This version of the report is a draft. Its contents and subject matter remain under review and its contents may change and be expanded as part of the finalisation of the report. This draft has been created from the template dated 22/09/2022.

Grant Thornton

West Midlands Combined Authority Audit Progress Report and Sector Update

Year ending 31 March 2022

22 September 2022

Contents

The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit planning process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect the Authority or all weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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Introduction

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This paper provides the Audit, Risk & Assurance Committee (ARAC) with a report on progress in delivering our responsibilities as your external auditors.

The paper also includes:

- a summary of emerging national issues and developments that may be relevant to you; and
- includes a number of challenge questions in respect of these emerging issues which the Committee may wish to consider (these are a tool to use, if helpful, rather than formal questions requiring responses for audit purposes)

Members of the ARAC can find further useful material on our website, where we have a section dedicated to our work in the public sector. Here you can download copies of our publications https://www.grantthornton.co.uk/en/services/public-sector-services/

If you would like further information on any items in this briefing, or would like to register with Grant Thornton to receive regular email updates on issues that are of interest to you, please contact either your Engagement Lead or Engagement Manager.

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Progress at 22 September 2022

Financial Statements Audit

We undertook our initial planning for the 2021/22 audit in March 2022, and interim audit in April. We issued a draft audit plan in April and this was presented to ARAC.

The Accounts and Audit Regulations 2015 were amended by SI 2021 No. 263. The Department for Levelling Up, Housing and Communities (DLUHC) previously stated their intention to introduce secondary legislation to extend the deadline for publishing audited local authority accounts to 30 November 2022 for the 2021/22 accounts. This is enacted by The Accounts and Audit (Amendment) Regulations 2022 (SI 2022 No. 708) that came into force on 22 July 2022. The deadline for publishing audited local authority accounts for 2021/22 is extended to 30 November 2022 and thereafter changed to 30 September for years up to 2027/28.

We began our work on your draft financial statements in late June, with a work plan in place to report back to ARAC on the 4th October. However a number of factors have prevented us from achieving this deadline, most notably, these include staff sickness in both the finance and audit team, coupled with increasingly complex audit trails.

We reflected this risk in our key recommendation arising from the audit last year, which was as follows:

> *"As the Authority has grown, the level and complexity of the transactions entered into has increased. While the accounting system enables individual transactions to be tracked the production of the statutory financial statements are heavily reliant on a set of detailed spreadsheets which provide the links back to the accounting system.*
>
> *The audit trail therefore becomes protracted, leading to inefficiencies and delays in the completion of the audit process. It also requires substantial officer time to provide the information that is required. The current method of compilation of the financial statements also means that we are unable to apply a range of automated audit techniques which would enable us to gain assurance over the balances provided in a shorter timescale.*
>
> *A full, joint review of the process should be undertaken following the completion of the audit to try and identify more efficient ways to gain the necessary assurance in future years."*

A joint review meeting was held following the audit last year, to identify areas for improvement, however the fundamental changes needed to the audit trails have not yet been made.

Our progress on key areas of the financial statement audit are outlined on pages 7 and 8. A revised delivery and resource plan has been agreed with management and is in place for a November sign off, but this will be dependent on outstanding issues being resolved in a timely manner, and the resolution of the national issue on infrastructure assets.

Value for Money

The new Code of Audit Practice (the "Code") came into force on 1 April 2020 for audit years 2020/21 and onwards. The most significant change under the new Code was the introduction of an Auditor's Annual Report, containing a commentary on arrangements to secure value for money and any associated recommendations, if required.

The new approach is more complex, more involved and is planned to make more impact.

Under the 2020 Code of Audit Practice, for relevant authorities other than local NHS bodies auditors are required to issue our Auditor's Annual Report no later than 30 September or, where this is not possible, issue an audit letter setting out the reasons for delay.

As a result of the ongoing pandemic, and the impact it has had on both preparers and auditors of accounts to complete their work as quickly as would normally be expected, the National Audit Office has updated its guidance to auditors to allow us to postpone completion of our work on arrangements to secure value for money and focus our resources firstly on the delivery of our opinions on the financial statements. This is intended to help ensure as many as possible could be issued in line with national timetables and legislation. The extended deadline for the issue of the Auditor's Annual Report is now no more than three months after the date of the opinion on the financial statements. We anticipate issuing our Auditor's Annual Report in December 2022. We have also written separately to the Chair of the ARAC confirming this.

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Progress at July 2022 (continued)

Other areas

Meetings

We meet with Finance Officers on at least a weekly basis as part of the ongoing final account process. We met with the Executive Director of Finance in July as part of our quarterly liaison meetings. We also met with your Chief Executive in September to discuss the Authority's strategic priorities and plans.

Events

We provide a range of workshops, along with network events for members and publications to support the Authority. Further details of the publications that may be of interest to the Authority are set out in our Sector Update section of this report.

Audit Fees

During 2017, PSAA awarded contracts for audit for a five year period beginning on 1 April 2018. 2021/22 is the fourth year of that contract. Since that time, there have been a number of developments within the accounting and audit profession. Across all sectors and firms, the Financial Reporting Council (FRC) has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge and to undertake additional and more robust testing.

Our work in the Local Government sector in the period 2018/19 to 2021/22 has highlighted areas where financial reporting, in particular, property, plant and equipment and pensions, needs to improve. There is also an increase in the complexity of Local Government financial transactions and financial reporting. This combined with the FRC requirement that all Local Government audits are at or above the "few improvements needed" (2A) rating means that additional audit work is required.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and local government financial reporting.

We have reviewed the impact of these changes on both the cost and timing of audits. We have discussed this with your s151 Officer including any proposed variations to the Scale Fee set by PSAA Limited. Based on these factors, the fee proposed at the planning stage of the audit is £68,355. Given the difficulties experienced with the audit trails on the audit and the additional time to resolve them a further variation will be needed. This will be discussed with finance officers in the first instance on the conclusion of the audit.

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Audit Deliverables

2021/22 Deliverables	Planned Date	Status
Audit Plan We are required to issue a detailed audit plan to the ARAC setting out our proposed approach in order to give an opinion on the Authority's 2021/22 financial statements and to report on the Authority's value for money arrangements in the Auditor's Annual Report	April 2022	Completed
Audit Findings Report The Audit Findings Report will be reported to the November Audit Committee.	November 2022	Not yet due
Auditor's Report This includes the opinion on your financial statements.	November 2022	Not yet due
Auditor's Annual Report This report communicates the key outputs of the audit, including our commentary on the Authority's value for money arrangements.	December 2022	Not yet due

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Progress on key areas of the accounts

Section of the Financial Statements	Percentage complete	Matters Arising	Outstanding information
Queries raised as part of interim and planning	50%	• No issues arising to date	• Queries to Internal Audit • Queries to IT • Queries on significant variances between management accounts and financial statements
Groups	20%	• No issues arising to date. Audit team to arrange file reviews with the auditors of MML • The auditors of WM5G have provided a small element of tax compliance in addition to the audit fee. As a result we are evaluating the ethical impact of that and our ability to rely on their work for the group audit.	
Technical Review of Financial Statements	20%	• Initial review has identified some changes required to the disclosures in the financial statements. Also some changes required to the group Movement in Reserves Statement (MiRS)	
Journals	75%	• No issues arising to date	• Sample queries outstanding
Property, Plant and Equipment	25%	• No issues arising to date	• Officers have written a paper on both the treatment of infrastructure assets and impairment. This has raised a number of further queries • The audit trail to support capital additions has required a number of iterations. The complexity of the audit trail has caused a delay in sample selection. • Paper on the impact of whistleblowing investigations on valuations used in the financial statements
Investments	75%	• No issues arising to date	• Some third party confirmations outstanding
Debtors	90%	• No issues arising to date	
Cash	75%	• No issues arising to date	
Creditors	60%	• No issues arising to date	• Sample queries outstanding
Borrowings	50%	• No issues arising to date	• Third party confirmations outstanding

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Progress on key areas of the accounts (continued)

Section of the Financial Statements	Percentage complete	Matters Arising	Outstanding information
Provisions	80%	• No issues arising to date	
Grants	10%	• Audit trail for grants is complex and not all balances in the accounts are currently supported by listings that enable transactional testing. • A prior period adjustment has been made by officers that requires further investigation	• Technical paper that supports officers decisions for a prior period adjustment with full supporting evidence. • A transactional listing that supports the balances as disclosed in the financial statements in relation to capital grants.
Other Income	10%	• No issues arising to date	• Sample evidence to be provided. This has been outstanding for a number of weeks.
Employee expenses	70%	• A change in system has resulted in difficulties in obtaining the appropriate supporting information for all transactions	• Queries on substantial analytical review outstanding. If these are not appropriately resolved, additional substantive testing will be required on a sample basis.
Operating expenditure	60%	• As in prior years, the audit trails are overly complex, and require significant manual intervention to arrive at listings that are at a transactional level. This has delayed sample selection	• Sample evidence to be provided and queries outstanding
Related Party Transactions	70%	• No issues arising to date	• Queries outstanding on agreement of supporting information to what has been provided in the draft financial statements
Cashflow Statement	70%	• Disclosure does not include all required lines on the face of the statement. Adjustment is required.	• Copy of revised CIPFA cashflow toolkit
Narrative statement and Annual Governance Statement (AGS)	25%	• No issues arising to date	
Movement in Reserves Statement (MiRS)	25%	• Amendments required to group MiRS	

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Sector Update

Authorities continue to try to achieve greater efficiency in the delivery of public services, whilst facing the challenges to address rising demand, ongoing budget pressures and social inequality.

Our sector update provides you with an up to date summary of emerging national issues and developments to support you. We cover areas which may have an impact on your organisation, the wider local government sector and the public sector as a whole. Links are provided to the detailed report/briefing to allow you to delve further and find out more.

Our public sector team at Grant Thornton also undertake research on service and technical issues. We will bring you the latest research publications in this update. We also include areas of potential interest to start conversations within the organisation and with audit committee members, as well as any accounting and regulatory updates.

- Grant Thornton Publications
- Insights from local government sector specialists
- Reports of interest
- Accounting and regulatory updates

More information can be found on our dedicated public sector and local government sections on the Grant Thornton website by clicking on the logos below:

Public Sector

Local government

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Response to local audit consultation – Department for Levelling Up, Housing and Communities (“DLUHC”)

The Department for Levelling Up, Housing and Communities (“DLUHC”) has published its response to the local audit consultation. This follows the “Redmond Review”, which reported in September 2020.

The response confirms plans to establish a new regulator, the Audit Reporting and Governance Authority (ARGA), as the system leader for local audit within a new, simplified local audit framework.

Ahead of ARGA’s establishment, a shadow system leader arrangement will start at the Financial Reporting Council (FRC) from September 2022.

The consultation response also announces:

- Plans to make audit committees compulsory for all councils, with each audit committee required to include at least one independent member. This will create greater transparency and consistency across local bodies.
- ARGA will take over statutory responsibility for preparing and issuing the Code of Audit Practice (from the National Audit Office).
- A post-implementation review of the new Value for Money arrangements. The Code is a key part of the local audit system, and it is important to ensure that it helps to facilitate effective local audit. To allow time for the new arrangements to bed in the response proposes this is completed within three years.

The full response can be found here:

[Government response to local audit framework: technical consultation - GOV.UK (www.gov.uk)]

Department for Levelling Up, Housing & Communities

Levelling up White Paper – Department for Levelling Up, Housing and Communities ("DLUHC")

On 2 February the Department for Levelling Up, Housing and Communities ("DLUHC") published its Levelling Up White Paper.

The paper states "Levelling up requires a focused, long-term plan of action and a clear framework to identify and act upon the drivers of spatial disparity. Evidence from a range of disciplines tells us these drivers can be encapsulated in six "capitals":

- Physical capital – infrastructure, machines and housing.
- Human capital – the skills, health and experience of the workforce.
- Intangible capital – innovation, ideas and patents.
- Financial capital – resources supporting the financing of companies.
- Social capital – the strength of communities, relationships and trust.
- Institutional capital – local leadership, capacity and capability."

The paper also states "This new policy regime is based on five mutually reinforcing pillars." These are set out and explained as:

1) The UK Government is setting clear and ambitious medium-term missions to provide consistency and clarity over levelling up policy objectives.
2) Central government decision-making will be fundamentally reoriented to align policies with the levelling up agenda and hardwire spatial considerations across Whitehall.
3) The UK Government will empower decision-makers in local areas by providing leaders and businesses with the tools they need.
4) The UK Government will transform its approach to data and evaluation to improve local decision-making.
5) The UK Government will create a new regime to oversee its levelling up missions, establishing a statutory duty to publish an annual report analysing progress and a new external Levelling Up Advisory Council.

Levelling Up the United Kingdom - GOV.UK (www.gov.uk)

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Grant Thornton – reaction to Levelling up White Paper

On 2 February the Department for Levelling Up, Housing and Communities ("DLUHC") published its Levelling Up White Paper.

Commenting on the release of the government's Levelling up White Paper plans, Phil Woolley, Head of Public Sector Consulting, Grant Thornton UK LLP, said:

"The publication of today's White Paper plans is a welcome first step and it is reassuring to see the government recognise the need for systemic changes in order to deliver its central aim of Levelling up. The '12 missions' can be seen as an attempt to consolidate existing elements of government activity behind a singular banner and now provides a clearer picture of the levelling up opportunity.

"Following a decade of successful regional devolution and mayors, the White Paper marks the next stage of the country's devolution journey. With government now offering a clear framework of devolved powers and accountability, local leaders will need to embrace the opportunity and collaborate across the public and private sector to ensure they negotiate and then deliver the best deal for their communities. Grant Thornton's Levelling Up Index shows that the economies of the 10 worst performing local authorities in England are on average over five times smaller than their best performing counterparts - highlighting the scale of the challenge ahead.

"To level up, these areas would need to grow their economies by £12billion, increase employment rates by 6 percentage points, create 1,700 new businesses a year and increase average weekly pay by £200. It is too early to determine whether the measures announced today will be sufficient, but it is a start. Success will ultimately depend on the ability and willingness of local and national government to translate these new frameworks into meaningful change in people's lives.

"The Spending Review offers the next opportunity for government to show its commitment by realigning departmental objectives behind these new goals."

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Prudential Code and Treasury Management Code – CIPFA

On 20 December CIPFA published the new Prudential Code for Capital Finance in Local Authorities (Prudential Code) and Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes (the Treasury Management Code).

CIPFA commented "These two statutory and professional codes are important regulatory elements of the capital finance framework in which local authorities operate. Local authorities are required by regulation to 'have regard to' their provisions. These two codes have been published a principles-based consultation from February to April, which was followed by a second consultation on the detailed changes to the code from September to mid-November.

The updated Prudential Code includes some substantive changes. Most notably, the provisions in Code which present the approach to borrowing in advance of need in order to profit from additional sums borrowed have been strengthened. Additionally, the relevant parts of Code have augmented to be clear that borrowing for debt-for-yield investment is not permissible under the Prudential Code. This recognises that commercial activity is part of regeneration but underlines that such transactions do not include debt-for-yield as the primary purpose of the investment or represent an unnecessary risk to public funds."

The updated Prudential Code removes the "advance of need" terminology and emphasises the legislative basis for borrowing, namely that a local authority can borrow and invest for any legislative function and/or for the prudent management of their financial affairs.

The examples listed in the Code of legitimate prudential borrowing are:

- Financing capital expenditure primarily related to the delivery of a local authority's functions;
- Temporary management of cash flow within the context of a balanced budget;
- Securing affordability by removing exposure to future interest rate rises; or
- Refinancing current borrowing, including replacing internal borrowing, to manage risk or reflect changing cash flow circumstances.

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The Value of Internal Audit – CIPFA

One of the key elements of good governance is an independent and objective internal audit service. Some organisations engage fully and reap significant benefits from the assurance, insight and expertise they bring whilst others pay lip-service to them and see their work as an administrative burden.

CIPFA's recent report, Internal Audit: Untapped Potential, lifts the lid on internal audit in public services. For some chief financial officers and chief executives, this report confirms the value and contribution of internal audit teams with 87% of respondents recognising the contribution internal audit makes to their organisation. However, some leadership teams saw internal audit as providing a basic service at minimal cost.

Getting the most out of the function requires honest conversations and long-term planning. Maintaining appropriate skills and knowledge within the function is necessary to ensure high quality internal audit in public services are retained.

Culture and governance

The Audit Committee should monitor the delivery of internal audit and their output will be a key part of the annual work-plan. However, internal audit is not a substitute for risk management and should enhance the overall assurances received by management. Executives and Officers should engage with internal audit recommendations to ensure the organisation gains maximum value from reviews.

Capacity

Reducing internal audit days can lead to a lack of 'corporate grip' and not identifying issues at an early stage. This report raises concerns over the capacity of internal audit across the public sector. The profession needs to valued and invested in to make it more attractive to new blood and for bodies to be able to attract the best candidates to their service.

Expectations

To maximise the impact of internal audit, a clear and aligned strategic audit plan and annual audit plan should be in place. This should be agreed with all stakeholders.

Future plans

Internal audit needs to adapt to the changing landscape, including risks such as climate change, digital and technological developments, cyber-security and ongoing financial and service pressures within their planning processes. For financial resilience and medium- and long-term financial strategies internal audit can provide vital independent assurance to decision makers to allow them to take on more risk and be more ambitious. Leadership teams need to be clear on what assurances they will require going forward.

For more information, Rob Whiteman share his views on this report.

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Good practice in annual reporting – NAO

The National Audit Office (NAO) has published this guide which sets out good practice principles for annual reporting with examples from public sector organisations

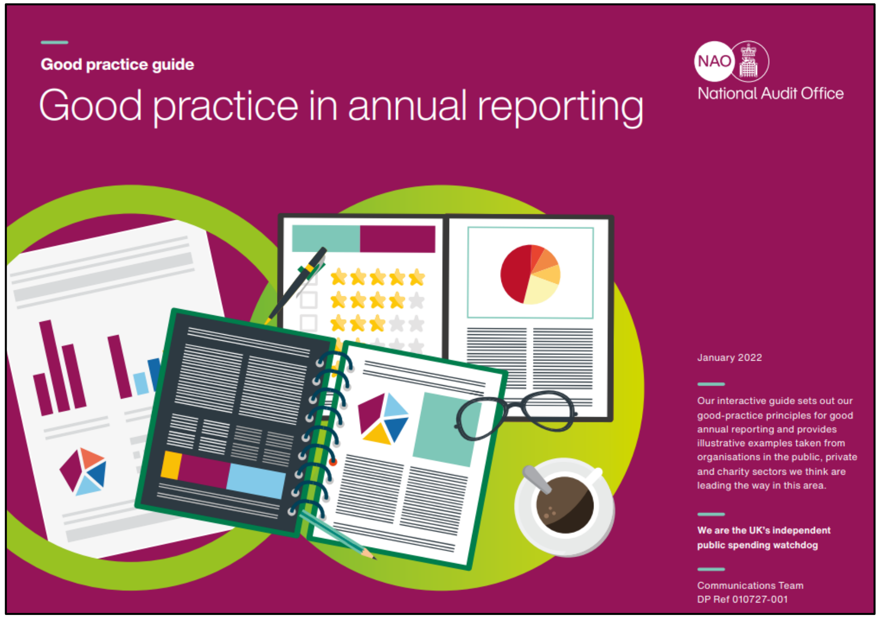
The NAO comment that the guide sets out "good-practice principles that we believe underpin good annual reporting. These principles are: Supporting Accountability; Transparency; Accessibility; and the need for the report to be Understandable."

The NAO further comment "The best annual reports we have seen use these principles to tell the "story" of the organisation. It is important that stakeholders, including the public and Parliament, are able to hold an organisation to account. To do this effectively, stakeholders need to properly understand the organisation's strategy, key risks that might get in the way of delivering this strategy and the effectiveness of their management, and the amount of taxpayers' money that has been spent to deliver the outcomes the organisation seeks to achieve."

The guide draws on examples of good practice from within each of the six sections of an Annual Report:

- Strategy
- Risk
- Operations
- Governance
- Measures of success
- Financial performance
- External factors

Although the guide does not include any local authority examples, those included, and the underlying principles, are equally relevant to all public facing organisations.



The guide can be found here:
[Good practice in annual reporting - National Audit Office (NAO) Report]

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Audit and Risk Assurance Committee effectiveness tool – NAO

The National Audit Office (NAO) has published this tool which supports Audit Committees in assessing their effectiveness.

The NAO comment "Audit and Risk Assurance Committees (ARACs) play a crucial role in supporting the effective governance of central government departments, their agencies and arm's-length bodies.

ARACs are operating in a highly challenging context. Government organisations are managing many short- and long-term risks and are required to be resilient to a number of pressures. This has created an environment where ARACs need to be dynamic and responsive to the changing risk profiles and demands of their organisations. ARACs can see this as an opportunity to work out how they can most proactively work with the Board and accounting officer.

Against this background, the NAO's effectiveness tool provides a way for ARACs to assess their effectiveness against more than just the basic requirements. It provides aspects of good practice to give ARACs greater confidence and the opportunity to meet the requirements of their role.

The NAO's effectiveness tool is a comprehensive way for ARACs to assess their effectiveness on a regular basis."

The tool covers:

- Membership, independence, objectivity and understanding
- Skills and experience
- Roles and responsibilities
- Scope
- Communication and reporting

Although the tool is designed for central government Audit Committees it is also relevant to local government.

The guide can be found here:
[Audit and Risk Assurance Committee effectiveness tool - National Audit Office (NAO) Report]

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Guide for audit and risk committees on financial reporting and management during COVID-19 – NAO

The National Audit Office (NAO) has published this guide which aims to help audit and risk committee members discharge their responsibilities in several different areas, and to examine the impacts on their organisations of the COVID-19 outbreak

The NAO comment "Audit and risk committees are integral to the scrutiny and challenge process. They advise boards and accounting officers on matters of financial accountability, assurance and governance, and can support organisations, providing expert challenge, helping organisations focus on what is important, and how best to manage risk.

Each organisation will have existing risk management processes in place, but risk appetite may have changed as a result of COVID-19, for the organisation to operate effectively and respond in a timely manner. This may result in a weakening of controls in some areas, increasing the likelihood of other risks occurring. Organisations will need to consider how long this change in risk appetite is sustainable for."

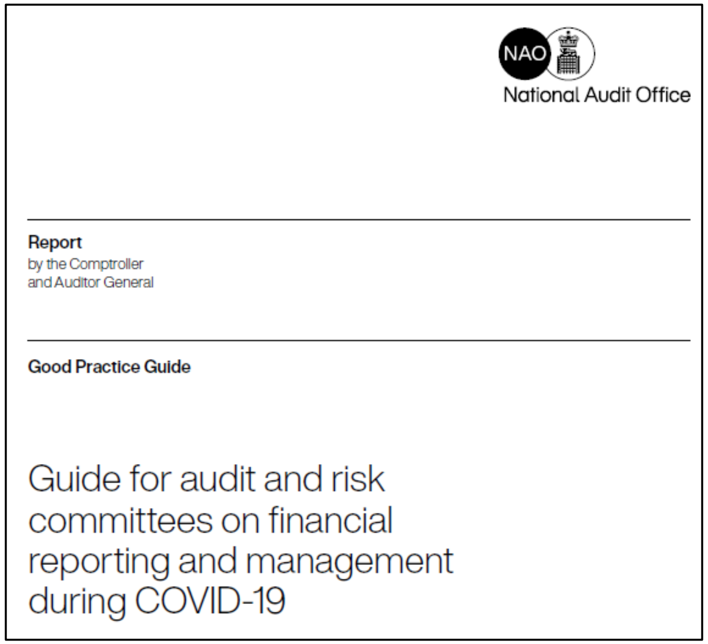
The guide includes sections on:

- Annual reports
- Financial reporting
- The control environment
- Regularity of expenditure

The guide can be found here: https://www.nao.org.uk/report/guidance-for-audit-and-risk-committees-on-financial-reporting-and-management-during-covid-19/

The guide includes a number of key questions covering areas such as:

- Property valuations
- Pension scheme valuations
- Completeness of liabilities
- Events after the reporting period
- Control environment
- Fraud and error


NAO
National Audit Office

Report
by the Comptroller
and Auditor General

Good Practice Guide

Guide for audit and risk committees on financial reporting and management during COVID-19

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