

NOTTINGHAM CITY COUNCIL

AUDIT COMMITTEE

MINUTES of the meeting held at Ground Floor Committee Room - Loxley House, Station Street, Nottingham, NG2 3NG on 6 May 2022 from 2.32 pm - 4.27 pm

Membership

Present

Councillor Audra Wynter (Chair)
Councillor Graham Chapman
Councillor Michael Edwards
Councillor Jane Lakey
Councillor AJ Matsiko
Councillor Sajid Mohammed (Vice Chair)
Councillor Anne Peach
Councillor Ethan Radford
Councillor Andrew Rule

Absent

Colleagues, partners and others in attendance:

Nancy Barnard	- Governance and Electoral Services Manager
Beth Brown	- Head of Legal and Governance
Andrew Smith	- Grant Thornton External Auditors
Clive Heaphy	- Interim Corporate Director for Finance and Resources
Kevin Lowry	- Interim Director of Housing Development
Councillor David Mellen	- Leader of the Council
Shail Shah	- Head of Audit and Risk
John Slater	- Group Auditor

1 APOLOGIES FOR ABSENCE

None

2 DECLARATIONS OF INTEREST

In the interests of transparency, in relation to agenda item 4 (External Review of Housing Financial Management and Council Response) Councillor Graham Chapman declared that he is a member of CIPFA and of the Nottingham City Homes Board, but he did not consider these to constitute interests that would require him to leave the meeting.

In the interests of transparency, in relation to agenda item 4 (External Review of Housing Financial Management and Council Response) Councillor Anne Peach declared that her partner is a former member of the Nottingham City Homes Board, but she did not consider this to constitute an interest that would require her to leave the meeting.

3 AUDIT PROGRESS REPORT AND SECTOR UPDATE

Andrew Smith of external auditors Grant Thornton gave a presentation, providing a progress report and general update on the sector. The following points were highlighted:

- (a) The position in relation to the financial statements audit for 2019/20 remains largely unchanged from that reported to the Committee in February 2022 as officers are working with new external valuers to gain valuations for specialist properties. This impacts on the financial statements for 2019/20 and 2020/21 and there is no definitive timeline for when updated 2019/20 accounts will be available.
- (b) High level initial planning for the 2020/21 audit has been completed but no further work can be done until the 2019/20 audit is completed.
- (c) The full 2020/21 Statement of Accounts has not yet been published due to the awaited property valuations and further information required in relation to Robin Hood Energy for the period prior to administration.
- (d) Because of the delays to the 2019/20 and 2020/21 financial statements, work on the 2021/22 audit has not yet commenced.
- (e) From Audit year 2020/21 onwards, Auditors are required to produce an Auditor's Annual Report containing a commentary on arrangements to secure value for money and any associated recommendations. This report had been required by 30 September but the deadline has now been extended to allow completion to be postponed to no more than three months after the date of the opinion on the financial statements. The February report set out reasons why the 2019/20 Value for Money conclusion would be likely to be qualified and significant weaknesses in 2020/21.
- (f) There are sector wide issues in relation to accounting for infrastructure assets. A CIPFA review is not expected until June or July.

In response to questions from the Committee the following points were highlighted:

- (g) The process in relation to Robin Hood Energy is complete but there is one outstanding action with a creditor.
- (h) The Finance Team is in a state of flux and staff turnover is a concern. This is a sector wide problem exacerbated by higher rates of pay in the private sector. The external audit recruitment market is also challenging but is being addressed through trainee schemes and international recruitment.

The Committee noted the update.

4 EXTERNAL REVIEW OF HOUSING FINANCIAL MANAGEMENT AND COUNCIL RESPONSE

Councillor David Mellen, Leader of the Council, introduced the item stating that the two investigations into the misattribution of Housing Revenue Account (HRA) funds (conducted by Richard Penn and CIPFA) had been commissioned by the Council in order to identify and understand the extent of the problems. The issues originated several years ago and the aim now is to understand how and why they arose and how they can be prevented from arising again. The Council is already under the observation of an Improvement and Assurance Board who are reporting to the Department for Levelling Up, Housing and Communities including regarding the HRA. The Council is committed to improvement and putting things right.

Clive Heaphy, Interim Corporate Director for Finance and Resources, then gave a presentation covering the following points:

- (a) The role of the Audit Committee in relation to the HRA issue and the findings of the Penn and CIPFA reports is to look at the adequacy of the control environment, to understand the steps being taken to rectify the failures and provide assurance that those failures cannot happen again and to identify lessons that can be learned.
- (b) The following facts were identified:
 - Nottingham City Council is the Local Housing Authority and hold a non-delegable duty to maintain an HRA
 - The HRA is ringfenced with permissible transactions set out in law and mandatory guidance
 - Nottingham City Homes (NCH) was established as an arms length management organisation (ALMO) to administer housing management and repairs on behalf of the Council
 - The assets remain on the Council's balance sheet and the tenants are the Council's
 - The Council owns NCH and its two subsidiaries. NCH is a Teckal company. Therefore NCH must carry out 80 percent of its trade with the Council and the Council must exercise close control over NCH.
- (a) Both the Penn and the CIPFA report identified issues relating to poor governance, culture and financial and operational control environments. The Council must now provide assurance that it has addressed these issues.
- (b) The Penn report found:
 - Awareness of payments was wide and covered many officers of the Council, NCH and Councillors but officers with the right knowledge were either reassured about legitimacy, ignored or dissuaded from voicing concerns. Some officers failed to demonstrate the necessary standards
 - Governance arrangements and the Council's client role were weak and need strengthening
 - NCH's Articles of Association do not give the Council the required level of control meaning NCH could run to its own agenda
 - The Council's three statutory officers and specialist staff must be respected and given due weight in decision making. Any new proposals in

relation to the HRA now go through these officers and a Housing Accountant and Director of Housing have been appointed.

- The role of External Audit should be questioned
- The Constitution and Code of Conduct were in need of review.

(c) The CIPFA report found:

- The Council's duty to ensure the HRA is dealt with correctly does not cease when it delegates service provision and the Council failed to require NCH to maintain the ringfence
- Funds totalling £8m were charged to the HRA with insufficient basis or evidence
- NCH received £32m more in HRA funding than it spent on HRA activity between 2014/15 and 2020/21
- There was a lack of financial direction from NCC to NCH on ring-fencing and surpluses
- There was no culture of challenge within the Council and poor evidence and basis for charges
- There was a lack of acceptance of the ring-fence within NCH.

(d) To date the following actions have been taken by the Council:

- The process of bringing housing management and repairs in house has begun
- The role of the three statutory officers has been strengthened and they now review all new HRA proposals
- The appointment of an Interim Director of Housing and commencement of strengthening of the client function
- Writing to the new Director of Finance at NCH to clarify the Council's expectations in relation to financial management and commencing work on a financial framework
- Requiring NCH to have full evidence based accounting for transactions with its subsidiaries
- A review of the Articles of Association to give the Council appropriate control.
- Reviewed processes for evidencing and recording financial transactions.

(e) Learning to date includes:

- Companies develop their own ways of working which must be fully understood by the Council as ownership does not equal control
- Specialists must be engaged with and listened to
- Financial performance and risk must be monitored and assessed in a way that recognises the differences between corporate entities. A shareholder unit has been established to understand this
- Governance arrangements must allow for agility on decisions so emerging issues can be addressed quickly to avoid any potential for company distress
- Do the boring stuff well – accounting, compliance and contract management.

(f) In addition to the actions already underway next steps include

- Seeking assurances on other ring-fenced funds to provide to external auditors and DLUHC
- ascertaining what funds are available to bridge the £17m gap identified in the CIPFA report, through analysis of cash flows between the Council, NCH and its subsidiaries, taking account of any loans.

During the subsequent discussion and in response to questions from the Committee the following points were made:

- (g) Taking NCH back in house is not a bad reflection on the staff or the work NCH is doing. Examples of good work include the actions they have taken post-Grenfell and on tenant involvement.
- (h) A ballot is not required to bring an ALMO in house, despite one being required to create an ALMO. There will be no change to policy or service delivery as a result of the transfer.
- (i) Basic bookkeeping needs to be done well. CIPFA were unable to find records to identify how HRA funds were spent although there were some clear examples of it having been mis-spent on general fund matters.
- (j) The view was expressed that more time should have been allowed to establish the facts of what happened and that NCH had disputed some of the findings. Cllr Mellen observed that they Council was under significant pressure from the government to take swift action and failure to do so could result in the loss of democratic control. The timetable had been challenged but the pressure continued. Clive Heaphy added that if CIPFA cannot find evidence they will find against. The evidence should be present for all transactions. Work is continuing however to understand the figures and seek supporting evidence where possible.
- (k) The earliest date to which the review was applied was selected because that was the point at which the management fee rebate started.
- (l) The expectation is that the £17m will not have to be found from the General Fund. The heart of the issue is the £32m gap between what went into the HRA and what was spent by NCH on HRA activity. If this is a matter of correction rather than a deficit this will be welcome but currently the Medium Term Financial Plan will need to be adjusted.
- (m) The Penn review interviewed up to 30 people and found that senior officers had given assurance in relation to HRA activity.
- (n) Many Councils have brought their ALMOs in house. The new Director of Housing has experience of this and has been brought in to oversee the process to ensure it is smooth and risks are managed. Capacity is being increased and a dedicated project team has been established including legal, HR and Communications expertise. Links will be made with resident engagement and NCH have established their own project team which mirrors the Council's. There is ongoing and open dialogue with Trade Unions and with

staff. A RAG rated risk register has been developed and work will be done with tenants to identify early any decline in service.

- (o) Andrew Smith from Grant Thornton, the Council's current External Auditors observed that Grant Thornton was appointed in 2018/19, after the management rebate had been included in the budget book. At the point at which they took over it was not cost or time effective to look into the opening balance in depth and therefore the issue was not identified. Sample testing is done on transactions but the relevant transactions may never have formed part of that sample due to not being material. There is not necessarily a failure of audit. Auditing standards have been complied with, but the issues were not picked up.

Clive Heaphy assured the Committee that he would write to the appointments body for external auditors whose function it is to review the quality of audit, and ask them to review the working papers of KPMG and Grant Thornton.

The Committee noted the update and agreed to have further reports back to future meetings when appropriate.