

## **NORTHUMBERLAND COUNTY COUNCIL**

### **AUDIT COMMITTEE**

At a meeting of the **Audit Committee** held at County Hall, Morpeth on 24 July 2019 at 10.15 a.m.

### **PRESENT**

Councillor G Hill (Chair)

### **COUNCILLORS**

G Castle  
L Grimshaw  
M Swinburn

ICF Swithenbank  
D Towns

### **CO-OPTED MEMBERS**

A Hall

AN Haywood-Smith

### **ALSO PRESENT**

Councillor N Oliver

Portfolio Holder for Corporate  
Services and Cabinet Secretary

### **OFFICERS IN ATTENDANCE**

A Bridges  
A Elsdon  
A Lister  
A Mason  
K McDonald  
B McKie  
A Mitchell  
A Stewart  
N Turnbull

Head of Communications  
Service Director - Finance  
Principal Accountant (Pensions)  
Finance Manager  
Group Assurance Manager  
Group Assurance Manager  
Chief Internal Auditor  
Finance Manager  
Democratic Services Officer

### **Also present:**

Ms C Mellons and Mr S Reid of Ernst & Young (External Auditors)

1 member of the press

### **8. APOLOGIES FOR ABSENCE**

Ch.'s Initials.....

Apologies for absence were received from Councillors LJ Rickerby and M Purvis.

## **9. MINUTES**

### Minute No 28/2018-19

The Chair reported that, following the discussion at a previous meeting, a public interest assessment had been carried out by the Chief Internal Auditor and Chief Executive on the letter signed by 5 Directors of Arch regarding a consultant's remuneration. They had agreed that the letter could be considered in the public domain and a copy was circulated to the members of the committee at the meeting.

**RESOLVED** that the minutes of the meeting of the Audit Committee held on Wednesday 22 May 2019, as circulated, be confirmed as a true record and signed by the Chair.

## **10. REPORTS OF THE EXTERNAL AUDITOR**

### **(a) ISA260 Annual Accounts**

A copy of the External Auditor's Audit Results Report for the year ended 31 March 2019 was circulated at the commencement of the meeting. (A copy of the report is filed with the signed minutes as Appendix A.)

Mr S Reid, External Auditor EY, stated that whilst they had substantially completed their standard audit work on the financial statements of the Council for the year ended 31 March 2019, on 25 June 2019 they had notified management that they had received correspondence which they were obliged to investigate under EY's whistleblowing procedures. Allegations related to senior management and others that had a significant role in internal control which may impact on the financial statements and / or their value for money opinions. They hoped to commence work in the next few days but would be unable to issue their opinions by the accounts publishing date of 31 July 2019.

He highlighted the following issues:

- An increase in materiality (the threshold for reporting misstatements had increased to £890,000)
- Areas of work which EY still had outstanding.
- Control observations included consideration of a system-based approach to managing the asset base and reimplementation of the monthly control account reconciliations which had been unavailable following upgrades to the general ledger in November 2018.
- Areas of audit focus - risk of fraud in revenue and expenditure recognition, misstatements due to fraud or error, valuation of land and buildings. With regard to the latter, an adjustment was to be made by Management

regarding an understatement of £7 million on the valuation of other land and buildings. Also, the valuation of land at East Sleekburn of £13.4 million was confirmed to be within an acceptable range. (A range was used when considering valuations due to the availability of different methodologies and reliance on judgement).

- Impact on the pension disclosures which had been restated by the actuary following the decision by the Court of Appeal not to grant the Government leave to appeal against the McCloud judgement (an age discrimination case). Allowance for the constructive obligation on the Council as a result of the McCloud judgement and future indexation of GMPs resulted in an increased pension liability in the financial statements of £25.9 million.
- A review of the valuation of the shares in Newcastle International Airport Ltd (NIAL), commissioned following the introduction of IFRS 9, had after audit resulted in an adjustment of £6.4 million to the draft accounts and a £0.1 million surplus overall rather than a deficit as originally notified to the Council and included in the draft accounts.

The Chair sought reassurance regarding the investigation of the whistleblowing correspondence and clarification of the independence of officers involved in the instigation of the investigation. She also sought reassurance in relation to the assessment of this as a whistleblowing complaint.

Mr Reid commented that although the letter had been received on 17 March 2019, they had been unable to raise the issue at the meeting of the Audit Committee on 27 March 2019 as their assessment against EY criteria had not been concluded at that time. As External Auditor they received numerous letters all of which had to be assessed although many did not proceed to a more detailed investigation. He also confirmed that the assessment and investigation was undertaken by himself and other senior officers within EY.

Mr Reid stated that he was a member of a professional institute with ethical standards and had statutory responsibilities which overrode any fee driven motivation. He referred to the quality assurance arrangements and involvement of forensic and professional colleagues who would be involved in the investigation.

It was not possible for a timescale for the work to be given at this stage and brief explanation of the process to be followed was provided which included a review of information provided by management before discussions with individual officers. At any point this could lead to further questions. He hoped that, given the time of year and holiday period, the matter would be concluded before the end of August and reported to an additional meeting of the committee, or if not concluded soon enough, reported to the next scheduled meeting on 25 September 2019.

In response to questions the following information was provided:

- The External Auditors were unaware of any further legal rulings which had reached a stage where they would impact on pension liabilities or be disclosed in the financial statements. The level of LGPS employer contributions from April 2020 would be determined at the triennial valuation of the Pension Fund.
- All of Local Authority shareholders of NIAL had been affected by the valuation commissioned by the lead authority. There were 2 External Auditors who were now comfortable with the revised valuation. There had been no discussions or plans to sell the shares in the airport which was an important asset in the region.

Councillor Oliver, Portfolio Holder for Corporate Services, commented on the following matters:

- Whilst the Administration had been dismayed in the delay from March to June before being notified of the whistleblowing allegations, it was understood that the External Auditors had requested more information from the whistleblower before the allegation could be thoroughly assessed and the Council informed. The issues had been raised and investigated before and information supplied as part of previous audits. It was hoped that the matter would now be dealt with quickly and the matter concluded.
- A formal piece of work was to be undertaken to assess the systems available on the market to replace the fixed asset spreadsheet currently being used.
- They were confident that governance was in place with a separation of duties for Advance Northumberland with the implementation of a Loans Board to ensure application of correct procedures.
- Assets had been transferred from Arch to Advance Northumberland to ensure that reputational issues had been resolved and the credibility of the new organisation.

Several Members expressed their concerns regarding views being formed whilst the whistleblowing process was followed and the investigation concluded. It was recommended that there should be no further discussion or speculation on the matter at this stage.

**RESOLVED** that the draft report be received and the information noted.

#### **(b) ISA260 Pension Fund Accounts**

A copy of the External Auditor's Pension Fund Audit Results Report for the year ended 31 March 2019 was circulated at the commencement of the meeting. (A copy of the report is filed with the signed minutes as Appendix B.)

Ms C Mellons, External Auditor EY, introduced the report and confirmed that, whilst the audit of the Fund was substantially complete, they would be unable to issue their opinion on the Pension Fund due to the ongoing investigation and inability to issue an opinion on the accounts of Northumberland County Council as administering authority by the publication deadline of 31 July 2019.

Ms Mellons reported that:

- Materiality had been updated however the threshold for reporting misstatements remained at £250,000 as requested by the Pension Fund Panel.
- They were seeking clarification from the actuary regarding the estimated value of assets to be transferred to Tyne and Wear Pension Fund following the merger of Northumberland College with Sunderland College. However, it was not anticipated any changes would be required.
- Two audit differences had arisen as a result of more up to date investment valuations being received after the preparation of the accounts. Management had chosen not to adjust as it was not believed to be material to the financial statements. This was a timing issue which occurred every year and was not of concern.
- Control observations related to the upgrade of the Oracle General Ledger and difficulties accessing reports which had impacted on regular account reconciliations.
- Areas of audit focus included misstatements due to fraud or error. This area may need to be reviewed following the conclusion of the whistleblowing investigation although revenue and expenditure for the Pension Fund was more stable in terms of regular monthly payments.
- The implementation of IFRS 9 and 15 had not had a significant impact on the financial statements of the Pension Fund. EY was satisfied that the classification and measurement of financial instruments was appropriate with the few minor updates to disclosures made.

**RESOLVED** that the draft report be received and the information noted.

## **11. REPORTS OF THE EXECUTIVE DIRECTOR OF FINANCE (SECTION 151 OFFICER)**

### **(a) Statement of Accounts 2018-19 (including Annual Governance Statement)**

Mrs A Elsdon, Service Director - Finance introduced the report which presented the Statement of Accounts for the year ended 31 March 2019 to Members of the Audit Committee. (A copy of the report is filed with the signed minutes as Appendix C.)

The Service Director - Finance responded to the issues raised by the External Auditor in the earlier item with the following comments:

- Additional changes to the figures in the statement of accounts had been circulated at the meeting.
- Options were being investigated to replace the fixed asset working papers and interest had been expressed in a particular system, although further research was required. A replacement system was unlikely to be in place before 2020/21.

- Monthly reconciliations were now being undertaken.
- The differences in the valuation of land and buildings would be taken up with the organisation that had undertaken the original appraisals.
- The draft statement of accounts had been prepared without knowledge of the whistleblowing allegations. They had been available for inspection by members of the public between 3 June 2019 and 12 July 2019, although no requests to inspect the statements had been received.
- Drop in sessions had been held to answer questions from members of the Audit Committee.
- There had been a deficit on the provision of services of £52 million and total comprehensive income and expenditure of £10.621 million. Cabinet had considered the provisional outturn position for both Revenue and Capital at its meeting in May 2019. It had been agreed that the 2018/19 underspend on the General Fund be transferred to create a Transformation Fund Reserve. The provisional figure of £8.095 had now been revised to £8.18 million.
- The revised valuation of NIAL had resulted in changes throughout the balance sheet as had the McCloud judgement and increase in pension liability.

The Committee were requested to note the changes to the draft Statement of Accounts as they were now unable to approve them due to the whistleblowing investigation.

The following information was provided in response to questions from members:

- Investment property was held by Advance Northumberland.
- Ascent Homes was a subsidiary of Advance Northumberland. Members were advised to obtain advice from legal regarding any possible conflict of interest.
- The closing value of property, plant and equipment for Advance Northumberland had reduced to £9.135 million following purchase, sale, reclassifications and depreciation of assets during the year.
- The statement of accounts would likely have been approved by the publication deadline of 31 July 2019 if the whistleblowing allegation had not required investigation.
- The Council were not land banking, however, they would not agree to the disposal of an asset if a low offer was received and it did not represent a fair value as the Council had a duty to obtain the best value. Sites were only acquired if there were development opportunities to create jobs and not purchased to prevent them being developed by competitors. There were rules of procedure which had to be followed to ensure transparency but unfortunately sometimes this resulted in delays whilst the proper process was followed. Consideration had recently been given to move from a 2 to 5 year strategy.
- Any member with a query regarding a specific parcel of land was invited to contact the Portfolio Holder after the meeting.

- The relationship with Active Northumberland was reviewed every year by Internal Audit and the report had been accepted by External Audit.
- Clarification would be provided to Members regarding the settlement of a dilapidation claim by a landowner regarding a long-term lease previously held by the Council. The property had now reverted back to the landowner with a lump sum final payment to settle the claim.

**RESOLVED** that:

- (i) The changes made to the draft Statement of Accounts in Appendices A and B and the additional document circulated at the meeting, be noted.
- (ii) Approval of the Statement of Accounts for the financial year ended 31 March 2019, be deferred.

**(b) Pension Fund Annual Report and Accounts 2018-19**

The report provided the Audit Committee with an overview of the key issues relating to the Northumberland County Council Pension Fund draft Annual Report and Accounts for the year to 31 March 2019 to assist Members in carrying out their role in reviewing the Financial Statements. (A copy of the report is filed with the signed minutes as Appendix D.)

The Principal Accountant (Pensions) commented that the NCC Pension Fund Accounts needed to be consistent with the NCC Statement of Accounts, and therefore would also be deferred due to the whistleblowing allegation discussed earlier in the meeting. Points to note included:

- The draft Annual Report and Accounts had been considered by both the NCC Pension Fund Panel and NCC LGPS Local Pension Board at meetings on 21 June 2019 and 12 July 2019, respectively.
- There had been a net withdrawal from dealings with members in 2018/2019 of £30 million, where payment of pensions had exceeded contributions from active members. This included the estimated £26 million asset transfer to Tyne and Wear Pension Fund in relation to Northumberland College, which had exited NCC Pension Fund on 22 March 2019.
- An increase in Fund value from £1.344 billion to £1.4 billion over the period reflecting a 6.9% returns on investments.
- Changes to the Draft Pension Fund Annual Report and Accounts were itemised in paragraph 6 of the report and a small number of changes had been made following discussions with the External Auditor.

**RESOLVED** that:

- (i) Approval of the Pension Fund Annual Report and Accounts 2018-19, be deferred;

- (ii) The Annual Report of the Local Government Pension Scheme Local Pension Board for 2018-19 (Annex 1), be noted;
- (iii) The Minutes of the five meetings of the Board held during the 2018-19 financial year, dated 17 April 2018, 17 July 2018, 26 July 2018, 8 November 2018 and 25 March 2019 (Annex 2), be noted;
- (iv) The Annual Report of the Firefighters' Pension Scheme Local Pension Board for 2018-19 (Annex 3), be noted;
- (v) The Minutes of the two meetings of the Board held during the 2018-19 Council year, dated 23 October 2018 and 16 April 2019 (Annex 4), be noted.

**(c) Treasury Management Annual Report for the Financial Year 2018-19**

Mr A Stewart, Finance Manager introduced the report which provided Members with details of performance against the Treasury Management Strategy Statement (TMSS) 2018-19, approved by the County Council on 21 February 2018. (A copy of the report is filed with the signed minutes as Appendix E.)

He highlighted that all Treasury Management activities for the year had been conducted within the parameters of the Treasury Management Strategy Statement 2018-19, and best practice suggested by CIPFA's Treasury Management Code.

He referred to a number of changes during the year which included:

- A reduction in borrowing of £40 million and therefore interest paid.
- There had been 2 LOBO loans repaid in year totalling £33 million. This had saved the Council approximately £7 million over the lifetime of these facilities.
- The weighted average interest payable for the year at 2.97% compared favourably to the London Inter Bank Rate. However, the CIPFA benchmarking data was not available but will be reported to members later in the year.
- Actual interest payable for the year was under budget by £2.0 million. This was as a result of overall borrowing being lower than originally budgeted and the overall average weighted interest payable was lower than forecast.
- There had been a reduction in external investments of over £54 million and an increasing use of 'internal investments to support the financing of the Capital Financing Requirement.
- The weighted average return on interest receivable for the year, at 1.39%, compared favourably to the London Inter Bank Rate, and income from core treasury management investments exceeded the budget by £0.49 million due to higher than budgeted investment balances.



- Benchmarking data was compared at 31 March 2019 (correction of typographical error in the last paragraph of section 6.2 on page 12 of the report).
- None treasury management investments, such as loans to third party organisations were lower than budgeted which had resulted in lower returns of £1.9 million .
- The Prudential Indicators and Treasury Management Limits set for 2018-19 had been adhered to.

**RESOLVED** that

- (i) The report be received and the performance of the Treasury Management function for 2018-19, be noted.
- (ii) The report be recommended to County Council.

**(d) Key Questions for the Audit Committee**

Members of the Audit Committee received a report containing responses to the “Key questions for the Audit Committee” which were posed by the Council’s external auditors at the previous meeting of the Audit Committee. (A copy of which is filed with the signed minutes as Appendix F.)

The Service Director - Finance agreed to obtain further information on why the NAO’s financial stability visualisation tool was not utilised by the Council.

**RESOLVED** that the contents of the report be noted.

## **12. REPORT OF THE CHIEF INTERNAL AUDITOR**

### **Risk Management Presentation**

Ms B McKie, Group Assurance Manager, gave a powerpoint presentation to update the Audit Committee on progress with the review of risk management arrangements and the development and implementation of a strengthened approach. (A copy of the presentation is filed with the signed Minutes of the meeting).

Effective risk management had been a statutory responsibility since the implementation of the Accounts and Audit Regulations 2015 and was integral to financial and performance management. Best practice and principles to be followed were set out by CIPFA / SOLACE Delivering Good Governance in the Public Sector 2016.

The presentation included:

- A definition of risk.
- An explanation of how the risk management arrangements and approach had been reviewed.

- The risk hierarchy specified 3 levels of risk management: Corporate, Service Strategic and Service Operational and the relationship with projects and partnerships.
- 18 risks were being managed at a corporate level which were owned by an officer and appropriate portfolio holder. A timetable set out the programme of meetings for discussion and review by relevant parties, which also included the Executive Team and Informal Cabinet, in addition to the risk owners. These were to be reviewed on a 6 month cycle.
- Management of service strategic risks had been rolled out across the four directorates in phases. The process had been implemented in the last directorate, Adults and Children, in July 2019. First phase reviews had been completed for Place, HR/OD and People and Finance. Reviews were to be undertaken on a quarterly basis.
- The Risk Management Framework had been aligned to the British and international quality standard for risk management BS ISO 31000:2018.

A review of the new arrangements and approach was planned to seek feedback and make adjustments as required and to inform the update of the framework.

The Portfolio Holder for Corporate Services commented on the thoroughness of the process which provided members with an opportunity for involvement and the value of the process to mitigate risks following changes to processes and behaviour.

In answer to questions from members it was confirmed that:

- As part of the review of Audit Committee, their role and involvement in the process will be reviewed. Members will be provided with a copy of the templates and examples of the risk register dependant upon the outcome of the review.
- Risks were managed by officers on a daily basis and the new process had been well received although it would take time for the revised process to be embedded across the organisation. Updates would be provided to future meetings.

**RESOLVED** that the presentation be received and noted.

**CHAIR** \_\_\_\_\_

**DATE** \_\_\_\_\_