

Corporate Policy & Resources Committee



15 April 2024

Title	<i>To note the audited financial statements for Knowle Green Estates (KGE) for the year end 31 March 2023</i>
Purpose of the report	To note
Report Author	<i>Paul Taylor Chief Accountant</i>
Ward(s) Affected	All Wards
Exempt	No
Corporate Priority	Community Addressing Housing Need Resilience Environment Services
Recommendations	Committee is asked to note the report and in particular the unqualified audit report.
Reason for Recommendation	<p>The Board of Directors of Knowle Green Estates Ltd approved the accounts for the year ended 31 March 2023 on 18 October 2023 following a meeting with the External Auditors.</p> <p>The Auditors provided an unqualified audit report and the accounts have been filed at Companies House and with His Majesty's Revenue & Customs (HMRC), where there is no Corporation Tax to pay.</p>

1. Summary of the report

What is the situation	Why we want to do something
<ul style="list-style-type: none"> This Committee is responsible for the oversight over Knowle Green Estates (KGE). Every year the accounts of KGE are subject to an independent audit and this report looks back over the trading year ended 31 March 2023. 	<ul style="list-style-type: none"> As part of good governance, this Committee manages the relationship with KGE on behalf of Council. The KGE Board have discharged their duties and obtained an unqualified audit report for the year end 31 March 2023.

<ul style="list-style-type: none"> Note that the external auditors gave an unqualified audit opinion for the year end 31 March 2023. Whilst the company is trading at a loss, at the extraordinary Council meeting on 3 February 2023, council agreed to extend up to five years of financial support to KGE, whilst the Council suspends its direct housing delivery projects and seeks joint venture partners to complete the projects and deliver the much needed housing to the residents of the borough. 	
<p>This is what we want to do about it</p>	<p>These are the next steps</p>
<ul style="list-style-type: none"> To review the report and its appendices. Question managers and the Directors about the results contained in the financial statements, the comments in the management letter and the Directors response in the Letter of Representation, noting that this was a straightforward audit assignment. Focus on the figures for 2022-23, as the previous year has been noted by the Committee. 	<ul style="list-style-type: none"> That the Committee note the report.

2. Summary of the report

2.1 The unqualified audited accounts for the year ended 31 March 2023 were approved by the Knowle Green Estates (KGE) Board on 18 October 2023 and filed at Companies House and there was no Corporation Tax to pay.

2.2 A summary of the profit and loss account on page 6 of Appendix A is shown below, noting that under Company Law, losses are shown as a negative figure and profits are shown as a positive figure, which is the reverse situation when reporting under the Chartered Institute of Public Finance Accountancy Code for Local Authorities:

	2022-23	2021-22
Profit/(loss) for the year	(£896,857)	£144,334

Total Comprehensive Income/(Expenditure) for the year	£1,232,724	£3,464,975
Total equity	£4,411,839	£3,179,115

- 2.3 The main reasons for the loss being incurred was due to:
- (a) An increase of (£499k) in the depreciation charge, as Benwell 1 and West Wing are now fully operational.
 - (b) An increase of (£700k) in loan interest charges following the transfer of the West Wing in the summer of 2022 and the delay in getting the tenants in to the property in December 2022.
 - (c) A repayment of (£163k) to HMRC in respect of VAT.
 - (d) Offset by an increase in rental income of £350k.
- 2.4 The main reason for the improvement in total equity performance from 2021/21 to 2022/23 is due to the improvement to the property valuations, based on full occupancy and strong rental streams from private renters and affordable housing.
- 2.5 The positive movement is reflected in the revaluation reserve, noting that this reserve is an unusable reserve, as defined by the CIPFA Prudential Code.
- 2.6 The above is in line with the financial information communicated to Council in respect of KGE.

3. Key issues

- 3.1 Following a meeting with Tracey Wickens, the Senior Statutory Auditor at MGI-Midgely Snelling, the KGE Board of Directors formally accepted and signed the accounts (Appendix A) on 18 October 2023.
- 3.2 Also attached is the Management Letter from the Auditor, See Appendix B, which states that:
- (a) There was no change in the audit process.
 - (b) There were no significant findings coming from the audit.
 - (c) Some commentary on internal controls:
 - i) There are still some challenges with Bluebox (a Tenancy based application) when producing final accounts, as there has been little development work carried out by the Assets team to develop the software to deliver a recognisable trial balance from the system, making it a labour intensive process, and delaying the production of the audited accounts a consolidated Council accounts.

This is still being addressed by the Board of Directors.
 - ii) The two sums referred to come from the previous year, which was audited by Azets, and therefore, there should have been sufficient information in the audit files to deal with matter.

Officers subsequently review the journals from the previous auditors and ascertained that figures were as follows:

- 3.3 £10,793 – this was written off in year end 2021, by agreement with the auditors and the Board.
- 3.4 £4,134 – this was deferred income from 2021 and should be written to the profit and loss account.

However, these have not been reflected in the trial balance and the Chief Accountant is dealing with this matter in February.

Please note that both adjustments are favourable and under the company's materiality levels and will be adjusted accordingly going forward.

- 3.5 The auditors also provided confirmation:
- (a) of an anticipated clean audit report being issued, subject to final checks and submissions.
 - (b) that the auditors agree with the Directors views on:
 - i) Going concern
 - ii) Accounting policies and disclosures
 - (c) that there were no related party issues.
 - (d) that all third-party confirmations were received.
 - (e) of MGI-Midgley Snellings independence.
- 3.6 As part of the normal audit process, the Directors discussed, reviewed and signed the Letter of Representation, (Appendix C).
- 3.7 This letter sets out key affirmations that the Directors have made during the audit process and is a standard request from external auditors.
- 3.8 Where adjustments are material, the Board requested that the financial statements were amended to reflect these adjustments, As a result of these adjustments the Spelthorne Borough Council Group accounts will need to be updated to reflect these favourable adjustments.

4. Financial implications

- 4.1 There are no further financial implications in respect of the financial accounts.

5. Risk considerations

- 5.1 The property valuations are based on a variety of data, and does not reflect the best valuation, i.e., an offer to buy the premises or company, which could be higher or lower than the asset carrying value included in the audited financial accounts for the year ended 31 March 2022.
- 5.2 The Bluebox financial system, is not widely recognised within the finance profession and it has been difficult for the Finance Team to support the Assets Team to deliver timely year end accounts, management accounts and budgets. Officers are in discussion to look at moving the accounts production to Centros, where greater resilience and support can be provided.
- 5.3 Delays to the Development Projects has put financial pressure on KGE, and at the Extraordinary Council Meeting it requested a refinancing package, including the purchase of equity shares, to match the potential Homes England Funding and reduce the Loan to Property Value to 50%, as current PWLB interest rates are circa 5% and expected to rise further in mid-June, when the Bank of England meet to review the Base Rate.

- 5.4 The original projections approved by the KGE Board in June 2021, where prepared on the assumptions that Thameside House and Victory Place would be occupied from January 2024 and November 2023 respectively, as neither development has commenced yet, this is putting pressure on KGE, not only from a cashflow perspective, but also in its ability to establish a truly independent Board, as it is unable to generate the cashflow to support this additional expenditure.
- 5.5 Since the change of Council policy on 22 March 2022 – Transferring property to KGE at cost - this has ensured that there is no chance of a loss materialising upon transfer to KGE, in the Council's accounts.
- 5.6 To reduce the financial risk on KGE being unable to afford to manage any of the Council's development properties, since the last property was transferred in December 2021, viability assessment are now carried out on each development, which will include modelling over a 50 year period different scenarios, such as, changes in interest rates, loan term, rent increases and capital cost.

6. Options analysis and proposal

- 6.1 Not applicable

7. Financial management comments

- 7.1 As per section 2 and 3 above.

8. Procurement comments

- 8.1 There are no Procurement implications in this report

9. Legal comments

- 9.1 It is a requirement under section 441 of the Companies Act 2006 for accounts to be filed every year at Companies House.
- 9.2 As the sole shareholder of SDS, the Council should have sufficient oversight of the company's activities. This report assists with providing financial oversight and gives assurance that KGE is financially sound, with the continued support of the Council.

10. Other considerations

- 10.1 Detail any other considerations to be taken into account.

11. Equality and Diversity

- 11.1 Detail how the recommended proposals will impact equality and diversity and mitigation measures being taken.

12. Sustainability/Climate Change Implications

- 12.1 Detail how the proposal will support/impact sustainability/climate change issues.

13. Timetable for implementation

- 13.1 Set out a timetable, if required, showing when the proposal in the report will be implemented.

14. Contact

- 14.1 p.taylor@spelthorne.gov.uk

Background papers: There are none.

Appendices:

Appendix A – Signed Audited Accounts for Knowle Green Estates for the year end 31 March 2023.

Appendix B – Management Letter

Appendix C – Letter of Representation