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# 2020/21 Draft Financial Statements Highlight Report

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<b>Committee considering report:</b>	Governance and Ethics Committee
<b>Date of Committee:</b>	26 July 2021
<b>Portfolio Member:</b>	Councillor Ross Mackinnon
<b>Date Portfolio Member sent/agreed report:</b>	15 June 2021
<b>Report Author:</b>	Shannon Coleman-Slaughter
<b>Forward Plan Ref:</b>	GE3820

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## 1 Purpose of the Report

- 1.1 This report is to inform members of the key highlights from the draft 2020/21 financial statements and progress against the implementation of recommendations made by the Council's external auditors Grant Thornton in respect of the 2019/20 external audit.

## 2 Recommendation

This report does not include any recommendations and is for members to note only.

## 3 Implications and Impact Assessment

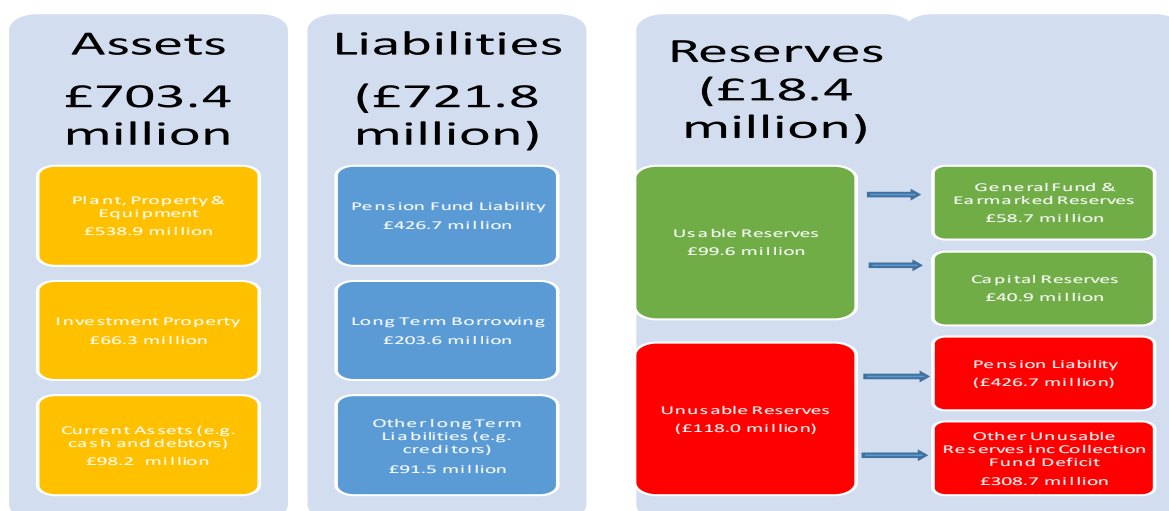
Implication	Commentary
<b>Financial:</b>	The Council continues to maintain healthy usable reserve levels for future deployment in support of services and expenditure. The negative Balance Sheet of £18.4 million is driven by the increase in the pension fund liability to £426 million, which is subject to significant changes between reporting periods due to changes in underlying actuarial assumptions.
<b>Human Resource:</b>	Not applicable
<b>Legal:</b>	The Council is required to ensure the annual financial statements are properly prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting

	and prepared in accordance with the Local Audit and Accountability Act 2014.			
<b>Risk Management:</b>	Where external auditors deem that the Council's annual financial statements are not prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting and the Local Audit and Accountability Act 2014, this can result in additional testing and external audit fees. If the external auditor finds that the Council has not produced financial statements that provide a true and fair view of the Council's financial position and performance this will result in a qualified audit opinion with significant reputational repercussions.			
<b>Property:</b>	Not applicable			
<b>Policy:</b>	Not applicable			
	<b>Positive</b>	<b>Neutral</b>	<b>Negative</b>	<b>Commentary</b>
<b>Equalities Impact:</b>				
<b>A</b> Are there any aspects of the proposed decision, including how it is delivered or accessed, that could impact on inequality?		X		
<b>B</b> Will the proposed decision have an impact upon the lives of people with protected characteristics, including employees and service users?		X		
<b>Environmental Impact:</b>		X		
<b>Health Impact:</b>		X		

<b>ICT Impact:</b>		X		
<b>Digital Services Impact:</b>		X		
<b>Council Strategy Priorities:</b>		X		
<b>Core Business:</b>		X		
<b>Data Impact:</b>		X		
<b>Consultation and Engagement:</b>	Joseph Holmes – executive Director for Resources, s151 Officer			

## 4 Executive Summary

4.1 The financial statements are produced in compliance with the CIPFA/LASAAC code of practice on local authority accounting and the Local Audit and Accountability Act 2014. The 2020/21 financial statements are currently under production and the figures in this report are subject to change. It is anticipated that the draft financial statements will be produced by the extended national deadline of 31st July 2021. The draft Balance Sheet is currently in a negative £18.4 million position. In respect of overall net assets held by the Council, i.e. total assets less total liabilities, the graphic below provides a high level overview of the Balance Sheet as at 31.3.2021.

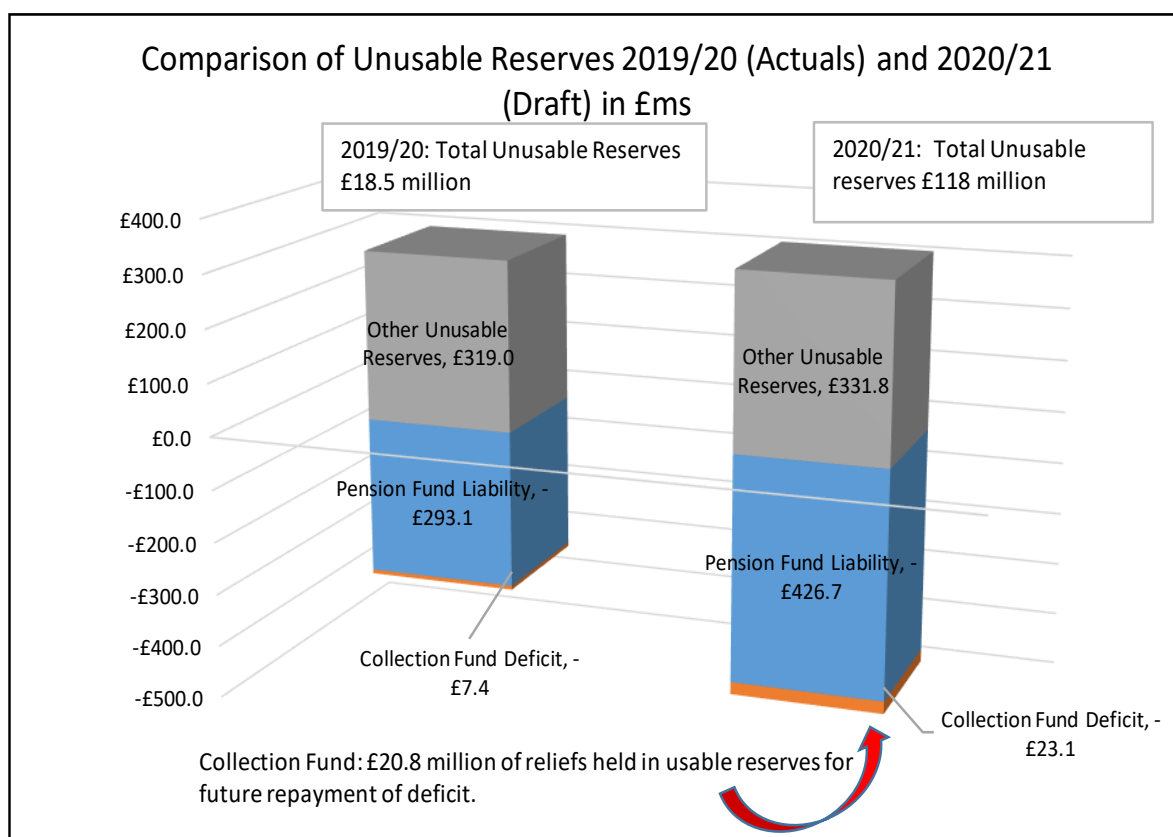


4.2 The main driver for the negative Balance Sheet position is the pension liability. The pension liability as at 31.3.2021 has grown by £133.6 million to £426.7 million. The pension fund liability is determined by the external actuaries and the performance of

The Royal Berkshire Pension Fund. The two main contributing factors to the £133.6 million increase between 31.3.2020 and 31.3.2021 are:

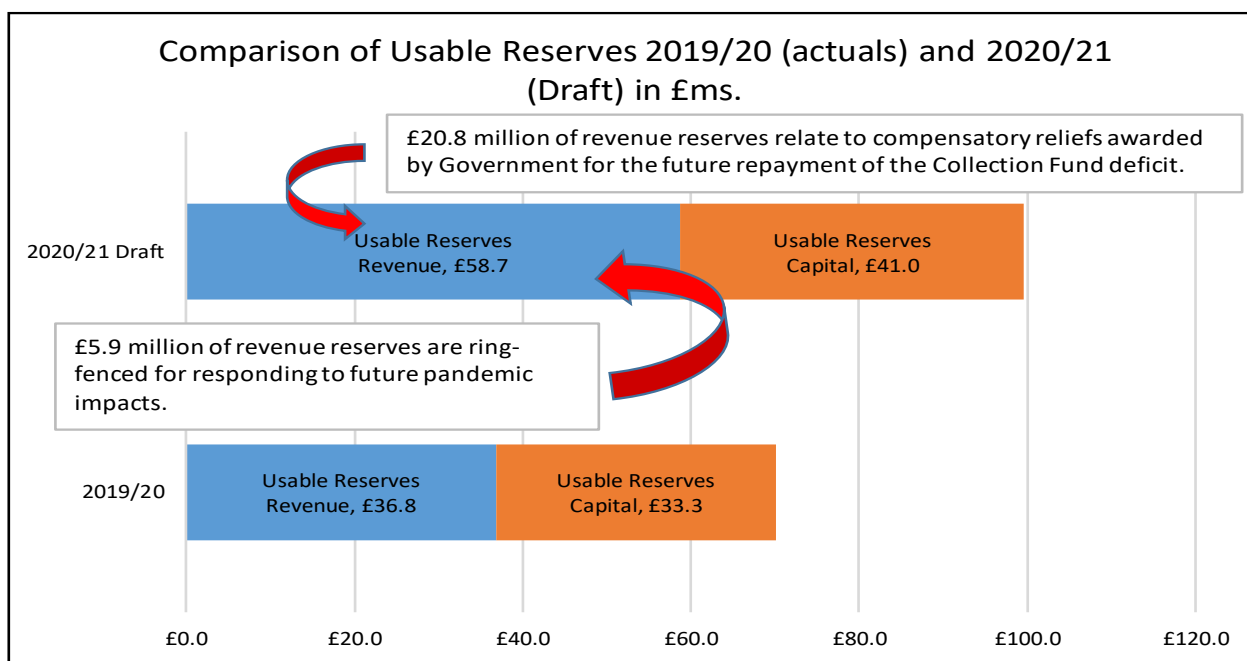
- (a) A fall in bond rates between 31.3.2020 and 31.3.2021 (bond rates are used to discount to present value, a lower bond rate results in a higher value placed on the present value increasing the liability),
- (b) The increase in CPI assumptions as pensions payable are linked to inflation increasing the liability.

4.3 The pension liability is shown as a liability within the Council’s net assets on the Balance Sheet and has a corresponding deficit held in the unusable reserves. The other main significant reserves move relates to the Collection Fund (Council Tax and Business collections). The Collection Fund deficit has grown substantially between 31.3.2020 (£7.4 million) and 31.3.2021 (£23.1 million) due to extraordinary circumstances relating to the pandemic. The financial downturn has caused collection rates to be substantially lower than those estimated, whilst the Government has introduced emergency rate reliefs for particular business sectors and compensation schemes for Councils. The collective Collection Fund deficit as at 31.3.2021 is broken down into Council Tax (deficit of £1.5 million) and Business Rates (deficit of £21.6 million). Accounting regulations require that the gross deficit of £23.1 million is held within unusable reserves on the Council’s Balance Sheet. Compensatory reliefs totalling £20.8 million (Council tax £1 million and Business Rates £19.8 million) are required to be held within usable reserves.



4.4 The overall reserves position (usable plus unusable) is a negative £18.4 million (£99.6 million usable and £118 million unusable). Usable reserves have increased from £70

million as at 31.3.2020 to £99.6 million as at 31.3.2021. The increased usable reserves balance is inclusive of £20.8 million of Collection Fund compensation reliefs and £5.9 million of earmarked funding to response to impacts of the pandemic in future financial years. Usable reserves are split between capital reserves of £40.9 million and revenue reserves of £58.7 million.



4.5 Under International Standard on Auditing 570 the Council’s appointed External Auditor Grant Thornton, request that as part of the closure of the 2020/21 financial statements, a going concern assessment as at the Balance Sheet date of 31st March 2021 is completed. In light of the Covid-19 outbreak and the significant expenditure, and lost income, for the Council as well as the financial support provided by Government, this is increasingly important. When financial statements are prepared on a going concern basis, assets and liabilities are recorded on the basis that the Council will be able to realise its assets and discharge its liabilities in the normal course of business. A negative Balance Sheet, i.e. a net liability position requires a greater level of management assurance to underpin a positive going concern assessment. The Draft Financial Statements Highlights Report should therefore be read in conjunction with the 2020/21 Going Concern Assessment Report.

## 5 Supporting Information

### Introduction

5.1 Councils are required to annually produce a set of financial statements that comply with CIPFA/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014. The statutory deadline for production and publication of the annual financial statements is 31<sup>st</sup> May. As a result of the Covid pandemic the deadline has been temporarily extended to 31<sup>st</sup> July 2021 for the financial year 2020/21 draft statements.

5.2 Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice ('the Code'), the Council's appointed external auditors are required to report whether, in their opinion, the Council's financial statements:

- (a) Give a true and fair view of the financial position of the Council and Council's income and expenditure for the year; and
- (b) Have been properly prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014.

## Background

5.3 The 2019/20 Financial Statements were finalised on 28<sup>th</sup> May 2020 with an unqualified audit opinion issued by the Council's external auditors Grant Thornton. A number of recommendations were made by Grant Thornton (full Action Plan dated 7.4.2021 is included in appendix A), which impact on the preparation of the 2020/21 financial statements, summarised as follows:

- (a) "Review of the Fixed Asset Register (FAR) and agreement to the statement of accounts identified that one asset valued at £2.4m had been incorrectly classified as an investment property and £6.1m of Investment property land had been double counted. This has resulted in a material adjustment to the primary statements. Recommendation: The Council should review all supporting documentation for Property, Plant and Equipment to ensure that balances are appropriately and accurately disclosed in the statement of accounts." **Progress: New review procedures have been adopted for preparation of the 2020/21 financial statements.**
- (b) "Substantive testing of transactions identified that the Council has an issue with providing a full breakdown of transactions and in reconciling populations to the balances disclosed in the statement of accounts. This has required management to run individual reports on an ad-hoc basis to provide the listing to Audit and has resulted in a number of errors being noted. There is a risk that the balances disclosed in the statement of accounts are either misstated or cannot be supported which could lead to a material adjustment within the primary statements. Recommendation: The Council should ensure that balances disclosed in the statement of accounts are fully supported by an auditable transaction listing or other supporting documentation." **Progress: The current Agresso system is not mapped, i.e. it functions as a general ledger as opposed to a system which has capability to produce a set of financial statements. The statements were produced manually for 2019/20. Partial mapping of the system is now in place and a Balance Sheet, Comprehensive Income & Expenditure Statement and a number of disclosure notes can be produced from the system. Full mapping of the system is an ongoing process.**
- (c) "The Audit approach requires the identification and testing of debit balances in income. Testing of these items identified that they were expenditure items and therefore incorrectly classified. There is a net nil impact on the statement of accounts. Recommendation: The Council should ensure that all transactions are appropriately classified within the General Ledger and subsequently the statement

of accounts.” **Progress: This is in progress and is linked to the mapping of the Agresso system.**

- (d) “The Code requires that the Council disclose an Expenditure Funding Analysis within the statement of accounts to show a reconciliation between the figures in the statement of accounts and the outturn figures reported to members. Review of these identified that the figures did not reconcile. Recommendation: The Council should ensure the consistency of reporting between the statement of accounts and the figures reported to members.” **Progress: Pending - upon completion of the draft 2020/21 financial statements, a reconciliation between the financial position at outturn reported to members and the position of the Comprehensive Income & Expenditure Statement in the accounts will be provided within the Director’s Narrative Statement.**

5.4 In respect of statutory changes which will impact on the preparation of the 2020/21 accounts, no new accounting standard have been adopted in relation to financial year 2020/21. The implementation of IFRS 16 Leases has been delayed until financial year 2022/23. Other changes that will impact on the 2020/21 financial statements are:

- (a) Council’s with an accumulated deficit on the Dedicated Schools Grant (DSG) as at 31.3.2020 are required to transfer any deficit at 31.3.2021 to a newly created DSG Adjustment Account held within unusable reserves. There was an accumulated deficit on the DSG as at 31.3.2020 of £1.6 million, the revised deficit at 31.3.2021 is £1.4 million.
- (b) The requirement for additional disclosures in the financial statements relating to pandemic grant funding received and distributed during the financial year. Additional disclosures of pandemic funding and application within the Finance Director’s Narrative Statement within the financial statements.

## Proposals

There are no proposals included within this report. This report is to note only.

## 6 Other options considered

Not applicable, report is to note only.

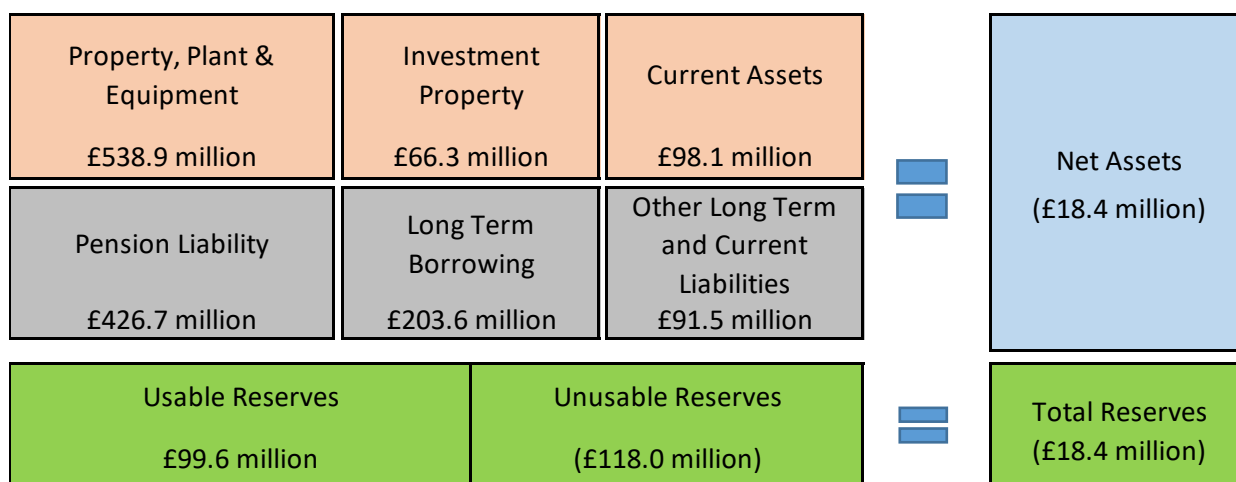
## 7 Conclusion

- 7.1 The financial statements are produced in compliance with the CIPFA/LASAAC code of practice on local authority accounting and the Local Audit and Accountability Act 2014. The 2020/21 financial statements are currently under production and the figures in this report are subject to change. It is anticipated that the draft financial statements will be produced by the extended national deadline of 31<sup>st</sup> July 2021.
- 7.2 The draft Balance Sheet is currently in a negative £18.4 million position. The negative position is being driven by the pension fund liability which has increased substantially between 31.3.2020 (£293 million) and 31.3.2021 (£426.7 million) financial year ends. The pension liability is based on the assumption that if the Council ceases to exist as at

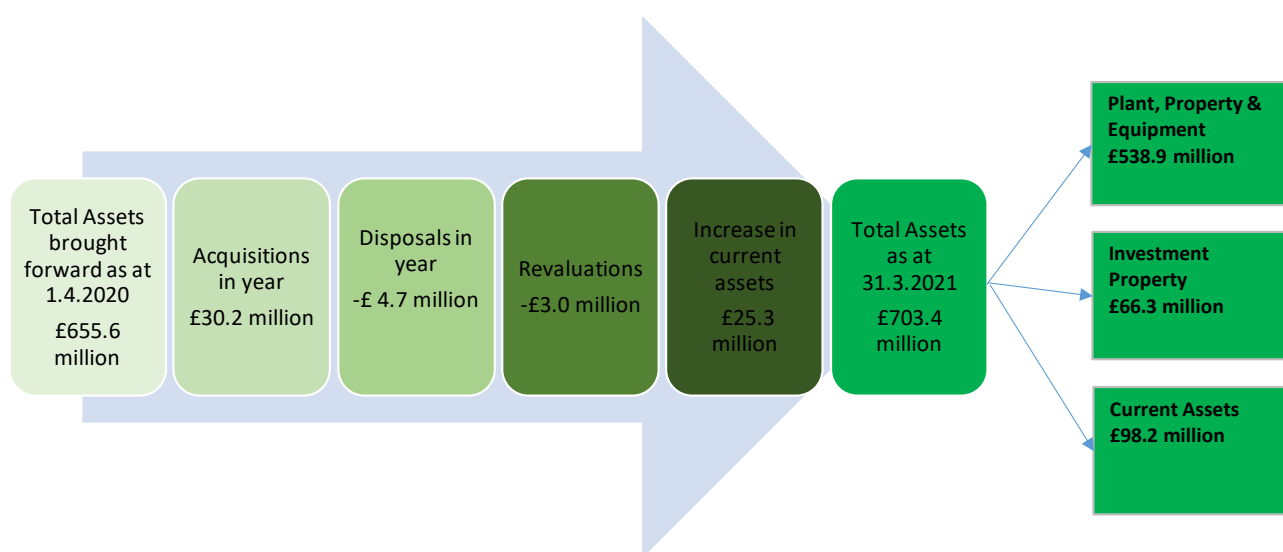
31.3.2021 then the full liability would be payable. The two main contributing factors to the £133.6 million increase are:

- (a) A fall in bond rates between 31.3.2020 and 31.3.2021 (bond rates are used to discount to present value, a lower bond rate results in a higher value placed on the present value increasing the liability),
- (b) The increase in CPI assumptions as pensions payable are linked to inflation increasing the liability.

7.3 In respect of overall net assets held by the Council, i.e. total assets less total liabilities, the graphic below provides a high level overview of the Balance Sheet as at 31.3.2021.



7.4 The Council’s total assets have increased from £655.6 million as at 31.3.2020 to £703.4 million as at 31.3.2021. The uplift is detailed in the following graphic.



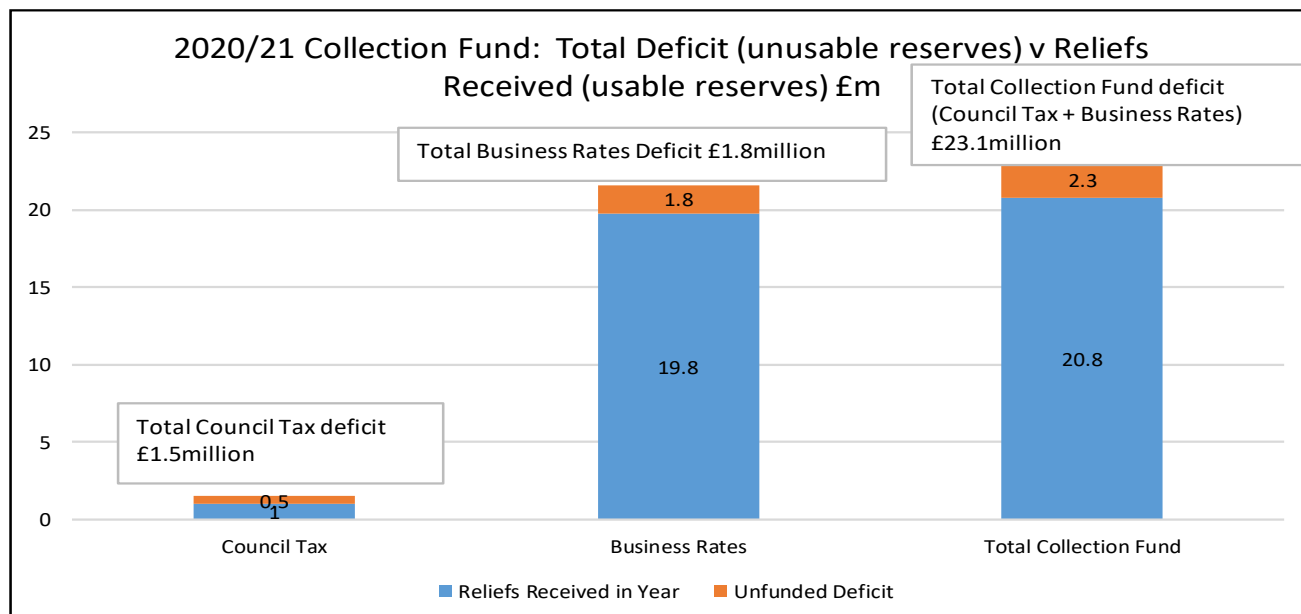
7.5 Asset additions of £30.2 million primarily relate to infrastructure improvements and improvements to operational buildings inclusive of Council controlled schools. £4.7



million of disposals were processed relating to actual sale of assets (e.g. Waterside Youth Centre) and a writing out of assets from the accounts where ownership/existence of the asset could not be substantiated (£4.2 million).

- 7.6 Current assets inclusive of cash balances held by the Council increased from £61 million as at 31.3.2020 to £98.1 million as at 31.3.2021. The main drivers of the increase have been additional cash balances held in year as a result of additional funding received from Government in response to the pandemic (£15.9 million as at 31.3.2020 and £21.0 million as at 31.3.2021) and a substantial increase in short term debtors of £31.5 million (£28 million as at 31.3.2020 increased to £59.5 million as at 31.3.2021). Debt recovery action was suspended during financial year 2020/21 in response to the pandemic impacting on the debtor levels contained within the financial statements. Debt recovery processes were re instigated in early 2021/22, the debtor levels will require review during the current financial year to ascertain and monitor the level of unrecoverable debt as the impacts of the pandemic continue to be felt.
- 7.7 In respect of the overall reserves position, usable reserves have increased from £70.0 million as at 31.3.2020 to £99.6 million as at 31.3.2021. The increased usable reserves balance is inclusive of £20.8 million of section 31 reliefs provided by Government to offset the Collection Fund deficit of £23.1 million held in unusable reserves. A further £5.9 million of funding is earmarked in a ring-fenced reserve to respond to impacts of the pandemic in future financial years. Usable reserves are split between capital reserves of £40.9 million and revenue reserves of £58.7 million.
- 7.8 Unusable reserves have been impacted by the Pension Fund liability and the Collection Fund Deficit. Unusable reserves are amounts set aside that the Council is unable to use to fund expenditure because they are unrealised or notional, i.e. they are not cash backed and relate to accounting adjustments.
- 7.9 The Collection Fund deficit has grown substantially between 31.3.2020 (£7.4 million) and 31.3.2021 (£23.1 million) due to extraordinary circumstances relating to the pandemic. The financial downturn has caused collection rates to be substantially lower than those estimated. In addition, after the estimated proceeds were fixed for 2020/21, the Government introduced emergency rate reliefs for particular business sectors. In the cases of both reduced collection rates and emergency rate reliefs, the Government has implemented grant schemes to compensate Councils for the lost income. However, accounting regulations require that the shortfalls in estimated income are reversed out of the General Fund at 31 March 2021 and into the Collection Fund Adjustment Account in unusable reserves. The grants that compensate for these losses however remain within the General Fund. In essence the deficit incurred between estimated income for 2020/21 and actual income received is held in the unusable reserves and the compensatory reliefs are held in the General Fund in usable reserves.
- 7.10 As at 31.3.2021 the total Collection Fund deficit is £23.1 million gross and £2.3 million net after consideration of reliefs held in the General Fund. The deficit is broken down into Council Tax (gross deficit at 31.3.2021 of £1.5million, net deficit of £0.5million after consideration of £1 million of reliefs) and Business Rates (gross deficit £21.6 million, net deficit of £1.8 million after consideration of £19.8 million of reliefs). The reliefs are held in the General Fund and earmarked for future repayment of the Collection Fund deficit over three financial years determined under statutory guidance passed in response to the pandemic. The total Collection Fund deficit in unusable reserves is

£23.1 million and £20.8 million of grant reliefs is held in usable reserves, detailed in the graphic below.



7.11 In preparing the 2020/21 financial statements there has been a change in accounting practice relating to treatment of the cumulative deficit on the Dedicated Schools Grant (DSG). In prior years the deficit has been treated as a debtor in net assets. For 2020/21 new guidance was released in May 2021 requiring for the deficit to now be held within the Council’s unusable reserves. The DSG deficit held in unusable reserves as at 31.3.2021 is £1.4 million.

7.12 The Section 151 Officer concludes based on the draft Balance Sheet as at 31.3.2021, the Council continues to maintain healthy usable reserve levels for future deployment in support of services and expenditure. The negative Balance Sheet is driven by the increase in the pension fund liability which is subject to significant changes between reporting periods due to changes in underlying actuarial assumptions.

## 8 Appendices

8.1 Appendix A – 2019/20 LG Audit Findings Report Action Plan supplied by Grant Thornton dated 7.4.2021.

8.2 Appendix B – Directors Narrative Statement

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### Subject to Call-In:

Yes:  No: X

The item is due to be referred to Council for final approval

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- Delays in implementation could have serious financial implications for the Council
- Delays in implementation could compromise the Council's position
- Considered or reviewed by Overview and Scrutiny Management Committee or associated Task Groups within preceding six months
- Item is Urgent Key Decision
- Report is to note only

**Officer details:**

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**Document Control**

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**Change History**

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