a result of a decision made by Corporate Policy and Resources Committee on Tuesday this week to approve a heads of terms for a new tenant we should be returning by June to having a floor area void across the Investment Assets Portfolio of less than 10%.

By the end of 2022/23 we anticipate that we will have approximately £36m in the sinking funds reserves. It is due to our sinking funds reserves that we have the highest ratio of revenue reserves to net revenue budget of any district or borough council in the country. This is on the basis of independent benchmarking by LG Improve. The Auditors' report does not make a single reference acknowledging our sinking funds approach as a key part of our risk mitigation strategy – an approach not all councils with investment assets have in place. The Auditors equally fail to acknowledge our prudent approach to Minimum Revenue Provision under which we are paying down our debt on an annual basis like a mortgage, again, in contrast to some councils. We have committed to do a full review this year over a 50-year time horizon of our sinking funds' portfolio, and this will be part of the Action Plan. Indeed, earlier today, myself and the Chief Accountant had a very constructive discussion with Coralie Holman, the new Group Head, in terms of how we will in practice take this forward.

As was stated at the Extraordinary Council Meeting on 8th December it is important that we move forwards to ensure that on an ongoing basis we meet the recommendations and that we undertake pulling together an Action Plan to address any improvement opportunities such as refining our Key Performance Indicators and, again, this is an issue we are already discussing with the new Group Head for Assets.

Dealing with the three recommendations with financial aspect:

Recommendation 3 - The Council should ensure that it has regard to all relevant statutory guidance, including specific aspects of that guidance that apply to particular decisions or transactions, and specifically record its reasons for departing from such guidance if it decides to do so.

We have agreed the recommendation. The Council has always had regard to all relevant statutory guidance seeking relevant expert advice and will continue to do so. It will in future more clearly record reasons for departure, not that we are anticipating any departures from statutory guidance. Note that moving forward the Council's Capital Programme and Capital Strategy are focused on ensuring that all capital spend is consistent with the revised terms of the Public Works Loan Board and the CIPFA Prudential and Treasury Management Codes. We run our Treasury Management and Investment Strategy reports past our professional advisers to ensure that they appropriately reference and comply with all statutory guidance. We will seek early discussions with our auditors if we have concerns about issues of interpretation with regard to accounting or statutory guidance, and a recent example of this being discussions officers had recently around risks of abortive capitalised costs. We will also be receptive to engaging with other sources of advice such as CIPFA, the LGA or DLUHC to seek external opinions and advice.

Recommendation 4: The Council should develop its investment property portfolio modelling to bring these in line with the expected practice of an institutional investor. This should include robust stress testing and sensitivity analysis which incorporates scenarios that cover the highest level of risk for expenditure, revenue, tenant behaviour and external socio-economic factors. Consideration should also be given to the diversification of the portfolio and whether this should be addressed over the medium to longer term.

Again, the Council agreed the recommendation. The Council since the commencement of the Covid-19 Pandemic in March 2020, and the national lockdown three years ago, has been refreshing and reviewing on a regular basis scenario modelling on a worst case and expected case basis to assess the adequacy of its sinking funds reserves.

The Council sought to invest within the Borough and close to the Borough within the Heathrow Functional Economic Area which it understands well, and which drives the prosperity of the Borough. This was the rationale for the geographic concentration of the portfolio. Whilst the Council is managing a small number of investment assets it does have a considerable number of tenants who are operating across a wide range of economic sectors and this is monitored in the regular investment reports. There is in this respect considerable diversification by tenant sector.

The Council is already undertaking a review of its Sinking Fund Strategy over the next 50 years and looking to bring in external advice to review assumptions about future income levels, rental activity and to make recommendations around levels of sinking funds contribution to reserves to ensure that we have a sufficient level of reserves to cover any dips in income and to cover all financing and management costs. The modelling will include stress testing, we will ensure parameters and assumptions tested are clear and transparent. And, again, the Chief Accountant and I have been having some very constructive discussions with the Group Head for Assets who had some very useful ideas in terms of how we can move forward with some aspects of this particular recommendation.

Recommendation 5: The Council should develop an action plan as part of the management of its investment portfolio which addresses each of the weaknesses identified in paragraph 6.9 of the PIR report. This should be linked to a portfolio risk register, which monitors each of the KPIs, tenant performance and risk to the debt repayment strategy for each investment property asset.

Whilst we believe we undertake actions which address the risks set out in 6.9 of the report, we will, linked to the sinking funds reserves review, undertake an action plan to identify the scope for any improvements which address the points made in the report. Relevant points to notes with respect to the issues in 6.9 are as follows:

- The investment assets portfolio is constrained geographically by a desire to be focused within our local Heathrow Functional Economic Area (an area which the Council has a good understanding of, and which helps drives the economic prosperity of the Borough), however the tenants by sector are relatively diversified.
- The sinking fund review strategy will look at 50-year time horizon, including a) short term 5-year perspective, b) medium term 5 to 30 years perspective and c) 30 years plus perspective. Since 2019 the Council has diversified its overall portfolio by its regeneration acquisitions, with regular reporting against KPIs of the overall portfolio and of individual tenants, along with maintaining five yearly business plans plus five yearly refreshing of the sinking fund reserves modelling.
- We already undertake regular worst case and expected case sensitivity analysis on a rolling 10 year basis.
- The Assets team has increased significantly in size since 2017/18 with the addition of a number of skilled assets professionals with private sector experience of managing portfolios of office and retail assets. A testament to the skills of the team and their proactive approach to managing the portfolio and engaging with tenants are the investment asset rental collection percentages of 100% and 99.98% for rental invoiced for the years 2020/21 and 2021/22. We have not quite finished the current year so we do not yet have a figure for 2022/23. We have just welcomed a new very experienced Group Head for Assets to the team.
- The sinking funds reserves balances have continued to be built up (anticipated to be £36m at end of 2022/23) in order to mitigate against repayment risk. However we do highlight, as was reported annually in the budget report to Council in February, that in line for the purpose for which we set aside the sinking fund reserves there will be some anticipated draw down of those sinking fund reserves over the next two financial years. Thank you very much."

Members noted that all of the recommendations in the PIR had been accepted by the Council.

Clarification was sought as to the reason for the delay in issuing the PIR Report. The Monitoring Officer confirmed that a by-election was a legal reason for the delay in issuing the report. The Committee noted that the Council had received legal advice in relation to its purchases.

The action plan would be put on the forward plan for the Development Sub Committee as well as the Audit Committee and would be used to drive improved risk management. It would focus on all of the recommendations with particular emphasis on Recommendation 5.

The Committee **resolved**

1. to note and agree the Public Interest Report Recommendations Follow up, and
2. to agree that a PIR Action Plan be brought before the July meeting of the Audit Committee and therefore be added to the Committee's Forward Plan.

6/23 Report on DLUHC's Review of Councils with High Debt Levels

A question was received from a member of the public in relation to this agenda item.

Question from Ms Kath Sanders:
"Please could the report to the committee lay out the terms of reference for the DLUHC's capital review of Spelthorne Borough Council's position and when does the Council expect to receive any interim and final report?"

Response from the Chair:
"Spelthorne Borough Council like other authorities are being externally and independently reviewed by DLUHC. We are therefore not privy to the terms of reference or have any expectations to receive the final report within any given period as we are not the commissioning authority."

The Chief Finance Officer gave a verbal update on the Department for Levelling Up, Housing and Communities' (DLUHC) Review of Councils with High Debt Levels. The Chartered Institute of Public Finance and Accountancy (CIPFA) was conducting the review on behalf of DLUHC. The Council hoped to have a draft report by the time of the next Committee meeting.

The Committee **resolved**

1. to receive and note the verbal update on DLUHC's Review of Councils with High Debt Levels, and
2. to place the DLUHC Review on the Forward Plan for the Committee's meeting in July.

7/23 Corporate Risk Management

As part of Risk Category 7 “Corporate Capacity, Resources, Recruitment and Retention” members discussed the impact of the Council’s hybrid working policy, focussing particularly on the risks involved. The Group Head Commissioning and Transformation presented a report on hybrid working which set out many of its benefits and associated challenges (risks). She stressed that the mixture of office and remote working was always in line with business need and that most staff were expected to work in the office two days a week. Those who wanted to work in the office full time were able to do so. Working from home had become the norm during the Covid-19 pandemic, particularly for public sector workers. This had become an expected benefit for staff and assisted with recruitment. From an environmental perspective, working from home reduced the Council’s carbon footprint. Members noted that public facing services were still provided to residents by office-based staff and that not all employees had the option of working from home.

Members gave their own examples and experiences of hybrid working, some good, others less so.

The efficiency and effectiveness of hybrid working was due to be considered as part of the forthcoming Corporate Establishment Review requested by the Corporate Policy and Resources Committee.

The Committee agreed that Risk Category 7 of the Corporate Risk Register be widened to incorporate hybrid and flexible working.

The Committee took a break between 9.30pm and 9.43pm.

It was proposed by Councillor I Harvey and seconded by Councillor Bateson that standing orders be suspended in order to continue the meeting until 10.30pm. This was agreed by the Committee.

The Internal Audit Manager presented a report on Corporate Risk Management. This included an updated Corporate Risk Register (CRR), with red-amber-green (RAG) colour coding at the top of each risk category and blue highlighting within the report to show the risks which were significantly impacted by wider externalities, and a colour coded Risk Action Plan. Risks had been assessed taking into account current controls and mitigations, in line with good practice.

The Internal Audit Manager highlighted external risk areas over which the Council had limited scope for risk mitigation; these included the current economic crisis and macroeconomic environment, such as inflationary pressures, increased rates of borrowing, and the continued cost-of-living crisis. She noted an indicative risk score moving in a favourable direction if all risk actions in the Risk Action Plan were completed. Continued visibility and recognition of all strategic risks in the Corporate Risk Register was important.

The Internal Audit Manager introduced three new actions in the Risk Action Plan; developing a long term relationship management in relation to existing tenants, any forthcoming recommendations from CIPFA and DLUHC reports in relation to capital risk mitigation, and the medium-term financial strategy and efficiency savings plan for addressing the budget deficit.

The Committee had an initial discussion of risk management software and whether it should be used by the Internal Audit team to support presentation of the Corporate Risk Register which has continued to evolve . The possibility of using an in-house system was mooted. The Independent Member recommended seeking advice from other local authorities who already used such systems. The importance of risk ownership was also discussed as it is important that risk management processes and reporting continue to embed this principle.

The Committee **resolved**

1. to note the significant strategic risks and issues highlighted in the report, subject to the changes discussed, and
2. to recommend that the Corporate Risk Register and Risk Action Plan be presented to the Corporate Policy and Resources Committee, and
3. to note the discussion in relation to hybrid working and to add hybrid and flexible working to risk category 7 of the Corporate Risk Register.

8/23 The Council's Risk Exposure to Wider Externalities and Impact

The Internal Audit Manager presented a report to the Committee on the impact of wider externalities to the Council, its operations, and local communities as well as a wider externalities and impact risk assessment.

The Internal Audit Manager drew attention to the two major externalities presenting significant impact; the macro-economic environment (which was referred to earlier in the meeting) and the current geo-political uncertainty (war in Ukraine). These wider externalities had a particular impact on three broad risk categories: economic activity and prosperity, the Council’s financial position in relation to sustainability and resilience, and housing and communities. The refreshed risk assessment noted no movement from the previous review in November 2022 and no changes to report in terms of RAG ratings or positioning of risks on the risk matrix.

The context for the report was interest rates increases, little or no growth in the economy, rising unemployment, long term uncertainty regarding the macro-economic environment, with the cost-of-living crisis continuing to present increased demand on Council services. Members noted local control measures and mitigating actions to alleviate pressures and further actions are set out in the last column of the risk matrix.

The Committee discussed reducing the overlap between this report and the Corporate Risk Management Report. The Committee agreed to combine the two reports and to restructure some of the reporting in the Corporate Risk Register.

The Committee **resolved**

1. to note the report, and
2. to note the close linkages and common themes between this report and the Corporate Risk Management Report referred to earlier in the meeting, and
3. to agree to combine this report and the corporate risk register, and
4. to update the forward plan to reflect the changes agreed.

9/23 Internal Audit Annual Plan 2023/24

The Internal Audit Manager outlined the proposed Internal Audit Plan for 2023/24 which demonstrated how the Council would fulfil its statutory and professional requirements and provide independent assurance to the Council on the adequacy of internal control, governance, and risk management arrangements.

The Plan included several higher risk areas that aligned with the council's corporate priorities and objectives, and these had been prioritised "A" or "B" according to risk. The wider externalities referred to earlier in the meeting would cut across the workstreams in the Internal Audit Plan. Members noted the summary of work and that it included reactive and unforeseen work.

Members noted the likely Internal Audit interaction with the incoming external auditors and that it was intended to commission external resource for some audits on the internal audit work programme. Funding for these would come from the audit contractor budget.

The Committee **resolved** to note and approve the Internal Audit Plan for 2023/24.

10/23 Counter Fraud, Bribery & Corruption Strategy

The Internal Audit Manager presented a report on the Council's Counter Fraud, Bribery and Corruption Strategy and outlined proposed changes to the Strategy so that it remained relevant and current. The Strategy was last reviewed by the Audit Committee in July 2021. A tracked changed document and a final version of the Strategy were attached to the report which set out the reasons for the proposed changes.

The Committee noted that during economically challenging times fraud and corruption occurrences were perceived to be on the increase. An open and honest culture, adequate preventive measures, collaborative arrangements and practices, systems for detection and investigation and an understanding and awareness of fraud, bribery and corruption, and whistleblowing procedures were all key elements of the Council's strategy to prevent, detect and manage fraud.

The Strategy formed part of the Council's constitution, was in line with best practice, and underpinned the Council's commitment to dealing effectively with all forms of bribery, fraud, and corruption. The Committee was required to review the Counter Fraud Bribery and Corruption Strategy annually and make any recommendations for change to the Corporate Policy and Resources Committee. Counter fraud measures, in particular, had been increased and these were set out in the revised Strategy.

The Committee **resolved**

1. to endorse the Council's Counter Fraud, Bribery and Corruption Strategy, and
2. to approve the recommended changes to the Strategy and to submit these to the Corporate Policy and Resources Committee.

11/23 Introduction of New Audit Assurance Opinions

This item was deferred until the next meeting.

12/23 Committee Forward Plan

The Committee considered its forward plan for the forthcoming municipal year.

The Committee **resolved** to approve the forward plan for the forthcoming municipal year, with the addition of the following items:

- A Public Interest Report Action Plan
- DLUHC Draft Report
- To incorporate the Council's risk exposure to wider externalities and impact report into the Corporate Risk Register
- Spelthorne Direct Services (SDS) and Knowle Green Estates (KGE) Accounts for March 2022 and March 2023.