Essex County Council

Audit, Governance and Standards Committee

10:30	**Monday, 28 September 2020**	**Online Meeting**

The meeting will be open to the public via telephone or online. Details about this are on the next page. Please do not attend County Hall as no one connected with this meeting will be present.

For information about the meeting please ask for:
Andy Gribben, Senior Democratic Services Officer
Telephone: 033301 34565
Email: democratic.services@essex.gov.uk

Essex County Council and Committees Information

All Council and Committee Meetings are held in public unless the business is exempt in accordance with the requirements of the Local Government Act 1972.

In accordance with the Local Authorities and Police and Crime Panels (Coronavirus) (Flexibility of Local Authority and Police and Crime Panel Meetings) (England and Wales) Regulations 2020, this meeting will be held via online video conferencing.

Members of the public will be able to view and listen to any items on the agenda unless the Committee has resolved to exclude the press and public from the meeting as a result of the likely disclosure of exempt information as defined by Schedule 12A to the Local Government Act 1972.

How to take part in/watch the meeting:

Participants: (Officers and Members) will have received a personal email with their login details for the meeting. Contact the Democratic Services Officer if you have not received your login.

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Online:

You will need the Zoom app which is available from your app store or from www.zoom.us. The details you need to join the meeting will be published as a Meeting Document, on the Meeting Details page of the Council's website (scroll to the bottom of the page) at least two days prior to the meeting date. The document will be called "Public Access Details".

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The agenda is also available on the Essex County Council website, www.essex.gov.uk From the Home Page, click on 'Running the council', then on 'How decisions are made', then 'council meetings calendar'. Finally, select the relevant committee from the calendar of meetings.

Please note that an audio recording may be made of the meeting – at the start of the meeting the Chairman will confirm if all or part of the meeting is being recorded.

Exempt Items

(During consideration of these items the meeting is not likely to be open to the press and public)

The following items of business have not been published on the grounds that they involve the likely disclosure of exempt information falling within Part I of Schedule 12A of the Local Government Act 1972. Members are asked to consider whether or not the press and public should be excluded during the consideration of these items. If so it will be necessary for the meeting to pass a formal resolution:

That the press and public are excluded from the meeting during the consideration of the remaining items of business on the grounds that they involve the likely disclosure of exempt information falling within Schedule 12A to the Local Government Act 1972, the specific paragraph(s) of Schedule 12A engaged being set out in the report or appendix relating to that item of business.

Agenda item 1

Committee: Audit, Governance and Standards Committee

Enquiries to: Andy Gribben, Senior Democratic Services Officer

Membership, Apologies, Substitutions and Declarations of Interest

Recommendations:

To note

1. The membership of the committee as shown below

2. Apologies and substitutions

3. Declarations of interest to be made by Members in accordance with the Members' Code of Conduct

Membership
(Quorum: 3)

Councillor G Butland	
Councillor P Channer	
Councillor A Davies	
Councillor A Hedley	Chairman
Councillor A Jackson	
Councillor R Mitchell	
Councillor R Moore	
Councillor M Platt	Vice-Chairman
Councillor K Smith	
Councillor A Turrell	

Minutes of the meeting of the Audit, Governance and Standards Committee, that was held remotely on Monday, 6 July 2020

A recording of the meeting may be found on the ECC website.

Present:

Members:

Councillor G Butland	
Councillor P Channer	
Councillor A Davies	
Councillor A Hedley	
Councillor A Jackson	
Councillor M Maddocks	(substitute for Councillor R Mitchell)
Councillor Dr R Moore	
Councillor M Platt	
Councillor K Smith	
Councillor A Turrell	

Also Present:

David Eagles	BDO LLP (external auditor)
Norman Hodson	Independent Person appointed to advise the Council about standards issues
Barry Pryke	BDO LLP (external auditor)
Councillor C Whitbread	Cabinet Member for Finance (observing)

ECC Officers:

Joanna Boaler	Head of Democracy and Transparency
Paula Clowes	Head of Assurance
Christine Golding	Chief Accountant
Andy Gribben	Senior Democratic Services Officer (clerk to the meeting)
Paul Turner	Director, Legal and Assurance (Monitoring Officer)
Nicole Wood	Executive Director, Finance and Technology (section 151 officer)

1. Welcome and Introduction

Councillor Hedley welcomed everyone to the first virtual meeting of the Audit, Governance and Standards Committee and in particular:

- Members of the committee and any substitutes also attending
- Representatives of the External Auditors BDO
- Independent Person, Mr Hodson and
- Officers.

He paid tribute to the previous chairman of the committee the late Councillor Terry Cutmore and invited those present to observe a minute's silence.

2. Remote working

Councillor Hedley reminded everyone that although members are attending the meeting remotely, they should remain engaged in the meeting, refrain from responding to emails and texts during the meeting and put all devices on silent mode.

Members were reminded to keep their microphone on mute for the duration of the meeting unless they wished to speak and to address all remarks through the Chairman.

Councillor Hedley reminded members that the raise hand function was to be used and asked members not to send messages to the Chairman, but instead to send them to the Head of Democratic Services, Joanna Boaler who was managing the Zoom meeting.

Councillor Hedley also reminded members that the meeting was to be broadcast live over the internet and will then be publicly available on the County Council's website after the meeting. Although ECC was only making an audio recording of this meeting, Members should be aware that anyone attending this meeting, either as a panellist or an attendee, could make a video recording of all or any part of the proceedings. More details were set out in the agenda.

3. Election of Chairman

Having been moved by Councillor Platt and seconded by Councillor Maddocks and there being no further nominations Councillor Hedley was elected Chairman.

4. Appointment of Vice-Chairman

Having been moved by the Chairman, Councillor Hedley and seconded by Councillor Channer and there being no further nominations Councillor Platt was appointed as Vice-Chairman.

5. Membership, Apologies, Substitutions and Declarations of Interest

The report of Membership, Apologies and Declarations was received, and it was noted that:

1. The membership of the Audit, Governance and Standards Committee was as shown in the report.
2. Apologies for absence had been received from Councillor Mitchell who was substituted by Councillor Maddocks.
3. The following members declared interests:
    - Councillor Butland declared a Code Interest as a Director of South East Local Enterprise Partnership.

- Councillor Channer declared a Code interest in respect of agenda items 6, 8 and 9 as a Director of Essex Cares Ltd and a Code Interest in respect of agenda item 11 as she was named as a recipient of a gift she had declared.
- Councillors Davis, Hedley, Maddocks and Platt declared Code Interests as members of the Essex Pension Board.

The Chairman, Councillor Hedley reminded members that any interests must be declared during the meeting if the need to do so arose.

6. Minutes and Matters Arising

The minutes of the meeting held on Monday 20 January 2020 were approved as a correct record and signed by the Chairman.

7. Notes of discussion

The notes of the discussion that took place between the members of the Audit, Governance and Standards Committee, held online as a ‘virtual conversation’ on 23 March 2020 were received.

8. Internal Audit and Counter Fraud Annual Report for the year ended 31 March 2020

The report (AGS/69/20 and appendix), was presented by the Head of Assurance.

Members noted that, the Head of Assurance was required to form an opinion by the Public Sector Internal Audit Standards on the overall adequacy and effectiveness of the Council’s control environment and she had concluded that the Council had achieved an overall ‘satisfactory’ assurance rating. She also asked members to note that the Internal Audit and Counter Fraud Annual Report (Appendix 1 to the report) provided oversight of Internal Audit and Counter Fraud activity for 2019/20.

She also asked Members to note that, this year, she had been required to determine if sufficient evidence had been collected by Auditors in order to form an opinion prior to ‘lockdown’. She had concluded that sufficient Audit evidence had been achieved to allow her to reach an opinion.

She added that although the overall opinion remained at ‘satisfactory’ there was a perceivable positive direction of travel; less ‘limited assurance’; and a lack of ‘no assurance’. There had also been an improvement in the range of recommendations with no ‘critical recommendations’ being made this year and only eight ‘major recommendations.

She informed members of the committee that the council was compliant with Public Sector Audit Standards, the CIPFA Code on Management of Fraud, and all the work of the service had been carried out independently and free from interference.

There being no questions from members it was

Resolved

That the Internal Audit and Counter Fraud Annual Report and the opinion on the overall adequacy and effectiveness of the organisation's internal control environment be noted.

9. Prosecution and Sanction Policy (Fraud and Corruption)

The report (AGS/70/20 and appendix 1), deferred from the informal meeting on 23 March 2020, was presented by the Head of Assurance

Members noted that the report, other than the date shown on the front of the report, was exactly as had been presented to the informal meeting of the committee on 23 March and so, the discussion having taken place at that time it was

Resolved

That the Prosecution and Sanction Policy (Fraud and Corruption) be adopted in the form appended to the report.

10. Revised Internal Audit Plan for 2020/21

The report (AGS/71/20 and appendices a) and b) was presented by the Head of Assurance.

Members noted that the draft Internal Audit Plan for 2020/21 was originally presented an informal remote meeting of the members of the Audit, Governance and Standards committee in March 2020 and agreed in principle.

They also noted that since that time, with the impact of Covid-19, there have been significant changes to working practices and the risks have also changed, heightened or provided opportunities. Consequently, it was necessary to undertake a full review of the original plan and a revised plan was attached to the report at appendix 1 to the report and a detailed breakdown of all the proposed changes since the plan was considered by members of the Committee in March 2020 was attached at appendix 2.

It was noted that in future any changes to the Internal Audit Plan would be brought back to the Committee for approval.

In response to questions from Councillor Turrell it was agreed that a revision be made to Appendix 1 to ensure that, when the audit is undertaken on budgetary control, specific attention is placed upon what impact Covid-19 may have on commercial income over the next few years.

It was also suggested by Councillor Platt that the figure shown as being the Essex Pension Fund Assets of £4billion was incorrect. The Head of Assurance agreed to check the figure.

Councillor Smith declared an interest as he was an elected Member of Basildon Borough Council.

It was **Resolved**

That the 2020/21 Revised Internal Audit and Counter Fraud Plan be approved in the form at appendix 1 to the report subject to an amendment to the budgetary control audit including a reference to attention being required to the impact of Covid-19 upon Commercial Income.

11. To receive the Draft Statement of Accounts 2019/2020 and the Draft Annual Governance Statement

The report (AGS/72/20 and appendix 1) was presented by Christine Golding, Chief Accountant with additional information from the Executive Director, Finance and Technology. The Draft Annual Governance Statement was presented by the Director, Legal and Assurance

Members noted the report that presented a draft of the Statement of Accounts and the draft Annual Governance Statement for 2019/20 to the Committee for information and explained the committee's role with regard to approval of the Accounts and Annual Governance Statement in September.

Members noted the revised timetable for production and publication of the 2019/20 Statement of Accounts as detailed in the report and explained by the Chief Accountant. Members also noted that the external auditor planned to report the results of the audit work to the Committee on 28 September 2020, at which stage the Committee would be asked to approve the Statement of Accounts and Annual Governance Statement for publication.

In response to a request from members, the Executive Director, Finance and Technology explained that the financial impact of the Covid-19 pandemic was being monitored closely, and that quarterly updates would be reported to Cabinet. Financial risks include:

- Tax revenues which are at considerable risk, particularly council tax,
- Increased pressure in relation to Adults and Children's Social Care,
- Future waves of the pandemic.

Whilst the government has provided emergency funding to assist with the pandemic, it has yet to clarify the funding approach beyond their emergency funding.

The Draft Annual Governance Statement was presented by the Director, Legal and Assurance and explained that it was a legal requirement to produce it annually. He drew particular attention to the action plan. His opinion was that the Council's governance was in general strong but there were particular areas that required noting such as;

- Remote working,
- The implementation of the AGS Effectiveness Review,
- A review of Health and Safety,
- Preparation for elections to be held in May 2021.

In response to questions from members it was advised that a Risk Awareness review concluded that managers were cognisant of the risks arising and there has been a positive response to risk training and actually improved engagement.

Members were also advised that although FOIs, EIRs and SARs were responded to 'satisfactorily' there was an issue relating to GDPR and the nationally identified increased amounts of SARs being received by all local authorities. This is being constantly monitored by Essex.

It was **Resolved** that

1. The Committee note the arrangements for approval and publication of the Council's Statement of Accounts for 2019/20 and

2. The Committee, having reviewed the draft Annual Governance Statement for 2019/20, as appended to the report, determined that no comments or changes were required.

12. Consultation on proposed Local Government Association Model Code of Member Conduct.

The report (AGS/73/20 and appendices 1. 2 and 3) was presented by the Director, Legal and Assurance who advised the members of the committee that the National Committee on Standards in Public Life had published in 2019 a report on standards in local government. They had made a number of recommendations to local authorities, to the LGA and to central government. The Council ECC had implemented the recommendations, insofar as it was thought appropriate

The key recommendation of the CSPL to the LGA was that it should produce a draft model code for local authorities to consider adopting. The Council had welcomed the introduction of a model national code but there would be limited advantage in adopting the national code unless a significant number of Essex local authorities also adopt it.

In March 2020 the LGA published a consultation draft of the code. ECC was originally asked to respond to the code by the end of May 2020 but the LGA then decided to republish the draft Code, with a revised closing date of 17 August 2020.

Both the current ECC code and the draft LGA code have their roots in the former mandatory national code of conduct created by the Local Government Act 2000. This means that broadly the codes are similar but, as would be expected, there are a number of differences. The table appended to the report highlighted the differences between the current ECC code and compares it to the draft LGA Code, with a commentary.

In response to a question from the Chairman, Paul Turner explained the legislation concerning a member's employment or a potential pecuniary interest, what they should declare and the impact upon their ability to engage in decision-making.

The Chairman invited the Independent Person, Mr Hodson to comment on the report and having considered his views and those of members of the committee Paul Turner was requested to circulate to all Members, including Independent Persons, a draft of the proposed response for comment and encouraged them to respond to the consultation online directly. Alternatively, members could comment by email to the Chairman and these comments may be included in the Council's overall response to the consultation, in the name of the committee, which would be circulated to members of the committee before dispatch.

Resolved

That, subject to comments received from Members, and the review of the Chairman, the response be approved.

13. Review of Register of Gifts and Hospitality Register

The report (AGS/74/20 and appendix 1) was presented by the Director, Legal and Assurance and an opportunity for members of the committee to note the findings and raise any issues they may have.

Councillor Butland noted that there had been a change to a particular entry on the register since it had been circulated in draft and he sought an assurance that the Director, Legal and Assurance was now satisfied that the entry was currently correct. The Director, Legal and Assurance stated that the accuracy of the declaration was the responsibility of the member concerned but he believed that the declaration was now correct.

Members of the committee asked questions relating to specific entries and the process for declarations and they were urged to declare all potential interests, ownership of land, employment or gifts or hospitality received.

Resolved

The report was noted.

14. Work Programme

The report (AGS/75/20) was presented by the Director, Legal and Assurance. Members were reminded that the work programme was subject to regular revisions and change and noted that items arising from the recent Effectiveness Review had been added to the document since last it had been reviewed.

Resolved

The Work Programme was noted.

15. Date of the Next Meeting

Members noted that the next meeting of the committee would be held on Monday 28 September at 10.30am in Committee Room 1 or remotely (to be advised) and would be preceded by a private meeting for AGS members only.

Chairman……………………………….

Date……………………………….

Agenda item 3

Report title: Deferral of completion of the external audit of the Council's 2019/20 Statement of Accounts		**AGS/76/20**
Report to Audit, Governance and Standards Committee		
Report author: Nicole Wood, Executive Director, Finance and Technology		
Date of meeting: 28 September 2020	**For:** Information	
Enquiries to Nicole Wood, Executive Director, Finance and Technology **email** nicole.wood@essex.gov.uk **Tel.** 07946 705816 or Christine Golding, Chief Accountant **email** christine.golding@essex.gov.uk **Tel.** 03330 138401		
Divisions affected: All Essex		

1. Purpose of report

1.1 The purpose of this report is to present a report by the Council's External Auditor, BDO LLP, on deferral of completion of the audit of the Council's Statement of Accounts for 2019/20 (comprising the work necessary to provide audit opinions on the financial statements of the Council and Essex Pension Fund and reach a conclusion on the effectiveness of the systems in place to secure value for money in the Council's use of resources).

2. Recommendations

2.1 The Committee notes the reasons for deferral of completion of the external audit for 2019/20, as appended to this report.

2.2 The Committee agrees to move the meeting scheduled for **7 December 2020** to **16 November 2020** in order to meet BDO's revised expectations for completing their audit and for issuing their Audit Completion Reports for the Council and Essex Pension Fund for 2019/20, and to approve the Council's 2019/20 Statement of Accounts for publication.

3. Background

3.1 The Council is required by Regulation to:

- Produce draft accounts, and present them for external audit, by a specified date each year;
- Make the draft Statement of Accounts available for a period of 30 working days, during which time the public have the right to raise objections, inspect the accounts and question the Local Auditor; and
- Publish its final, audited accounts by a specified date each year.

3.2 Statutory regulations usually require these activities to be undertaken in accordance with the following timetable:

- Produce the draft Statement of Accounts and present them for external audit by **31 May**;
- Make the draft accounts available for public inspection for a period of 30 working days, to include the first **10 working days** of **June**; and
- Publish final, audited, accounts by **31 July**.

However, in recognition of the significant pressure local authorities have been under in responding to the COVID-19 pandemic, the Government extended the statutory deadlines for the 2019/20 financial year.

3.3 The Government extended the statutory deadlines as follows:

- The deadline for production of draft accounts was deferred from **31 May** to **31 August**;
- The deadline for publication of final, audited accounts, was deferred from **31 July** to **30 November**.

The Government also confirmed that authorities could choose when to commence their period for public inspection of their accounts.

3.4 An informal deadline of **30 June** was set for production of the draft Statement of Accounts for 2019/20.

3.5 In line with this aspiration, the Executive Director for Finance and Technology certified the draft (unaudited) Statement of Accounts for 2019/20 on **30 June**; and presented the draft accounts to the external auditor and commenced the 30-day period for the exercise of public rights on **1 July**. The draft Statement of Accounts was presented to the Committee (for information only) on **6 July 2020** (**AGS/72/20**).

3.6 Following discussions with BDO, it had been anticipated that the external auditor would report the results of the audit work to the Committee on **28 September 2020**, at which stage the Committee would be asked to approve the Statement of Accounts for publication. However, this has not proved possible, for the reasons outlined in BDO's report (as appended).

3.7 BDO now anticipate being able to complete most of their field work by the end of September and being able to present their Audit Completion Reports for the Council and the Essex Pension Fund to the Committee during week commencing **16 November 2020** (subject to the Committee being able to schedule a meeting during this week). Whilst this is much later than anticipated, audit sign off during week commencing 16 November would still be in accordance with the statutory deadline for publication of final, audited, accounts for 2019/20 which is 30 November 2020.

4. Policy context and Outcomes Framework

4.1 The Statement of Accounts for 2019/20 summarises the financial performance and financial position for the Council for the year ending 31st March 2020. As such, the Accounts provide a financial representation of activities during 2019/20 against the Organisation Strategy.

5. Financial Implications

5.1 It is not currently anticipated that there will be any specific financial implications arising because of deferral of completion of the 2019/20 audit.

5.2 From the Council's perspective, it would be difficult to understand why a delay in completion of its audit, for reasons outside of the Council's control, could justify an increase in audit fees. Consequently, any proposal by BDO to vary the audit fee for their 2019/20 audit would be subject to careful scrutiny.

6. Legal Implications

7.1 The Council is required to produce annual accounts in accordance with the Accounts and Audit Regulations 2015 as currently amended by the Accounts and Audit (Coronavirus) (Amendment) Regulations 2020. The Council is also required to produce an annual governance statement.

7. Staffing and other resource implications

7.1 There are no staffing implications associated with this report.

8. List of appendices

8.1 **Appendix A** – Report by BDO LLP on deferral of completion of the audit of the Council's 2019/20 Statement of Accounts.

9. List of Background Papers

9.1 None

1. INTRODUCTION

1.1. This report explains the reasons for deferral of completion of the audit of the Council's 2019/20 Statement of Accounts.

2. BACKGROUND

2.1. The Council is required to publish its unaudited Statement of Accounts by 31 May each year. The audited Statement of Accounts should be published by 31 July each year or, where the audited Statement of Accounts is not yet available on this date, a statement explaining why this is the case.

2.2. In mid March 2020, MHCLG announced a deferral of the accounts publication deadline (also referred to as the "audit deadline", although there is no, and cannot be a, statutory deadline imposed for auditors issuing an opinion) to 30 September 2020. In early April 2020, MHCLG announced that the deadline for publication of the audited 2019/20 Statement of Accounts would be pushed back further to 30 November 2020, with the draft accounts due by 31 August 2020, recognising the impacts of the Covid-19 pandemic.

2.3. Following the original announcement, the Council assessed the potential impact of Covid-19 arrangements on accounts preparation and we agreed with the Council on 27 March 2020 that if the Council could provide a draft Statement of Accounts by 30 June 2020, our audit fieldwork would be rescheduled backwards and planned to be undertaken in July and August. Sign-off of the Statement of Accounts would then take place by the end of September 2020.

2.4. The Council provided us with the unaudited Statement of Accounts and supporting working papers at the end of June 2020 in accordance with the revised agreed timetable. We commenced our audit work at the start of July. However, a number of factors have resulted in our fieldwork continuing beyond the end of August 2020, making completion of the audit by the end of September 2020 unfeasible. The next section of this report describes these factors.

3. WHAT HAS CONTRIBUTED TO THE DELAY?

3.1. The booked resource for completion of the audit has been eroded to the extent that, whilst we can still complete the vast majority of our work by the end of September 2020, we cannot guarantee that our full and necessary audit quality arrangements will be complete, and so will not be in a safe position to issue our audit opinion.

3.2. BDO will not compromise on the quality of our audits and so it was necessary to communicate this position as early as we could to Management to enable alternative arrangements and timelines to be agreed. We communicated this position to the Chief Accountant on 26 August 2020 and followed this up with a direct discussion with the Executive Director Finance and Technology on 7 September 2020.

3.3. There is no single incident that has caused our planned profiled resource input to be reduced to the extent to which it has impacted on our completion of the audit to the end of September 2020 date. However, the following elements have cumulatively impacted on the availability of resource in July and August which we were unable to compensate for until September, which is unfortunately too late to mitigate the impacts and still achieve the planned delivery:

- ***NHS deadlines***: To reflect Covid-19, deadlines were pushed back from end May to 25 June 2020. Nationally, auditors were pushed right up to (and, in some cases, beyond) the later deadline because of significant delays in both the NAO-commissioned valuer expert report from Gerald Eve (only received 18 June 2020, so 3 weeks later than anticipated), which was key to Provider audits, and a controls assurance report on GP payments (which arrived late on 24 June 2020, a month late), which was key to Commissioner audits. These delays, both the general Covid-19 logistics and efficiency issues (see also below) and also the late key assurance reports, impacted on the very early phases of our local government portfolio audit work, with a consequent ripple effect to the July Essex planned work – whilst staff worked long hours to try and catch up, there was still a residual impact by July.

- ***Remote working due to Covid-19***: Unfortunately, remote working is making things take longer to complete than has previously been the case. There are a variety of factors, including remote communication (which is less efficient and effective than simply talking face to face with finance staff to discuss/explain/resolve issues) and the lack of "live" resolution of issues arising and team supervision. Whilst again not individually significant, the cumulative impact erodes planned resourcing. We understand that all firms are experiencing this and PSAA has coordinated communications with MHCLG on this issue. As a final point of clarification, there are genuine benefits to audits of *some* remote working (i.e. it is not necessary to be physically on site for the whole audit), but the Covid-19 scenario has prevented *any* on site working, and it is this that has caused the problems.
- ***Other issues***: These have included days "lost" due to regulator-required mandatory professional training that was scheduled to take place during July after we had agreed the deferred timetable and, in one case, the departure of one member of staff at relatively short notice. In this latter case, we were able to make compensating resource arrangements, but not to the original profiling.

3.4. The combined effect of the above factors resulted in our audit fieldwork not being as far progressed by the end of August as originally planned. In order to bring our audit procedures to completion as soon as possible, we have secured additional resource in the second half of September to make up for the shortfall caused by the reasons stated above.

4. NEXT STEPS

4.1. The audit team continue to work closely with the Council to progress procedures and clear queries arising from our audit work. The Senior Audit Manager and Chief Accountant meet on a weekly basis to discuss progress and outstanding issues (as they have done since early July).

4.2. We intend to substantially complete our fieldwork by the end of September 2020. Once our fieldwork is complete, there are a number of internal quality control processes which must be undertaken before we are able to conclude the audit and issue our opinion.

4.3. To ensure that these quality control processes can be completed and to allow sufficient lead times for reporting to the Audit, Governance and Standards Committee, whilst ensuring the 30 November 2020 deadline is met, our preferred timing for sign-off would be mid-November 2020.

4.4. Following completion of the audit, we will hold debriefs both internally and with the Council's finance team to discuss what worked well and what could be improved.

4.5. Needless to say, we regret the need to defer the date for completion of the audit, but we have not been able to mitigate against the lost time to the original profile of delivery and, because we are absolutely committed to delivering the highest quality audit to the Council, the only option is to defer to enable all necessary quality control processes to be fully completed. The revised target date, however, remains within the statutory deadline set by MHCLG.

David Eagles, Partner
For and on behalf of **BDO LLP** 15 September 2020

Agenda item 4

	AGS/77/20
Report title: Redmond Review	
Report to: Audit, Governance and Standards Committee	
Report authors: Nicole Wood, Executive Director, Finance and Technology and Paul Turner, Director, Legal and Assurance	
Date of meeting: 28 September 2020	**For:** Noting
Enquiries to Nicole Wood - Executive Director, Finance and Technology (nicole.wood@essex.gov.uk Tel 07946 705816) Paul Turner, Director, Legal and Assurance (paul.turner@essex.gov.uk Tel 03330 134591) or Christine Golding, Chief Accountant (christine.golding@essex.gov.uk Tel 03330 138401)	
Divisions affected: All Essex	

1. Purpose of report

1.1 The purpose of this report is to inform members of the conclusions and recommendations arising from the independent review into **Oversight of Local Audit and the Transparency of Local Authority Financial Reporting** (the 'Redmond Review').

2. Recommendations

2.1 That the report and the three recommendations to local authorities be noted.

2.2 Agree that the Committee should ask the Chairman of the Council to receive a report on the accounts as soon as possible after the Committee has considered the annual accounts.

2.3 Note that the Council is in the process of complying with the recommendation regarding the appointment of at least one independent member, suitably qualified, to the Audit Committee.

2.4 Note that the Chief Executive, the Monitoring Officer and the Chief Financial Officer currently have the facility to meet with the Key Audit Partner at least annually.

3. Background

3.1 The **Local Audit and Accountability Act 2014** (the 2014 Act) transferred the audit functions previously carried out by the **Audit Commission** to a range of successor bodies. The audit of the 2018/19 accounts was the first full year in which all the new arrangements were in operation.

3.2 In July 2019, the Secretary of State for the Ministry of Housing, Communities and Local Government (MHCLG) launched an independent review into the arrangements in place to support the transparency and quality of local authority financial reporting and external audit. The Secretary of State appointed **Sir Tony Redmond** to conduct this review.

3.3 The Redmond Review was tasked with examining the existing **purpose**, **scope** and **quality** of statutory audits of local authorities in England and the supporting regulatory framework to determine whether:

- It is operating in line with policy intent;
- The reforms introduced by the 2014 Act had improved the effectiveness of the control and governance framework along with the transparency of financial information presented by councils;
- The current statutory framework for local authority financial reporting supports the transparent disclosure of financial performance and enables users of the accounts to hold local authorities to account.

3.4 The conclusions and proposals from this review were published on **8 September 2020**. The full report is appended, but the following paragraphs provide a summary of the key findings and recommendations.

4. Redmond Review findings

Direction and regulation of local audit

4.1 Currently there are a range of different entities with a statutory role in overseeing and/or regulating elements of the local authority accounting and audit framework:

- **Public Sector Auditor Appointments Ltd** (PSAA) – is the appointing body for 98% of local authority audits because virtually all local authorities opted into using its services. It has responsibility for management of the contracts.
- **Comptroller and Auditor General** (C&AG) **/ National Audit Office** (NAO) – sets the Code of Local Audit Practice.
- **Financial Reporting Council** (FRC) - sets standards and guidance for auditors and monitors the quality of larger local authority audits.
- **Institute of Chartered Accountants in England and Wales** (ICAEW) – responsible for registration of local authority Key Audit Partners and audit firms and for quality monitoring of smaller local authority audits.
- **Chartered Institute of Public Finance and Accountancy** (CIPFA) – sets the Code of Local Authority Accounting Practice and other statutory Codes and produces sector specific good practice guidance.

- **Ministry of Housing, Communities and Local Government** (MHCLG) – has policy responsibility for the effectiveness of the local authority audit and governance framework. It also has the power to change the system and to intervene directly in a failing local authority.

4.2 None of these entities has a statutory responsibility to make sure that the framework operates in a coherent manner. The Redmond Review concluded that this lack of coordination and leadership is a significant weakness in the current framework.

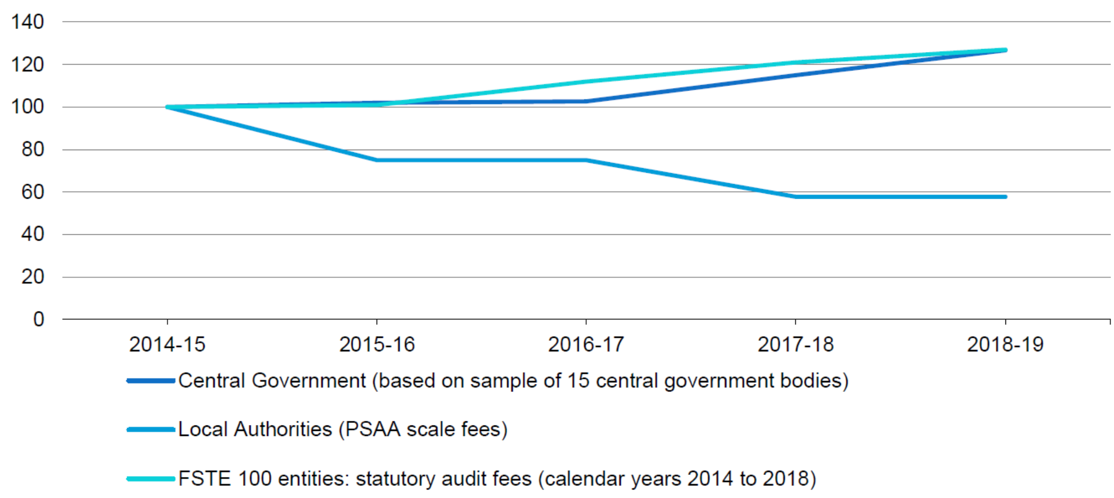
Procurement of local audit

4.3 Both the audit firms and their key audit partners need to be approved by the ICAEW to undertake local authority audits. A prerequisite to entry is recent experience of undertaking local authority audits.

4.4 When the PSAA ran a procurement in 2017, to appoint local authority auditors for the period 2018/19 to 2022/23, there were **9** firms registered with the ICAEW to undertake these audits, with a total of **96** key audit partners able to issue an audit opinion. Of the **9** firms registered to undertake these audits, only **5** were awarded contracts by the PSAA, with **67** key audit partners able to issue audit opinions (a **13%** reduction from the number of key audit partners under the previous contracts).

4.5 Audit fees in the local authority sector have dropped significantly since the Audit Commission was abolished, while audit fees in other sectors have risen.

Sector by sector comparison of change in audit fees over time



4.6 The scale fee paid by individual local authorities under the contracts let by the PSAA in 2017 were set with reference to the fees allocated to individual authorities when the Audit Commission let the 2012 and 2014 audit contracts. The PSAA did not seek to assess the amount it would cost to audit each local authority based on their level of audit risk in the past ten years.

4.7 As the scale fees have fallen, there has been an increasing prevalence of auditors requesting fee variations over the same period. The PSAA asked all firms active in the market to estimate the additional scale fee required to ensure that current quality standards are satisfied. Four audit firms suggested that increases of between **15%** to **25%** are required, and the fifth firm suggesting an increase of **100%** is needed.

Audit performance

4.8 Auditors of local authorities provide two audit opinions:

- A **financial audit opinion** which aims to confirm that the financial statements are free from material error and are properly prepared in accordance with the relevant accounting and legislative framework.
- An opinion on the effectiveness of the systems in place to meet the best value duty (referred to as the **value for money** conclusion).

The Review concluded that coverage of these audits is far narrower that many stakeholders expect.

4.9 The Review considered the extent to which auditors of local authorities:

- Meet **contract specifications** in respect of the financial audit opinion and value for money conclusion.
- Demonstrate **sufficient understanding** of the local authority environment through identification and testing of key financial audit and value for money risks.
- Deliver audits in a **cost-effective** way.
- Make **balanced** and **considered recommendations**.
- Issue reports and recommendations in a **timely manager**.

4.10 Although the Review concluded that external auditors were meeting the contract specification by delivering audits that, for the most part, meet relevant quality standards, an increasing number of audits are not being completed by the statutory deadline for publishing audited accounts. In 2018/19, only **57%** of opinions were issued by the statutory publication deadline, compared to **95%** in 2016/17. For the first time in 2019/20, having insufficient qualified individuals to deliver the audits at the appropriate time is being given as the reason for some of the delays.

4.11 There is some evidence that the reduction in audit fees referred to above, combined with the accelerated timetable for publication of audited accounts introduced in 2017/18, has led to a decline in the number of auditors with appropriate skills, knowledge and expertise. Indeed, many local authorities reported concerns about:

- Auditors not having a full understanding of how local authorities are funded and how this impacts the accounts;
- A lack of continuity in members of the audit team; and

- A lack of understanding of local authority specific financial statements.

4.12 Underpinning concerns about audit performance is auditor focus. There is a perception amongst many local authorities that an increasing amount of time is spent auditing fixed asset and pension valuations. What is less clear is the extent to which this has led to a reduction in audit work in other areas, but given the reduction in audit fees, it is likely to have had some impact.

4.13 The Review found it harder to assess audit performance in relation to VFM engagements as auditors have more discretion about the amount of work they need to undertake before forming their VFM opinion. However, the squeeze in audit fees and the reduction in the number of auditors with appropriate skills, knowledge and expertise, is a matter of significant concern.

4.14 Auditors can issue recommendations to management through their end of audit communications. However, the Review found that number of recommendations issued has declined year on year. Most of the recommendation that were issued related to technical accounting issues rather than financial control or value for money matters, contributing to the perception that the process is not adding as much value as previously.

Governance arrangements in place for responding to audit recommendations

4.15 The Review commented that effectiveness of audit must, in part, be determined by the arrangements in place within local authorities for considering and acting upon external audit reports. All local authorities are required to set up Audit Committees or the equivalent, with responsibility for considering the annual accounts and receiving internal and external audit plans and reports and for providing independent challenge in respect of accountability and risk management arrangements.

4.16 The Review concluded that:

- That it is rare for Audit Committees to put a substantive item onto the Full Council's agenda.
- 56% of audit committees have no independent members.
- Frequency of attendance at Audit Committees by statutory officers (Chief Executive, Monitoring Officer and Chief Financial Officer) is mixed.
- The scope of most audit committees covers the majority of the items in the CIPFA position statement and supporting guidance on Audit Committees, but not all. There were two areas which either had minimal or no specific coverage: partnership governance and value for money and best value.

4.17 With regard to the external auditor's work, the Review concluded that:

- The content of the standard suite of external audit reports is mandated by auditing standards, making them highly technical.

- External auditors should report to Full Council on risks identified and conclusions reached in a transparent and understandable format.

Audit work on the financial resilience of local authorities

4.18 External auditors do not currently have a specific responsibility to provide an opinion on whether a local authority is financially sustainable, although are required to:

- consider whether a local authority is a going concern; and
- assess the adequacy of its arrangements to secure value for money in its use of resources.

4.19 CIPFA has attempted to define financial resilience in its:

- Financial Management Code (FM Code)
- Pillars of Financial Resilience

However, these do not have statutory backing. Neither do they explicitly cover the impact of commercialisation on an authority's financial resilience.

4.20 The Review concluded that scope of the external audit should include a substantive test of a local authority's financial resilience and sustainability.

4.21 The new NAO Code of Audit Practice will require auditors to provide a narrative statement on Councils' value for money arrangements rather than a binary opinion. This should provide more useful information to stakeholders.

4.22 Auditors should use the indicators of financial stress in the CIPFA 'Pillars of Financial Resilience' and critically evaluate the Chief Financial Officer's Section 25 reports on the robustness of the Council's budget estimates and the adequacy of its reserves, other statutory reports and management estimates to inform their view of an authority's financial resilience.

Financial reporting in local government

4.23 Local authorities are required to have regard to the statutory Code of Local Authority Accounting Practice issued by CIPFA. This Code is based on private sector accounting standards, adapted for the specific circumstances of local authorities and overridden by specific statutory provisions.

4.24 Local authority accounts are lengthy and complex. This is primarily because there is a difference between the budget analysis of information for council tax purposes and the statutory basis of year end accounts.

4.25 An issue related to the complexity of local authority accounts is the capacity of external auditors to validate technical accounting treatments without a familiarity with local authority finance and accounting. Auditors have also argued that local authorities do not always have accounting staff with relevant technical expertise either.

4.26 The Redmond Review identifies three broad options for enhancing the transparency and usefulness of local authority financial statements:

- Review of International Financial Reporting Standards (IFRS) as a basis for preparing the Accounts.
- Expand and standardise the current narrative statement.
- Introduce a new summary statement presented alongside the IFRS based accounts, prepared on a budget setting basis.

A new summary statement is favoured, but this would need to reconcile to the statutory accounts and be subject to external audit to have credibility.

Conclusions of the Redmond Review

4.27 The current local audit arrangements fail to deliver the policy objectives underpinning the 2014 Act.

4.28 The local audit market is vulnerable, and evidence suggests that audit fees are at least 25% lower than is required to fulfil the local audit requirements effectively.

4.29 A weakness of the current arrangements is that there is no coordination and regulation of local audit activity. This role is best discharged by a single overarching body.

4.30 There is a potential weakness in the way in which audit outcomes are considered and presented to both the local authority and to the public.

4.31 There is a compelling argument to extend the scope of audits to include a substantive test of financial resilience and sustainability.

4.32 In scrutinising financial sustainability, the auditor should assess the risks identified in the Chief Financial Officer's annual report on the budget and review of compliance with the CIPFA Financial Management Code.

4.33 The technical complexity of the Accounts means that service users and council taxpayers are unable to understand them. Transparency and consistency could be improved through production of a simplified statement of service information and costs that compares budgeted with actual financial performance.

5. Redmond Review recommendations

Direction and regulation of local audit

5.1 A new body, the **Office of Local Audit and Regulation** (OLAR), be created to manage, oversee and regulate local audit, with the following key responsibilities:

- Procurement of local audit contracts
- Producing annual reports summarising the state of local audit
- Management of local audit contracts
- Monitoring and review of local audit performance
- Determining the Code of Local Audit Practice
- Regulating the local audit sector.

5.2 A liaison committee should be established, comprising key stakeholders and chaired by MHCLG, to receive reports from the new regulator on the development of local audit.

Procurement of local audit

5.3 The current fee structure for local audit to be revised to ensure that adequate resources are deployed to meet the full extent of local audit requirements.

5.4 Statute to be revised so that audit firms with the requisite capacity, skills and experience are not excluded from bidding for local audit work.

Audit performance

5.5 All auditors engaged in local audit to be provided with the requisite skills and training to audit a local authority, irrespective of seniority.

5.6 Quality is to be consistent with the highest standards of audit within the revised fee structure.

5.7 In cases where there are serious or persistent breaches of expected quality standards, OLAR has the scope to apply proportionate sanctions.

5.8 External Audit recognises that Internal Audit work can be a key support in appropriate circumstances where consistent with the Code of Audit Practice.

5.9 Deadline for publishing audited accounts to be revisited with a view to extending it from 31 July to 30 September (subject to consultation with Health bodies).

Governance arrangements in place for responding to audit recommendations

5.10 An annual report should be submitted to full Council by the external auditor after 30th September each year, irrespective of whether the accounts have been certified (OLAR to decide the framework for this report).

5.11 Consideration should be given to the appointment of at least one independent member, suitably qualified, to the Audit Committee.

5.12 The facility for the Chief Executive Officer, Monitoring Officer and Chief Financial Officer to meet with the Key Audit Partner at least annually should be formalised.

Audit work on the financial resilience of local authorities

5.13 MHCLG reviews its current framework for seeking assurance that financial sustainability in each local authority in England is maintained.

5.14 Key concerns relating to service and financial viability should be shared between Local Auditors and Inspectorates including Ofsted and the CQC prior to completion of the external auditor's Annual Report.

5.15 The changes implemented on the 2020 Audit Code of Practice are endorsed; OLAR to undertake a post implementation review to assess whether these changes have led to more effective external audit consideration of financial resilience and value for money matters.

Financial reporting in local government

5.16 A standardised statement of service information and costs be prepared by each authority and be compared with the budget agreed to support the Council tax / precept / levy and presented alongside the statutory accounts. The standardised statement should be subject to external audit.

5.17 The optimum means of communicating such information to council taxpayers / service users be considered by each local authority to ensure access for all sections of the communities.

5.18 CIPFA / LASAAC are required to review the statutory accounts, in the light of the new requirement to prepare the standardised statement, to determine whether there is scope to simplify the presentation of local authority accounts by removing disclosures that may no longer be considered to be necessary.

6. Financial Implications

6.1 The fee payable by the Council for external audit services carried out by our appointed auditor for the 2019/20 financial year is estimated at **£138,000**. It is possible that this fee will be significantly higher in subsequent years, because of changes arising from the Redmond Review. An increase of at least **25%** is suggested; an increase of this magnitude would add an additional **£35,000** to the annual audit fee currently payable by the Council.

6.2 Officer time required to support the external audit process may increase as a consequence of a change in depth, scope and extension of the timetable for the external audit.

6.3 There may be a cost associated with appointing an independent Audit Committee member and of additional training for Audit Committee members.

7. Legal Implications

7.1 The recommendations in the review may lead to a change in the law as it applies to this Committee. Although we cannot know what any changes in the law may be, it is open for the Council to take steps to implement the three recommendations to local authorities (see paragraphs 5.10-5.12 of the report) and the recommendations in this report ask the Committee to implement them

8. Appendices and background papers

8.1 Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting.

Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting

Sir Tony Redmond
September 2020

This document/publication is also available on our website at www.gov.uk/mhclg

If you have any enquiries regarding this document/publication, complete the form at http://forms.communities.gov.uk/ or write to us at:

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September 2020

The Rt Hon Robert Jenrick MP

Secretary of State for Housing, Communities and Local Government
Ministry of Housing, Communities & Local Government
2 Marsham Street
London, SW1P 4DF

Dear Secretary of State,

In June 2019, I was asked to undertake an independent review of the effectiveness of local audit and the transparency of local authority financial reporting. I am grateful for the opportunity given to me by ministers to conduct this Review. Whilst conducting the Review my guiding principles have been accountability and transparency. How are local authorities accountable to service users and taxpayers and how are auditors accountable for the quality of their work; and how easy is it for those same individuals to understand how their local authority has performed and what assurance they can take from external audit work.

This report sets out my conclusions. It makes detailed proposals for a new organisation with the clarity of mission and purpose to act as the system leader for the local audit framework; and for a standardised statement of service information and costs, compared to the annual budget, that is aimed at taxpayers and service users.

As I conducted my work, it became clear that the local audit market is very fragile. The current fee structure does not enable auditors to fulfil the role in an entirely satisfactory way. With 40% of audits failing to meet the required deadline for report in 2018/19, this signals a serious weakness in the ability of auditors to comply with their contractual obligations. In addition, the ambition of attracting new audit firms to the local authority market has not been realised. Without prompt action to implement my recommendations, there is a significant risk that the firms currently holding local audit contracts will withdraw from the market.

It will be possible to achieve part, but only part, of what needs to be done without legislation. However, it is important to emphasise that to fully achieve the vision set out in the Review, primary legislation will be essential. Only this can give the new organisation the tools it needs to do its job and to rebuild the sustainability of the local audit market.

I should like to thank:

- First, all those stakeholders who have engaged with the Review and responded to the Review's Call for Views;
- Second, the excellent team which has supported the Review's work: Ollie Hulme, Joe Pilgrim, Beth Addison and Gareth Caller; and
- Third, all the members of the Review's advisory group: Lynn Pamment, Maggie McGhee, Professor Laurence Ferry, Catherine Frances, Vicky Rock, Richard Hornby and Mark Holmes. This formidable group provided much wise guidance and counsel, as well as lively challenge and debate, for which I am hugely grateful.

Responsibility for the Review's conclusions and recommendations, is however, mine and mine alone.

Sir Tony Redmond

Sir Tony Redmond

Contents

Executive Summary

- This Review has examined the effectiveness of local audit and its ability to demonstrate accountability for audit performance to the public. It has also considered whether the current means of reporting the Authority's annual accounts enables the public to understand this financial information and receive the appropriate assurance that the finances of the authority are sound. It is important to note that this Review encompasses not only principal local authorities but also PCCs, Fire and Rescue Authorities, Parish Councils and Meetings and Drainage Boards.

- The Review has received 156 responses to the Calls for Views and carried out more than 100 interviews. Serious concerns have been expressed regarding the state of the local audit market and the ultimate effectiveness of the work undertaken by audit firms. This is not to say that the audits are carried out unprofessionally but there remains a question of whether such audit reports deliver full assurance on the financial sustainability and value for money of every authority subject to audit. A particular feature of the evidence submitted relates to concern about the balance of price and quality in the structure of audit contracts.

- A regular occurrence in the responses to the calls for views suggests that the current fee structure does not enable auditors to fulfil the role in an entirely satisfactory way. To address this concern an increase in fees must be a consideration. With 40% of audits failing to meet the required deadline for report in 2018/19, this signals a serious weakness in the ability of auditors to comply with their contractual obligations. The current deadline should be reviewed. A revised date of 30 September gathered considerable support amongst respondents who expressed concern about this current problem. This only in part addresses the quality problem. The underlying feature of the existing framework is the absence of a body to coordinate all stages of the audit process. Although there is some scope to effect alterations to the individual roles, appropriately fulfilled with the existing framework, this would not achieve the overriding objective of providing a coherent local audit function which offers assurance to stakeholders and the public in terms of performance and accountability of the local authority and the auditor.

- Consequently, a key recommendation is to create a new regulatory body responsible for procurement, contract management, regulation, and oversight of local audit. It is recognised that the new body will liaise with the Financial Reporting Council (FRC) with regard to its role in setting auditing standards. The engagement of audit firms to perform the local audit role would be accompanied by a new price/quality regime to ensure that audits were performed by auditors who possessed the skills, expertise and experience necessary to fulfil the audit of local authorities. These auditors would be held accountable for performance by the new regulator, underpinned by the updated code of local audit practice. A further recommendation is to formalise the engagement between local audit and Inspectorates to share findings which might have relevance to the bodies concerned.

- The Regulator would be supported by a Liaison Committee comprising key stakeholders and chaired by the Ministry of Housing, Communities and Local Government (MHCLG). The new regulatory body would be small and focused and would not represent a body which has the same or similar features as the Audit Commission.

- The report recognises that local audit is subject to less critical findings in respect of audit procurement and quality relating to smaller authorities. However, the recommendations include a review by Smaller Authorities' Audit Appointments (SAAA) of current arrangements relating to the proportionality of small authority audits together with the process for managing vexatious complaints where issues have been raised by those bodies which have experienced such challenges.

- Governance in respect of the consideration and management of audit reports by authorities has also been examined in considerable detail. Based on evidence presented, there is merit in authorities examining the composition of Audit Committees in order to ensure that the required knowledge and expertise are always present when considering reports, together with the requirement that at least an annual audit report to be submitted to Full Council. This demonstrates transparency and accountability from a public perspective which is currently lacking in many authorities.

- The issue of transparency is of equal relevance to the current presentation and publication of the annual accounts. Given that the feedback from practitioners and other key stakeholders revealed that current statutory accounts prepared by local authorities are considered to be impenetrable to the public, it is recommended that a simplified statement of service information and costs is prepared by each local authority in such a way as to enable comparison with the annual budget and council tax set for the year. This would enable Council taxpayers and service users to judge the performance of the local authority for each year of account. The new statement would be prepared in addition to the statutory accounts, which could be simplified. All means of communicating such information should be explored to achieve access to all communities.

- The outcome of this Review is designed to deliver a new framework for effective local audit and an annual financial statement which enables all stakeholders to hold local authorities to account for their performance together with a robust and effective audit reporting regime.

- Aside from the additional costs arising from a fee increase, the resource implications of the new regulatory body would amount to approximately £5m per annum after taking into account the amount related to staff subject to transfer under the TUPE arrangements.

- Implementation of recommendations contained in this Review would, in part, require regulatory or legislative change but it is important to note that many of the issues identified in this report require urgent attention, given the current concerns about local audit demonstrated in this Review.

Recommendations

The recommendations of this Review are as follows:

External Audit Regulation

1. A new body, the Office of Local Audit and Regulation (OLAR), be created to manage, oversee and regulate local audit with the following key responsibilities:
    - procurement of local audit contracts;
    - producing annual reports summarising the state of local audit;
    - management of local audit contracts;
    - monitoring and review of local audit performance;
    - determining the code of local audit practice; and
    - regulating the local audit sector.

2. The current roles and responsibilities relating to local audit discharged by the:
    - Public Sector Audit Appointments (PSAA);
    - Institute of Chartered Accountants in England and Wales (ICAEW);
    - FRC/ARGA; and
    - The Comptroller and Auditor General (C&AG)

    to be transferred to the OLAR.

3. A Liaison Committee be established comprising key stakeholders and chaired by MHCLG, to receive reports from the new regulator on the development of local audit.

4. The governance arrangements within local authorities be reviewed by local councils with the purpose of:
    - an annual report being submitted to Full Council by the external auditor;
    - consideration being given to the appointment of at least one independent member, suitably qualified, to the Audit Committee; and
    - formalising the facility for the CEO, Monitoring Officer and Chief Financial Officer (CFO) to meet with the Key Audit Partner at least annually.

5. All auditors engaged in local audit be provided with the requisite skills and training to audit a local authority irrespective of seniority.

6. The current fee structure for local audit be revised to ensure that adequate resources are deployed to meet the full extent of local audit requirements.

7. That quality be consistent with the highest standards of audit within the revised fee structure. In cases where there are serious or persistent breaches of expected quality standards, OLAR has the scope to apply proportionate sanctions.

8. Statute be revised so that audit firms with the requisite capacity, skills and experience are not excluded from bidding for local audit work.

9. External Audit recognises that Internal Audit work can be a key support in appropriate circumstances where consistent with the Code of Audit Practice.

10. The deadline for publishing audited local authority accounts be revisited with a view to extending it to 30 September from 31 July each year.

11. The revised deadline for publication of audited local authority accounts be considered in consultation with NHSI(E) and DHSC, given that audit firms use the same auditors on both Local Government and Health final accounts work.

12. The external auditor be required to present an Annual Audit Report to the first Full Council meeting after 30 September each year, irrespective of whether the accounts have been certified; OLAR to decide the framework for this report.

13. The changes implemented in the 2020 Audit Code of Practice are endorsed; OLAR to undertake a post implementation review to assess whether these changes have led to more effective external audit consideration of financial resilience and value for money matters.

Smaller Authorities Audit Regulation

14. SAAA considers whether the current level of external audit work commissioned for Parish Councils, Parish Meetings and Internal Drainage Boards (IDBs) and Other Smaller Authorities is proportionate to the nature and size of such organisations.

15. SAAA and OLAR examine the current arrangements for increasing audit activities and fees if a body's turnover exceeds £6.5m.

16. SAAA reviews the current arrangements, with auditors, for managing the resource implications for persistent and vexatious complaints against Parish Councils.

Financial Resilience of local authorities

17. MHCLG reviews its current framework for seeking assurance that financial sustainability in each local authority in England is maintained.

18. Key concerns relating to service and financial viability be shared between Local Auditors and Inspectorates including Ofsted, Care Quality Commission and HMICFRS prior to completion of the external auditor's Annual Report.

Transparency of Financial Reporting

19. A standardised statement of service information and costs be prepared by each authority and be compared with the budget agreed to support the council tax/precept/levy and presented alongside the statutory accounts.

20. The standardised statement should be subject to external audit.

21. The optimum means of communicating such information to council taxpayers/service users be considered by each local authority to ensure access for all sections of the communities.

22. CIPFA/LASAAC be required to review the statutory accounts, in the light of the new requirement to prepare the standardised statement, to determine whether there is scope

to simplify the presentation of local authority accounts by removing disclosures that may no longer be considered to be necessary.

23. JPAG be required to review the Annual Governance and Accountability Return (AGAR) prepared by smaller authorities to see if it can be made more transparent to readers. In doing so the following principles should be considered:
    - Whether "Section 2 – the Accounting Statements" should be moved to the first page of the AGAR so that it is more prominent to readers;
    - Whether budgetary information along with the variance between outturn and budget should be included in the Accounting Statements; and
    - Whether the explanation of variances provided by the authority to the auditor should be disclosed in the AGAR as part of the Accounting Statements.

1. Introduction

1.1 The Local Audit and Accountability Act 2014 (the 2014 Act) introduced a new Audit regime for local government to replace the previous arrangements, under which the Audit Commission performed that role. This Review examines the effectiveness of local audit as now practised.

1.2 The purpose of the Review is to test not only the impact of external audit activity in local government but also to look, critically, at how this helps to demonstrate public accountability, particularly to service users and council taxpayers. In a similar context the brief of the Review extends to the issues of transparency in financial reporting of local authorities, with attention being directed towards whether the annual accounts and associated published financial information can be readily understood by the public.

1.3 The framework for local audit encompasses procurement, contract management and delivery, the code of audit practice and regulation and accountability for performance. All of these aspects of local audit have been examined in depth. Whilst the focus of this Review is on local audit and public accountability there are a number of related factors which have contributed to the shape and nature of the findings. Such matters include: the breadth and complexity of International Financial Reporting Standards (IFRS); the role of the sponsoring department (MHCLG); and the current state of the local audit market. Local authorities include Councils, Police and Crime Commissioners (PCCs), Fire and Rescue Authorities (FRAs), and National Parks Authorities. NHS bodies are not local authorities and are outside the scope of this Review.

1.4 It is also important to emphasise that the Review includes the functions of Police and Fire Services as well as Parish Councils and Drainage Boards and due regard has been paid to the specific requirements of these bodies, as appropriate.

1.5 Substantial evidence has been collated from the ‘Call for Views’ and individual stakeholder meetings and this has formed the basis of the Report’s findings. The co-operation received from all interested parties including local government practitioners, audit firms, professional accounting bodies, academia and the media and the general public has been much appreciated. All parties who have participated in the Review share a desire to ensure local audit is effective and that public accountability is seen to be achieved. The approach to the Review has sought to harness those valuable contributions.

1.6 Attention has been paid to the findings of the Brydon and Kingman Reviews as well as the study carried out by the Competition and Markets Authority (CMA). Each of these reviews offers an insight into the principles and practices of auditors in the corporate sector, which have relevance to the public sector, including local government.

1.7 While testing the quality of outcomes has been a key feature of this approach, attention has been directed towards the governance arrangements in the way in which audit reports are managed and reported. The focus here has been on the level of public awareness of audit findings. Current practices relating to the annual publication of financial information have also been reviewed with an emphasis on the transparency, access and intelligibility of such reports.

1.8 In examining options for change to the current local audit arrangements, account has also been taken of the potential resource implications of any new initiative or development contained in the recommendations.

Sir Tony Redmond

Sir Tony Redmond

2. The direction and regulation of local audit

2.1 Introduction

2.1.1 The direction and regulation of local audit must be structured as to enable public accountability to be served. Each stage of the local audit process must adhere to this and remain consistent throughout. Ultimately, the direction and regulation of audit must be coherent, consistent in quality monitoring and fulfil the public accountability principle. The test, therefore, is whether the current arrangements deliver that, or can be altered to achieve that, or whether a new structure for the local audit regulatory framework needs to be put in place.

2.1.2 Public Interest Reports may be seen as relating to the local community's serious concern, but these are rarely used. In any event, council taxpayers are entitled to know the outcome of the annual statutory audit whether it be positive or negative.

2.2 Overview of the Regulatory Framework

2.2.1 The 2014 Act split the responsibilities formerly carried out by the Audit Commission between a range of bodies. **Figure 2.1** summarises the entities that have a significant role or influence on the accounting, audit and governance framework within which local authorities operate.

2.2.2 Currently there are six different entities with a statutory role in overseeing and/or regulating elements of the local authority accounting and audit framework. This framework is further complicated by the fact that different elements apply to different sectors. The elements of the audit framework undertaken by the C&AG, FRC and the ICAEW apply jointly to the local authorities and NHS bodies in England. However, whereas PSAA is the appointing body for 98% of local authority audits, NHS bodies do not have an appointing body and as such appoint their own auditors. By comparison the accounting framework applies to local authorities in England, Scotland, Wales and Northern Ireland, but not to the NHS.

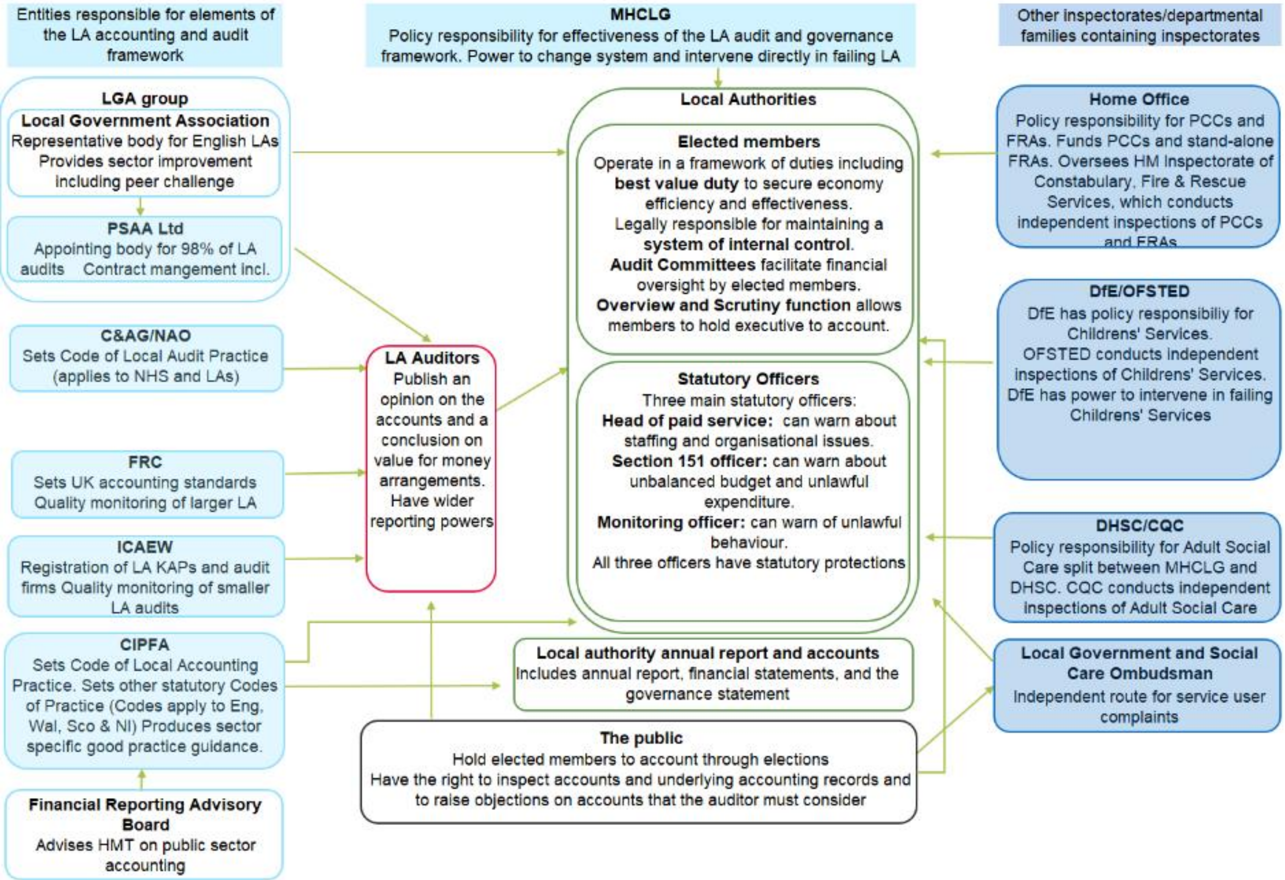
2.2.3 Another challenge is that the local authority sector is not the main focus for some of the regulatory bodies; specifically:

- The C&AG and National Audit Office's (NAO's) responsibilities relate mainly to holding central government departments to account on behalf of Parliament.
- The vast majority of the FRC's and the ICAEW's work relates to the private sector, and in the FRC's case, to regulating the audit and corporate governance arrangements within listed companies known as Public Interest Entities ("PIEs").

2.2.4 Finally, none of the six entities with responsibility for the different elements of the framework has a statutory responsibility, either to act as a system leader or to make sure that the framework operates in a joined-up and coherent manner. Although various ad hoc forums have been set up to share information, it is not clear how the membership and remit of these has been agreed. As a result, the lack of co-ordination and the lack of a system leader is widely recognised as a weakness in the framework by most of the stakeholder groups.

Figure 2.1

The Local Authority Governance, Audit and Accounting Framework 2018-19



Notes
1. Adapted from Figure 1 in NAO report *Local Authority Governance* (Jan 2019)
2. There are other statutory officers in local authorities, but between them, the three listed have overall responsibility for effective goverance
3. Arrows show the influences on local authority governance arrangements
4. In a Police and Crime Commissioner or Fire and Rescue Authority, the Commissioner is the sole elected member; in a Mayoral Combined Authority, the mayor is the sole
5. Audit Committees are mandatory in PCCs, stand-alone FRAs and mayoral combined authorities. They are not mandatory for other LAs.
6. ICAS also has the power to act as a registering body for KAPs and audit firms. However, following mergers, no firms active in England are currently registered with ICAS.
7. MHCLG part funds the LGA's sector improvement work

2.3 Functions of the bodies responsible for the framework

PSAA Ltd

2.3.1 One of the original objectives behind the 2014 Act was to widen participation in the local audit market by allowing local authorities to appoint their own auditors. Once the Act had passed, it became clear that the auditor appointment provisions in the 2014 Act were onerous and there was little appetite amongst local authorities to appoint their own auditors. As a result, MHCLG ran a tender exercise to identify an entity which would act as an appointing person for local authority audits.

2.3.2 PSAA, a new company set up by the Local Government Association (LGA), was the only bidder and accordingly was designated as an appointing person under legislation. Under the transitional arrangements, PSAA was given the responsibility of managing the framework contracts let by the Audit Commission in 2012 and 2014, and during the period to 2017-18 producing a report summarising the results of local authority and NHS audits.

2.3.3 Category 1 Authorities[1] were given the choice of opting in or out of the PSAA arrangements. Most (currently 98%) chose to opt in.

2.3.4 In 2017 PSAA let the new local audit framework contracts, active from the 2018-19 financial year. PSAA's current responsibilities[2] are:

- To perform the functions of an appointing person for local authority audits;
- To take steps to ensure that public money is properly accounted for and protected;
- To oversee the delivery of consistent high quality and effective audit services; and
- To ensure effective management of audit contracts.

More detail on the contracting process and on audit quality is contained in **Chapters 3 and 4** respectively.

The C&AG and the NAO

2.3.5 The C&AG is responsible for laying the Code of Local Audit Practice in Parliament. The C&AG is supported in this work by a small Local Audit Code and Guidance (LACG) team, which is part of the NAO. The LACG team is responsible for the preparation, maintenance and publication of the C&AG's Code of Audit Practice and supporting guidance to auditors. LACG undertakes the full range of activities associated with these responsibilities including:

- providing a point of contact to address significant issues raised by auditors and other stakeholders that may require the update of the Code of Audit Practice or issuing guidance to auditors; and
- facilitating timely engagement with, and advice to, auditors and other stakeholders to facilitate consistency of approach on significant issues – for example, through convening and providing secretariat support to a Local Auditors Advisory Group.

2.3.6 The 2014 Act provides the C&AG with the power to issue guidance to auditors which may explain or supplement the provisions of the Code of Audit Practice. The Act requires auditors to have regard to such guidance. The NAO maintains a series of Auditor Guidance Notes (AGNs) to support auditors in their work and facilitate consistency of approach between auditors of the same types of entity. The 2015 Code is supplemented by seven AGNs. These apply equally across local government and the NHS. The AGN on value for money arrangements is supplemented by sector specific supporting information.

2.3.7 The 2014 Act gives the C&AG the responsibility for undertaking value for money investigations on local government. However, the C&AG does not have the power to make recommendations directly to local authorities. This means that when a value for money study finds that one or more local authorities have breached either the letter or the spirit of the statutory framework, the accompanying recommendations must be addressed to MHCLG or Treasury, if they relate to the Public Works Loan Board, as the responsible central government departments.

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[1] "Category 1 authority" means a relevant authority that either— (a) is not a smaller authority; or (b) is a smaller authority that has chosen to prepare its accounts for the purpose of a full audit in accordance with regulation 8 of the Smaller Authorities Regulations https://www.legislation.gov.uk/uksi/2015/234/pdfs/uksi_20150234_en.pdf

2.3.8 The main roles of the C&AG and the NAO are to support Parliament in holding government to account, through auditing the accounts of government departments and arms-length bodies and undertaking value for money investigations. When the NAO undertook the 2019 study on Local Authority Governance, which included work on local authority audit, the team did not include the Audit Code within the scope of the review. This was to avoid the risk of self-review. As a result, the findings of that report could not take account of an element of the governance framework.

The Financial Reporting Council

2.3.9 The FRC is responsible for issuing standards and guidance to auditors for use in the UK. The suite of standards is known as *International Standards on Auditing (UK)*, and apply equally to audits of local authorities and entities in other sectors.

2.3.10 During the transitional arrangements operating from 2015-16 to 2017-18, the FRC had no formal responsibility for assessing the quality of local authority audit. PSAA took the decision to contract the FRC to undertake six quality assurance reviews of local authority audits, with coverage of at least one from each firm. In practice, the FRC conducted quality assurance reviews of seven audits in both 2016-17 and in 2017-18. This is because the FRC's methodology requires them to re-review all audits that received an unsatisfactory quality assurance review score in the prior year. The results of these quality reviews are discussed in **Chapter 4**.

2.3.11 From 2018-19, the FRC has taken on statutory responsibility for quality assurance reviews of the 230 larger local authority audits. It treats the NHS and local government bodies as a single population and, to maintain equivalence with their coverage of the audit of PIEs, look to cover at least 5% of that population in each year. For 2018-19, the sample included 3 NHS bodies and 12 local authorities. Because some of the audits originally selected for quality review were not complete when the FRCs Audit Quality Review team conducted its fieldwork, these had to be replaced with other audits. The results of the 2018-19 quality assurance reviews are expected to be available in the Autumn of 2020.

2.3.12 The methodology adopted for quality assuring audits in local authority sector is broadly equivalent to that of the Public Interest Entities sector. The review team focuses on what is on the audit file and assesses the extent to which that complies with the applicable quality framework. The document review is supplemented by meetings with the audit team and the Chair of the Audit Committee.

2.3.13 Formal client communications are included within the scope of the quality review. However, ongoing liaison between auditors and local authorities would be assessed only if included on the audit file.

2.3.14 Unlike for PIE audits, the FRC does not have the power to fine audit firms if the quality of their local authority audits proves to be deficient. However, all of the firms active in the market indicated that they are very conscious of the reputational damage of a poor rating from the FRC for one of their local authority audits.

2.3.15 FRC is of the view that the perception that it focuses mainly on asset valuations understates the scope of their quality reviews. It also believes that if a focus on asset and pension valuations is inappropriate, this is the responsibility of the partnership between CIPFA (England, Northern Ireland and Wales) and the Local Authority (Scotland) Accounts Advisory Committee (LASAAC) known as CIPFA/LASAAC to resolve, through modifications to the Accounting Code.

2.3.16 The FRC is in the process of being reconstituted as the Audit Reporting and Governance Authority (ARGA) in line with the recommendations made in the Kingman Review. Sir Donald Brydon also recently published a report that made a number of recommendations to develop corporate auditing as a profession. As the FRC and the Department for Business, Energy & Industrial Strategy (BEIS) consider these recommendations, there is a risk of divergence between the focus and methodologies used to quality assure external audit engagements. Managing this interaction will require ongoing engagement.

ICAEW

2.3.17 The ICAEW has two statutory functions. Since 2015 it has been responsible for maintaining the register of audit firms and Key Audit Partners (KAP) authorised to sign off local authority audits; and since 2018-19 it has been responsible for quality assurance reviews of the 313 smaller local authority audits. The framework for approving firms and partners is tightly controlled by legislation.

2.3.18 Like the FRC, the ICAEW treats local authorities and NHS bodies as a single population for quality assurance review purposes. The 2018-19 quality assurance process is ongoing. ICAEW has selected 15 audits for quality assurance review, split roughly two thirds local government and one third health. The results of this quality assurance review process are not yet available.

2.3.19 Similarly to the FRC, the ICAEW quality assurance reviews focus on what is on the audit file and assesses the extent to which that complies with the applicable quality framework. The methodology used to assess the audits of English local authorities is the same as is used to assess audits undertaken by the Auditor General for Wales. This methodology does not require review teams to meet with Audit Committee chairs. As with the FRC, the ICAEW does not have any powers to fine or otherwise sanction auditors whose audits do not meet appropriate quality standards.

2.3.20 ICAEW and the FRC liaise to make sure that all audits fall within one or other of their sample populations and use, broadly, the same quality ratings. Both use well established methodologies to arrive at those ratings.

CIPFA

2.3.21 CIPFA has a dual role. It has been given the statutory responsibility for producing many of the finance related codes of practice that local authorities are required to observe. At the same time, it is a professional institute that represents the majority of accountants working in the local government sector, including most CFOs.

2.3.22 The Accounting Code is prepared by a small secretariat employed by CIPFA who report to the CIPFA/LASAAC Accounting Code Board ("CIPFA/LASAAC"). CIPFA/LASAAC is responsible for preparing, maintaining, developing and issuing the Code of Practice on Local Authority Accounting for the United Kingdom. Its membership primarily comprises accounts preparers representing the different types of authorities in England, Scotland, Wales and Northern Ireland, the Supreme Audit Institutions, and a representative of one of the external audit firms active in the sector in England. The FRC along with representatives of MHCLG and the Scottish, Welsh and Northern Irish governments have observer status on CIPFA/LASAAC.

2.3.23 In England CIPFA/LASAAC is supported by a CIPFA facilitated Local Authority Accounting Panel, which focuses on local government accounting and financial reporting issues and produces guidance for practitioners.

2.3.24 The Accounting Code could be characterised as long and complex. Part of the reason for this is the challenge of writing a Code that covers four countries, each of which has its individual statutory framework with a different set of statutory adjustments and disclosures. In addition to this, CIPFA has taken the decision to draft a highly prescriptive Code that provides detailed guidance on the correct accounting for each class of transactions. An alternative approach would be to draft a principles-based Code, which requires local authorities to comply with generally accepted accounting practice ("GAAP") and only provides detailed guidance where GAAP is adapted or interpreted, specifically for the local authority context. **Chapter 7** covers the accounting framework in more detail.

Assessment of whether an existing body could act as the system leader

2.3.25 The detailed analysis of the bodies responsible for the framework supports the conclusion reached in Sir John Kingman's Independent Review of the Financial Reporting Council:

"The structure is fragmented and piecemeal. Public sector specialist expertise is now dispersed around different bodies. The structure means also that no one body is looking for systemic problems, and there is no apparent co-ordination between parties to determine and act on emerging risks"[2]

2.3.26 The Kingman Review recommended that the fragmented structure be resolved by designating a single body as the system leader. When asked whether an existing body or a new body would be best placed to take on the role of a system leader, 82% of respondents expressed a preference for a single regulatory body. Many stakeholders who were interviewed also agreed. The other suggestions made were either that the C&AG or the FRC should take the role of system leader.

2.3.27 The C&AG clearly has the relevant experience and expertise to take on such a role. However, taking on responsibility for an element of a framework that is the policy responsibility of a government department could significantly increase the risk of a conflict of interest with the C&AG's main responsibility, which, as already stated, is to hold government departments to account on behalf of Parliament.

[2] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/767387/frc-independent-review-final-report.pdf

2.3.28 As the regulator for the audit profession in the UK, the FRC will continue to have an important role in setting standards for all external auditors, including those working in local public audit. However, the FRC's main focus is corporate sector external audit, and to be fully effective the system leader for local public audit will need to demonstrate detailed expertise and a clear focus on that sector.

2.4 Interactions with other inspectorates

2.4.1 There are a number of other inspectorates who cover the local authority sector. Ofsted and the CQC assess the effectiveness of children's services and adult social care respectively in authorities with those statutory responsibilities; HM Inspectorate of the Constabulary and Fire and Rescue Services (HMICFRS) undertakes independent inspections of PCCs and FRAs covering both service delivery and financial planning; the Local Government and Social Care Ombudsman (LGSCO) looks at individual complaints against councils, all adult social care providers in both public and private sector, FRAs, and some other organisations providing local public services; and the Independent Office for Police Conduct performs the same function for PCCs.

2.4.2 Evidence suggests that where a local authority receives an "Inadequate" rating for its children's services, the auditor as a general rule qualifies the value for money conclusion. For example; when PSAA published its summary report on the results of 2017-18 audit work, it listed 32 qualified Value for Money (VfM) opinions; half of these were due to an "inadequate" Ofsted rating[3]. The auditor's value for money conclusion remains qualified until a future Ofsted inspection finds that children's services are no longer "Inadequate". Local authorities questioned the benefits of including Ofsted judgements in the audit report. The circumstances supporting an "inadequate" Ofsted rating are fully explained in a detailed and publicly available report. In the light of this there is a question as to how qualifying the VfM opinion solely for this reason fully reflects the governance arrangements within the authority that could be brought to the attention of elected representatives and other key stakeholders. When asked whether a value for money opinion should be qualified solely because a local authority has received an inadequate Ofsted opinion or a similar opinion from another inspectorate, 97% of respondents thought that it should not. There is no evidence of reports by other inspectorates leading to modifications to the auditor's opinion.

2.4.3 We have been told by external audit firms and local authorities that external auditors utilise inspectorate reports on a case by case basis. There is little evidence of any additional dialogue between external audit and other inspectorates to discuss inspectorate reports or take into consideration any improvements that a local authority may have made since an inspectorate rating had been issued. This is a change from practice since prior to 2015, where external auditors and inspectorates liaised much more frequently. Whilst external audit firms were broadly in agreement that there should be engagement with inspectorates, many felt that the current arrangements were sufficient.

[3] Report on the results of auditor's work (Oct 2018) – list of qualified opinions will not include LAs where the 2017-18 audit was concluded after the PSAA report was published.

2.4.4 Whilst recognising that each inspectorate focuses on a different area, there is a question as to whether more liaison may add value. Many examples of service delivery and financial failures are underpinned by weaknesses in governance and senior leadership. Given this, it may be valuable for the auditor or an inspector that has concerns, to find out if those concerns are reflected in other areas of a local authority's business or indicative of wider financial resilience issues.

2.5 The role of MHCLG

2.5.1 The Ministry of Housing, Communities and Local Government (MCHLG) has a statutory role in regulating and monitoring the financing and service delivery of local government. The Accounting Officer within the Department has responsibility for overall expenditure control within local authorities given the funding regime under which the sector operates. In addition, he has policy responsibility for the effective operation of the local authority audit and accounting framework.

2.5.2 Support to the Accounting Officer in fulfilling these responsibilities is split between two directorates:

- Local Government Finance; and
- Local Government and Communities (formerly Local Government Policy)

Local Government Finance

2.5.3 This Directorate covers payments to local authorities through the grant system, has responsibility for business rates and council tax policy, oversees borrowing, capital and fiscal arrangements and is responsible for assessing the financial sustainability of local government. When a local authority experiences financial difficulty, it is the Local Government Finance Directorate that usually leads the government response. It also provides the MHCLG representation on CIPFA's accounting panels.

Local Government and Communities

2.5.4 This Directorate has overall responsibility for MHCLG's local government assurance framework as set out in the Accounting Officer's system statement. Regular advice is given to the Accounting Officer on whether the framework for which he is responsible is operating effectively.

2.5.5 The directorate includes a team that maintains a view of local authorities where concerns exist about financial resilience, service delivery or officer/member conduct issues. In appropriate circumstances this may lead to statutory interventions into local authorities or, alternatively, statutory support. Qualified audit opinions are considered a part of this view.

2.5.6 Another team has responsibility for the local audit policy framework, the 2014 Act and the Accounts and Regulations 2015, managing relationships with PSAA, SAAA, NAO, ICAEW, Institute of Chartered Accountants of Scotland (ICAS) and FRC insofar as their activities relate to the local audit framework and logging Public Interest Reports.

2.5.7 In 2014 the team responsible for local audit set up a Local Audit Delivery Board to support implementation of the 2014 Act. In 2018, it became the Local Audit Monitoring

Board, with revised terms of reference and expanded membership. The Board comprises representatives of relevant departments and framework bodies to facilitate sharing of information about the operation of the framework. This Board is a consultative body, that holds meetings in private and has no formal powers or remit.

2.5.8 In viewing these roles from a local authority perspective, it is clear that MHCLG provides a national oversight of the financing of local government, capital and revenue spending, accounting arrangements and financial resilience. This work is substantial and seeks to offer assurance regarding the financial stability of individual local authorities and it includes, within its brief, responsibility for testing adherence to legislation and regulations governing local audit.

2.5.9 The responsibility for regulating local audit sits elsewhere yet MHCLG has a key role in offering assurance about the financial health of local authorities. The intelligence network and information flow relating to accounting and audit reporting on financial sustainability should reach MHCLG in a structured, timely and coordinated fashion. Given the strategic roles that the Department and The Accounting Officer carry it is crucial that systems and procedures are in place to enable this to happen. Clarity, coherence and consistency in fulfilling the Department's role are key to helping to ensure effective local audit.

3. Procurement of local audit

3.1 Statutory framework and eligibility criteria

3.1.1 In order to bid for a local authority audit, both audit firms and every individual responsible for signing off an audit opinion, typically but not always a KAP, needs to be pre-approved either by ICAEW or ICAS. Eligibility criteria are set out in Schedule 5 to the 2014 Act. These criteria stipulate that it is impossible to bid for local authority audits unless both the firm and each nominated KAP has recent experience of undertaking local authority audits. It is difficult for new entrants to enter the local authority market as a consequence of these criteria as audit firms not currently in the market are unable to gain the relative knowledge and expertise that would be required to become a KAP.

3.1.2 Despite the high barriers to entry, since 2016 there has been a 7% increase in the number of KAPs eligible to sign off local authority Audits. Firms active in the market continue to register new KAPs. 39% of KAPs currently registered were not KAPs in 2016, with the firms with a smaller market share being responsible for much of this increase. However, the headline KAP figure is slightly misleading. The number of KAPs has declined by 13% once those who are working for firms who do not currently hold contracts with PSAA are excluded.

Figure 3.1

Number of Key Audit Partners registered with ICAEW

Firm	2016	2020
BDO	5	7
EY	13	16
GT	32	26
Mazars	4	10
KPMG	22	23
Deloitte	6	8
Total KAPs (Firms holding contracts with PSAA)	76*	67*
Cardens	0	1
Moore Stephens	2	0
PWC	12	9
Scott-Moncrieff	0	3
Total KAPs	96	103

** Deloitte did not hold any PSAA contracts in 2016. KMPG does not currently hold any PSAA contracts.*

3.1.3 There is a risk that the Competition and Markets Authority: Statutory Audit Services Market Study[4] recommendation to implement an operational split between the Big Four's audit and non-audit businesses, to ensure maximum focus on audit quality will further reduce the number of KAPs qualified to sign off local authority audits. KAPs may be responsible for a mixture of external audit, internal audit and consultancy engagements. If required to choose between specialisms, there is, of course, no guarantee that they will opt for external audit.

[4] See Annex 5 for a more detailed analysis of the potential impacts of the CMA, Kingman and Brydon recommendations for local audit.

3.2 The 2017 procurement process

3.2.1 As detailed in **Chapter 2**, PSAA took over the administration of the bulk audit contracts let by the Audit Commission in 2014. These ran from 2015-16 to 2017-18. They comprised five lots let on a regional basis. In 2017 PSAA ran a new procurement to contract for local authority audits for the period 2018-19 to 2022-23.

3.2.2 PSAA chose to split lots by market share rather than on a regional basis. The reason for this was a concern that some regions could prove less popular with bidders than others. They also checked for potential conflicts of interest. Five lots comprising between 40% and 5% of the total market were let, each for a period of five years. No firm could win more than one lot. A sixth lot with no guaranteed work was let, with the aim of providing some resilience in the market.

3.2.3 Local authorities were notified of the lot to which they had been allocated and were given the opportunity to request transfer to a different lot; for example, if they were in a shared service arrangement with an authority in a different lot. Seven local authorities asked for their audit to be transferred to a different lot. Five of these requests were accepted.

3.2.4 Of the nine firms registered to undertake local authority audits seven bid for one or more lots. One firm decided not to bid and a second was excluded from the bidding process by PSAA because it felt the firm was too small to have a realistic chance of submitting a competitive bid.

3.2.5 Assessment of audit firms was split 50:50 between price and quality, compared to the final Audit Commission procurement which was done on a price quality ratio of 60:40. The team assessing quality scores was not given sight of the price each firm had bid. In addition, PSAA asked an ex-District Auditor working for the LGA to quality assure the assessors' quality scores. The assessment of quality was based solely on the tender documents submitted. Past performance was not considered.

3.2.6 One of the firms bid at a much higher price point than the other firms. This generated such a low "price" score that it was effectively impossible for its quality score to make up sufficient difference to win a lot.

3.2.7 Although the headline quality price ratio was 50:50, as highlighted in **Figure 3.2**, many of the questions included in the quality score do not directly relate to factors impacting audit quality.

3.2.8 Four firms bid for the largest two lots (including the firm who priced themselves out of the market); and six for the remaining four lots. Each successful firm was eliminated from consideration for each smaller lot, leaving only two firms from which to choose when awarding Lot 5.

3.2.9 After excluding the firm that priced itself out of the market, the firms awarded the five contracts were those with the highest quality scores. The firm with the highest quality score won the largest lot; the second highest quality score the second highest lot; and there was a marginal difference between the quality scores for the other successful firms.

Figure 3.2: Audit Quality Questions – PSAA tender document

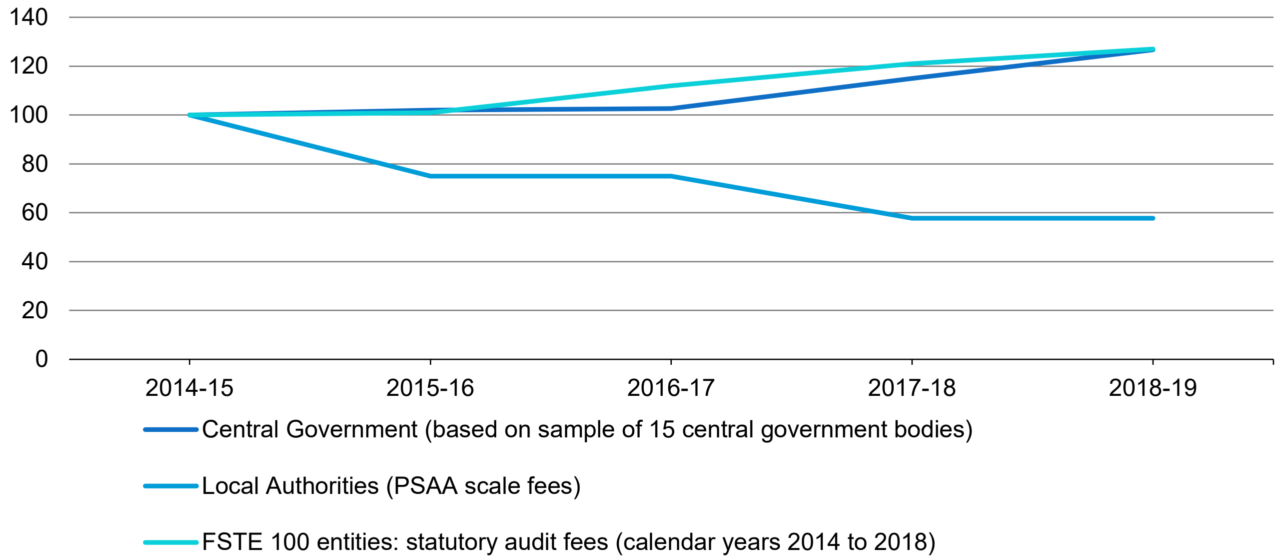
Question number	Question	Weighting	Maximum weighted score
1.1 and 1.2	Confirmation of information in SQ Response; and other declarations; Guarantee (if applicable) and completed, unqualified Form of Tender	N/A	N/A
2.1	Identifying and addressing risks and issues and engaging with different stakeholders	0.5	5
2.2	Continuing professional development	0.2	2
3.1	Providing a clearly articulated audit plan to address the risks identified, and arrangements for carrying out the planned work effectively	1	10
3.2	Information assurance	N/A	N/A
4.1	Quality assurance arrangements to ensure that local audits are undertaken to a consistently high standard	0.6	6
5.1	Schedule of staff	N/A	N/A
5.2	Details of resourcing	0.5	5
5.3	Details and role of Contact Partner	0.3	3
6.1	Selection of a team to work on an individual audit	0.5	5
6.2	Arrangements for discharging statutory reporting responsibilities under the Local Audit and Accountability Act 2014, managing authority and public expectations	0.4	4
7.1	Arrangements to ensure a smooth transition for audits of local government bodies transferring between audit firms	0.5	5
8.1	Opportunities to be commenced and completed	0.3	3
8.2	Other economic, social and environmental initiatives to be undertaken	0.2	2
Overall quality score			50
Price	Ranking of Bid Rate %	1	50%
Overall score (quality and price combined)			

Questions 2.1, 3.1 and 4.1 are direct indicators of quality.

3.2.10 Lot six was designed to provide spare capacity in the market. However, this has not worked as intended, in part because mergers mean that the firm that won Lot 6 no longer exists.

3.2.11 As demonstrated by **Figure 3.3**, audit fees in the local authority sector have dropped significantly at the same time that audit fees in other sectors have significantly risen. As well as the overall external audit fee paid by the sector declining in cash terms it has also dropped as a percentage of net current expenditure of local authorities, from 0.05% in 2014-15 to 0.04% in 2018-19. Within the sector there are further variations with PCCs and Local Authority Pension Funds typically paying much lower audit fees as a percentage of net expenditure than other types of local authorities.

Figure 3.3
Sector by sector comparison of change in audit fees over time



Notes

1 2014/15 base 100

3.3 Translating bids into audit fees paid by LAs

3.3.1 PSAA told the Review that the scale fee paid by individual LAs under the current contracts has been calculated by taking the total annual fee paid to external auditors under the contract and adding PSAA's margin; comparing the total amount paid to the total amount paid under the 2014 contracting process; and applying the percentage reduction in total amount paid equally across all local authority audits.

3.3.2 The Audit Commission adopted the same approach for allocating fees to individual local authorities when it let the 2012 and 2014 contracts. This means that no assessment of the amount it would cost to audit each local authority based on their level of audit risk has been made in the past ten years.

3.3.3 Since 2010, there have been changes to the major powers and duties of local authorities and to the business environment within which they operate. Individual local authorities will have been impacted by these changes to differing extents. As a result, there is no guarantee that the fee paid by each local authority accurately reflects the risk profile or amount of audit work required for their external audit.

3.3.4 88% of local authorities who responded to the Call for Views think that the current procurement process does not drive the right balance between cost reduction, quality of work, volume of external auditors and mix of staff undertaking the work.

3.3.5 Audit fees for those local authorities who have opted out of the PSAA arrangements have changed in a way similar to fees for those who have opted in.

3.4 Fee variations and contract management

3.4.1 When an auditor requests a fee variation, this must be agreed by PSAA[5]. In practice, PSAA may challenge fee variations by asking for more information from the firm but expects the auditor and the local authority to come to an agreement as to the additional fee to be paid. PSAA records and monitors this activity. It may also facilitate a conversation between the auditor and local authority in the case of disagreement.

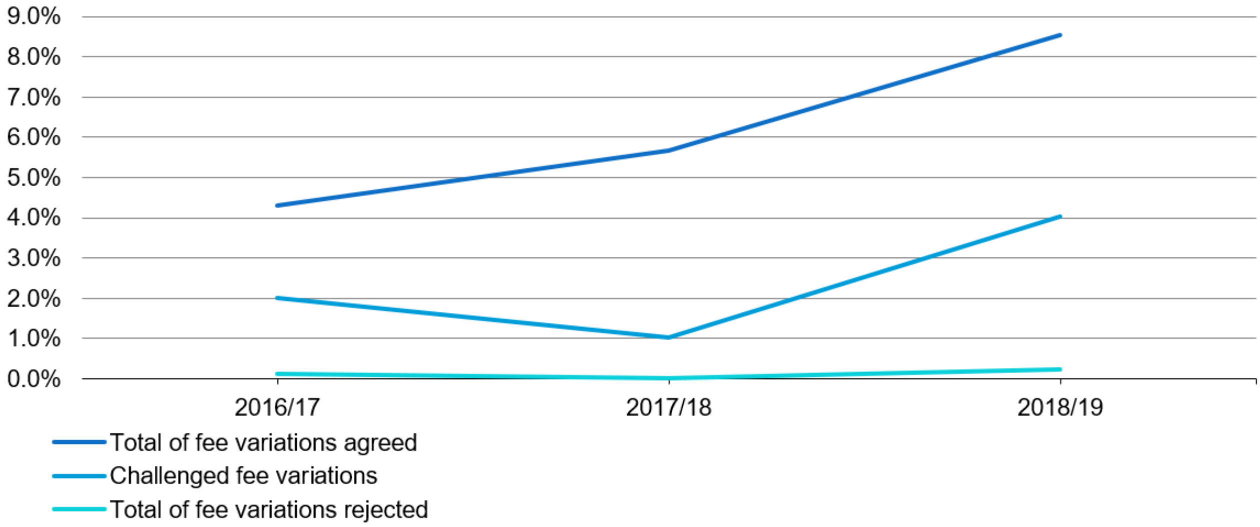
3.4.2 As demonstrated by **Figure 3.4** the number and size of fee variation requests have increased over time. Fee variation requests are often received some months after audits are completed, which means it is difficult to assess the true level of fees paid by the sector. As delayed audits are more likely to generate issues that require more work and thereby attract fee variations, and some firms are not always prompt in submitting fee variations, there are likely to be some requests outstanding relating to 2017-18 and 2018-19 audits.

3.4.3 Audit firms consider the fee variation process to be unsatisfactory. They have raised concerns that the scope to claim fee variations is not sufficient to meet their costs. Increasing the scale fee, to reflect changes in regulatory requirements is for practical purposes not possible under the current arrangements.

3.4.4 The majority of local authorities' representatives who offered a view on fee variations also considered them to be unsatisfactory. A concern, which has been raised by a not insignificant number of authorities, is the fact that fee variation requests are not always supported by any evidence of additional work done. Some local authorities passed examples to the Review of auditors, representing more than one audit firm, refusing to provide evidence to support a requested fee variation.

Figure 3.4

Fee variations as a percentage of total scale fees



Notes

1 Transitional arrangements in 2016-17 & 2017-18, PSAA contract in 2018-19.

2 Some fee variation requests for 2018-19 audits still to be received and agreed.

[5] https://www.psaa.co.uk/wp-content/uploads/2019/12/PSAA-fee-variation-process.pdf

3.4.5 Some local authorities questioned why they have been asked to join a call with a significant number of a firm's technical experts, most of whom do not contribute to the discussion, when they need to resolve technical accounting issues. They have questioned whether the costs of these calls are factored into later fee variation requests.

3.4.6 Fee variations can be submitted at any time which increases uncertainty for local authorities. In addition, some local authorities have claimed that they were led to believe by their auditors that they would refuse to sign off their accounts until they agreed a fee variation.

3.4.7 Finally, some authorities have also claimed that they are being asked to fund the costs of additional audit fieldwork because auditors have not resourced the planned audit visit properly and as a result, need to conduct additional audit testing. It has not been possible to assess whether this is happening or how widespread is the practice.

3.4.8 For the 2019-20 audit cycle, PSAA has taken steps to manage fee variations more proactively. Rather than wait for fee variations to be submitted, PSAA has asked all of the firms active in the market to estimate the additional fee required to ensure that their audit work and audit files meet current quality standards. Four of the firms have suggested that an increase of between 15% to 25% on the scale fee is required with the fifth firm requesting an increase of 100% on the scale fee. PSAA informed local authorities that it expects audit firms to provide fee variation information at the earliest possible opportunity, and that PSAA has emphasised this to the firms in its recent auditor communications. PSAA is currently in the process of reviewing how each firm's standard audit testing programmes have changed over the past three audit cycles to identify whether the increases requested are justified. PSAA will use this work to enable it to provide reassurance to audited bodies that extra work has been validated.

3.4.9 Some local authorities have suggested that PSAA has an incentive to approve fee variations as they are funded through making a margin on audit fees. This is not correct. Because PSAA calculates its margin on a total system cost, it is not possible for local authorities to calculate how much of each audit fee or fee variation is due to PSAA. However, as a not for profit company, PSAA has no incentive to claim more funding than it is entitled to. The company's Articles of Association requires PSAA to return surpluses to the sector. In late 2019, under the transitional arrangement, a distribution of the surplus funds of £3,500,000 (9.3% of the 17-18 scale fee £37.6m) was approved by the Board to be returned to the sector, apportioned between local authorities on a scale fee basis. This might be interpreted as an effective transfer of funds from LAs charged fee variations to those who have not been charged variations.

3.4.10 Some LAs have stated through interviews, that PSAA's role is opaque and that they feel that they have no route to challenge audit fees that they feel are unfair or to raise concerns relating to poor quality or delayed audits. The contract provides no mechanism for individual LAs to complain about the service they receive from their auditors.

3.4.11 PSAA states that its role as defined under statute does not include active contract management and it does not currently have the expertise to do so. However, in the *Local Audit (Appointing Person) Regulations 2015* the additional functions of appointing person include requirements to:

"monitor compliance by a local auditor against the contractual obligations in an audit contract… [and] resolve disputes or complaints from— (aa)local auditors, opted in authorities and local government electors relating to audit contracts and the carrying out of audit work by auditors it has appointed."[6]

3.4.12 During the transitional period implementing the new arrangements (2015-16 to 2017-18), there was a Memorandum of Understanding (MoU) between MHCLG and PSAA, which required PSAA to fulfil its statutory functions. When the MoU expired MHCLG did not renew it.

[6] https://www.legislation.gov.uk/ukdsi/2015/9780111126134

4. Audit performance

4.1 Introduction to local authority audit

4.1.1 Auditors of local authorities provide two audit opinions. These are:

- A financial audit opinion; and
- An opinion on the effectiveness of the systems in place to meet the best value duty (known as the 'value for money' opinion).

Scope of financial audit opinion

4.1.2 The purpose of a financial audit is to form an opinion on a set of financial statements. Financial audits are required to be conducted in accordance with International Standards on Auditing – UK (ISAs). The auditor is required to certify whether the financial statements are free from *material* misstatement and are properly prepared in accordance with the relevant accounting and legislative framework. For local authorities, the relevant accounting framework is the Code of Accounting Practice prepared by CIPFA.

4.1.3 In a local authority context, the audit opinion covers the financial statements, the Collection Fund Account and the Housing Revenue Account. It does not cover the narrative statement or annual governance statement. These are covered by what is known as a 'negative assurance' or 'consistent with' opinion. The auditor is required to read these statements to confirm that there is nothing inconsistent or misleading based on what is reported in the accounts and their understanding of the business. If these statements contain information which is misleading or inconsistent, auditors should insist that the relevant sections are appropriately reworded or removed. If not, no further work is required.

4.1.4 Materiality is a key concept in financial audits. Errors or misstatements are material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions that users take on the basis of the financial statements. Auditors are not required to take account of individual users, but do need to assess them as a group.

4.1.5 Auditors do not test every transaction supporting a set of financial statements. Instead they split the financial statements into groups of transactions with similar characteristics and assess the risks of material misstatement for each. The amount and types of audit testing for each of these areas is informed by this risk assessment.

4.1.6 It therefore follows that the key factors in delivering a quality audit are understanding the needs of the users of the accounts; and undertaking an effective risk assessment informed by a proper awareness of the business.

Scope of value for money opinion

4.1.7 The framework for the value for money opinion is set out in the NAO's Statutory Code of Audit Practice, published in April 2015.[7] ISAs do not apply to VfM audits.

[7] https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2015/03/Final-Code-of-Audit-Practice.pdf

4.1.8 The 2015 Audit Code requires auditors to:
"undertake sufficient work to be able to satisfy themselves as to whether, in the auditor's view, the audited body has put arrangements in place that support the achievement of value for money. In carrying out this work, the auditor is not required to satisfy themselves that the audited body has achieved value for money during the reporting period."

4.1.9 The Audit Code goes on to say:
"Ultimately, it is a matter for the auditor's judgement on the extent of work necessary to support their conclusion on value-for-money arrangements".

4.1.10 The Audit Code requires documentation of the overall conclusion, consideration of risk and of the planned response and work done to address significant risks. If there are no significant risks, the Code does not explicitly require documentation of work done.

Changes introduced by the 2020 Code of Audit Practice

4.1.11 In 2020, the C&AG published a new Code of Local Audit Practice. This is effective from the 2020-21 financial year. The main changes made are in respect of the value for money opinion and supporting work and have been broadly welcomed by auditors and those local authorities who have so far expressed a view.

4.1.12 The binary audit opinion on whether appropriate arrangements are in place has been replaced by a commentary on:

- *Financial sustainability: how the body plans and manages its resources to ensure it can continue to deliver its services;*
- *Governance: how the body ensures that it makes informed decisions and properly manages its risks; and*
- *Improving economy, efficiency and effectiveness: how the body uses information about its costs and performance to improve the way it manages and delivers its services.*

In addition, the updated Code will explicitly require auditors to document clearly the work that they have done to support their findings.

4.1.13 The consultation on the supplementary statutory guidance issued by the NAO to support the new Code closed on 2 September 2020. Once this guidance is finalised auditors will need to consider the factors including the following:

- whether a revised risk assessment is required;
- how to design an approach that moves away from obtaining evidence to support a binary audit opinion, to one that generates information to support a commentary on the arrangements in place.
- whether additional or different types of audit testing will be required, and how to structure and produce the new narrative reports.

Other statutory duties and powers

4.1.14 In addition, auditors of local authorities have other statutory powers and duties. These are:

- The power to issue a Public Interest Report at any time;
- The power to issue statutory recommendations to management, copied to the Secretary of State;
- The power to issue an advisory notice setting out potential illegal expenditure;
- The power to apply to the Courts to have unlawful expenditure disallowed;
- The duty to consider qualifying whistleblowing disclosures; and
- The duty to respond to objections raised by electors or other relevant persons.

The Audit Code includes guidance on the scenarios that might give rise to use of these powers and duties. Use of the powers along with the work required to support reports, recommendations and responses to objections is a matter of judgement.

4.2 Defining audit quality

4.2.1 Audit quality is a key determinant of audit performance and this must be seen, not only as a measure against agreed standards and principles, but also whether the output of an audit is seen to meet the legitimate expectations of council taxpayers and other users of accounts.

4.2.2 Financial audit is fundamental to these requirements to give assurance to the reader that the accounts are properly prepared and fairly reflect the council's financial position and use of resources.

4.2.3 Value for money audit should be designed to provide the reader with assurance that the systems in place for use of resources in an effective and efficient way are adequate and appropriate, and that the local authority plans will deliver financial resilience in the immediate and medium term.

4.2.4 The effectiveness of audit also depends on the usefulness, impact and timeliness of auditor reporting. Consideration of Public Interest Reports and Statutory Recommendations is relevant here. Finally, the effectiveness of audit also depends on the Authority's response to audit recommendations. This is a wider definition than that currently used by regulators. Ultimately, regulators consider a local authority financial audit to be of acceptable quality if the audit opinion is supported by sufficient and appropriate evidence and if the work complies with auditing standards, relevant legislation and the Code of Audit Practice. As VfM audit is not covered by auditing standards, the regulators focus principally on whether the audit complies with the Code of Audit Practice.

4.2.5 Nevertheless, the effectiveness and usefulness of local audit has to be measured alongside the assessment of quality. The Review has considered the extent to which the auditors of local authorities:

- Meet the contract specification;
- Demonstrate sufficient understanding of the local authority environment through identification and testing of key financial audit and value for money risks;

- Deliver audits in a cost-effective way;
- Make balanced and considered recommendations; and
- Issue reports and make recommendations in timely fashion.

4.3 Assessing Audit Quality

Meeting the Contract Specification

4.3.1 The contract between PSAA and audit firms largely follows standard terms and conditions. It requires providers of audit services to deliver audits in accordance with statutory obligations and appropriate professional standards. These are discussed below.

4.3.2 The contract is supplemented with a Statement of Responsibilities published, on the PSAA website, which is intended to set out the engagement between PSAA and the appointed auditors. The contract requires audit firms to familiarise themselves with this statement. In accompanying text on their website, PSAA makes clear that the responsibilities of auditors are derived from statute, principally, the 2014 Act and from the NAO Code of Audit Practice and nothing in the Statement is meant to vary those responsibilities.

Demonstrating an understanding of the local authority environment

4.3.3 Feedback received from interviews with local authorities is that KAPs tend to be knowledgeable, skilled and experienced. However, the amount of time devoted to the audit has become more limited in recent years. Anecdotal evidence on the accessibility of KAPs varies. Local authorities largely stated that the senior partners were brought in to resolve significant issues, so were not often visible during the course of the audit. This matched many audit firms' comments that senior partners were brought in for the specific and more complex issues. Most local authorities commented that this was reasonable, and as expected, but some felt that it was difficult to secure input from their KAP on specific issues. Some local authorities commented that during 2018-19 audits, the visibility of both the audit team and KAP had declined somewhat compared to prior years.

4.3.4 As demonstrated by the responses in **Figure 4.1,** despite valuing KAPs, many local authorities had a negative opinion of the overall knowledge and expertise of their audit teams. The two areas of particular concern were:

- the knowledge and continuity of working level audit staff; and
- whether audit work always covered the most important areas of the accounts from a financial resilience and service user perspective.

4.3.5 There is a question as to whether external audit could make more use of the knowledge and expertise of internal audit in developing sufficient understanding of the local authority. It is usual for the external audit team to meet the Head of Internal Audit as part of the audit planning process, but it is unclear if liaison extends much beyond that. Internal auditors are likely to be much closer to the business than external audit and, in many authorities, a proportion of their work focuses on governance and service delivery matters. This could make internal audit a rich source of knowledge, should the external audit team wish to use it.

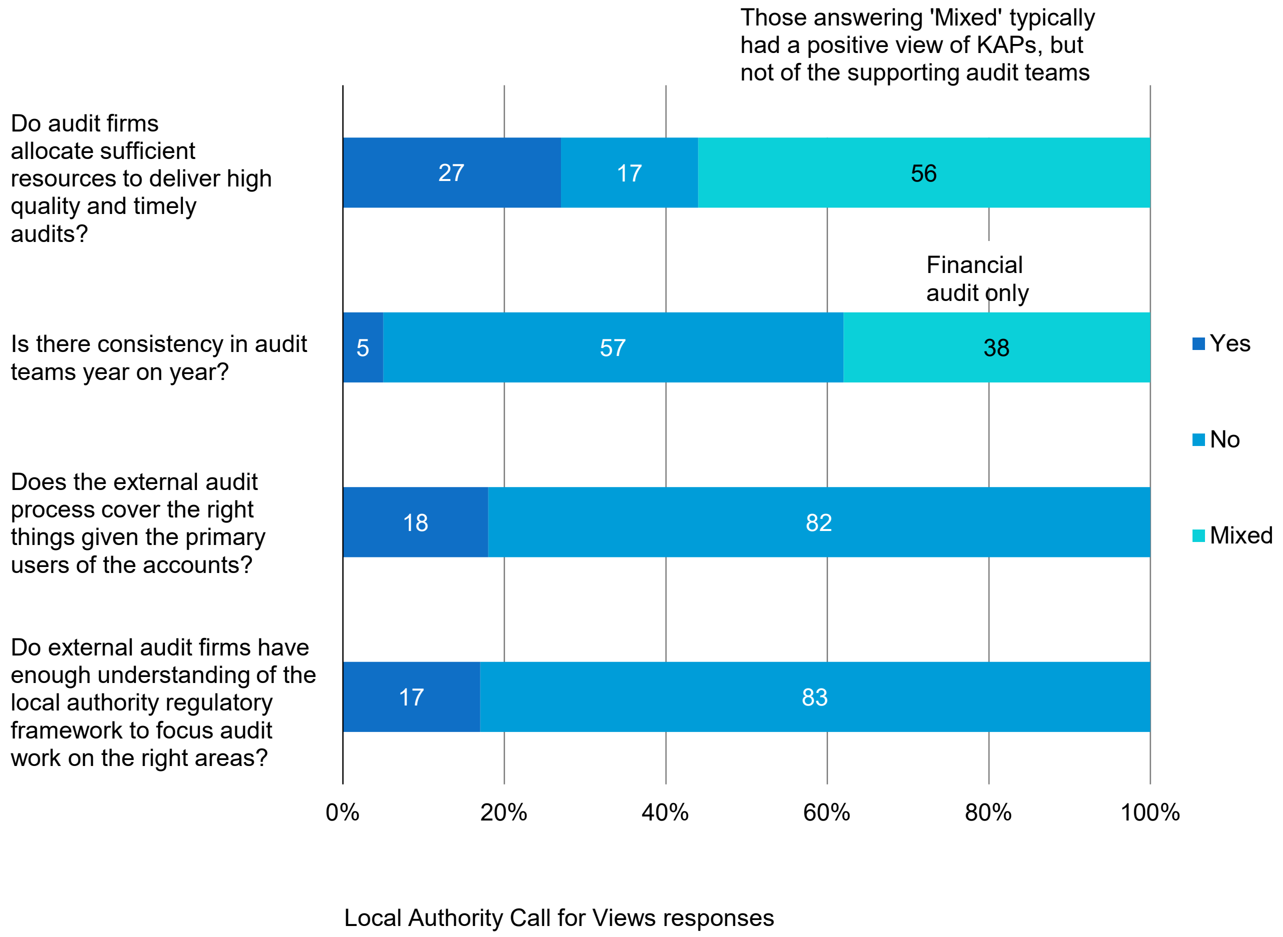
Knowledge, experience and continuity of audit staff

4.3.6 All audit firms active in the local audit market told the Review that they had expert technical teams who provided sector specific training to staff working on local authority audits. Nonetheless, many local authorities reported significant concerns about the knowledge and expertise of staff working on their audit. Issues identified included:

- audit examiners not having a full understanding of how local authorities were funded and how this impacted the accounts;
- a lack of continuity from year to year, or in some cases from week to week, leading to a lack of client knowledge; and
- a lack of understanding of local authority specific financial statements such as the Collection Fund and Housing Revenue Account.

4.3.7 Local authorities also reported the use of audit examiners from other countries to help manage the local audit peak. This is not unique to audits in the local authority sector and can be advantageous as different countries will encounter different audit peaks. However, may local authorities whose audits are staffed in this way reported that such examiners processed very little training in respect of English local government.

Figure 4.1
Opinions on External Audit Quality



4.3.8 Firms agreed that consistency in audit teams could sometimes be compromised by either the difficulty in attracting and retaining quality junior staff or the challenge to retain more experienced staff.

4.3.9 Underpinning the concerns about the quality and continuity of working level audit staff is a concern that there are not enough audit examiners with local authority expertise, and that this is an area in which accountancy trainees no longer wish to specialise.

4.3.10 This is a concern that has developed since 2015. Prior to 2012, the Audit Commission's in-house audit practice, District Audit (DA), was responsible for 70% of the local authority audit market. In its 2012 procurement the Audit Commission outsourced its audit practice. DA staff were TUPE'd[8] to the private sector firms who largely took over responsibility for auditing local authorities. This meant that there was then a plentiful supply of audit examiners with local authority experience. Since 2015, many of those audit examiners have left the external audit profession and have not always been replaced.

4.3.11 A reason for the decline in the number of audit examiners with sector specific expertise is the route taken by auditors to qualify as accountants. Currently, there are five chartered British and Irish professional accountancy bodies that include external audit as a significant element in their qualification. Only one of these bodies (CIPFA) has a mainly public sector focus. All District Audit service trainees would have followed the CIPFA qualification route. Only one of the firms currently active in the market (Grant Thornton) uses the CIPFA qualification route for its public sector audit staff. In addition, audit firms highlight that between 2010 and 2015 the Audit Commission cut back on its recruitment of audit examiners. This means that an increasing number of local authority auditors will not have had the public sector as their main focus whist studying for their accountancy qualification.

4.3.12 In March 2020, PSAA published research it had commissioned on the future of the local audit market.[9] In this research firms raised two main issues that made it difficult for them to attract and retain high quality staff that wanted to specialise in local authority audit:

- **Timetable** - In 2017-18 the target date for completing local authority audits was brought forward from 30 September to 31 July. This reform was requested by many local authorities, who wanted to complete their accounts and audit process as quickly as possible, so as to free up their finance teams to work on other areas. The compression of the audit timetable was mentioned as an issue by every audit firm. Firms raised concerns about the resulting peaks in workload, pressures on staff during the summer months, and knock-on effects when target dates are not met. These pressures contribute to making work unpopular with local audit staff.
- **Fees** – Firms stated generally that the lack of profitability changes the way that local audit work is perceived within the firm. As the contribution that local audit makes to the overall profit of the Partnership is low, specialising in this area is seen by many auditors as having a detrimental impact on career prospects.

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[8] TUPE stands for the Transfer of Undertakings (Protection of Employment) Regulations and its purpose is to protect employees if the business in which they are employed changes hands.

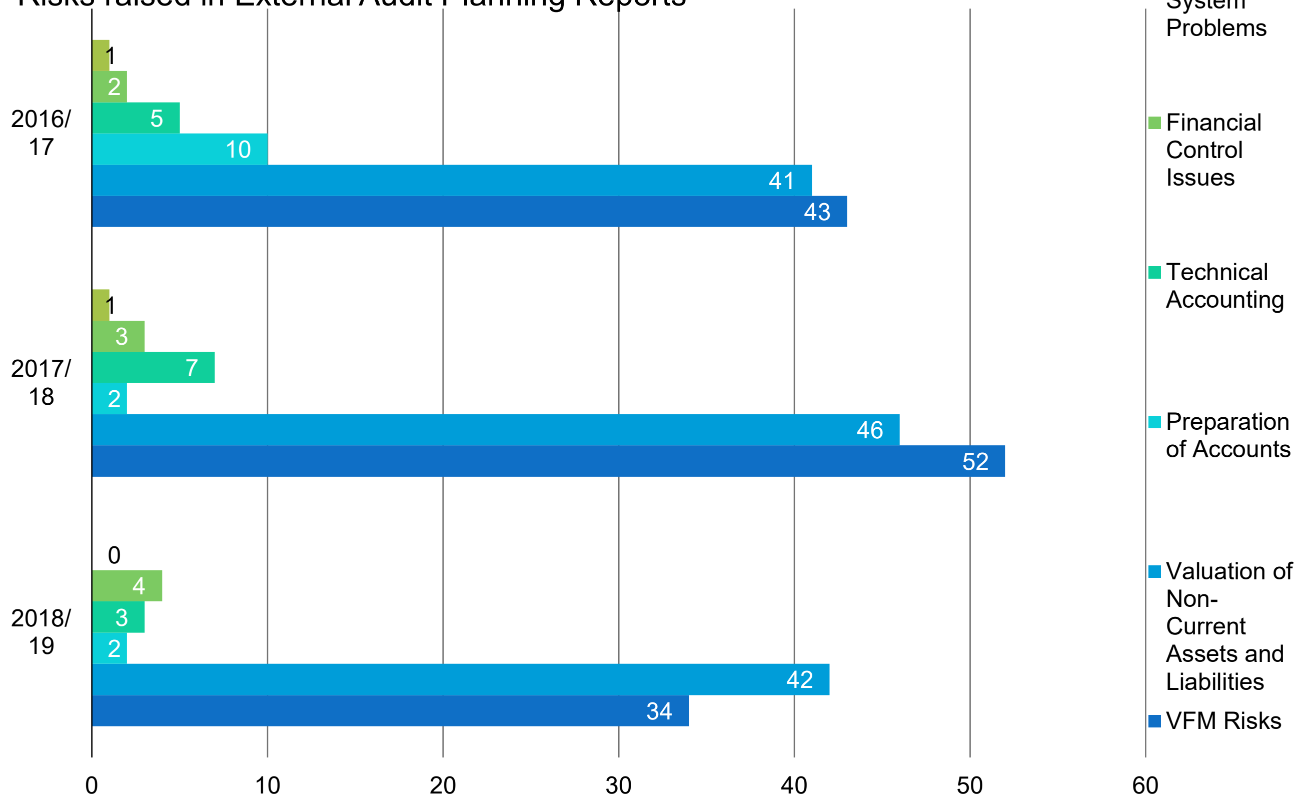
[9] https://www.psaa.co.uk/wp-content/uploads/2020/03/PSAA-Future-Procurement-and-Market-Supply-Options-Review.pdf

Focus of audit work

4.3.13 Many local authorities have raised concerns that auditors spend a significant amount of time focusing on fixed asset and pension valuations, whereas a fuller understanding of the business would lead to more of a focus on major areas of expenditure, together with the level of usable non-ringfenced revenue reserves. The reason for this argument is that most changes to fixed asset and pension values are ‘reversed out’ of the accounts by a range of statutory adjustments. As a result, in those circumstances, these valuations have no immediate impact on the cost of delivering services or on the financial resilience of a local authority.

Figure 4.2

Risks raised in External Audit Planning Reports



Notes

1 Representative sample of 30 local authorities. Presumed risks excluded

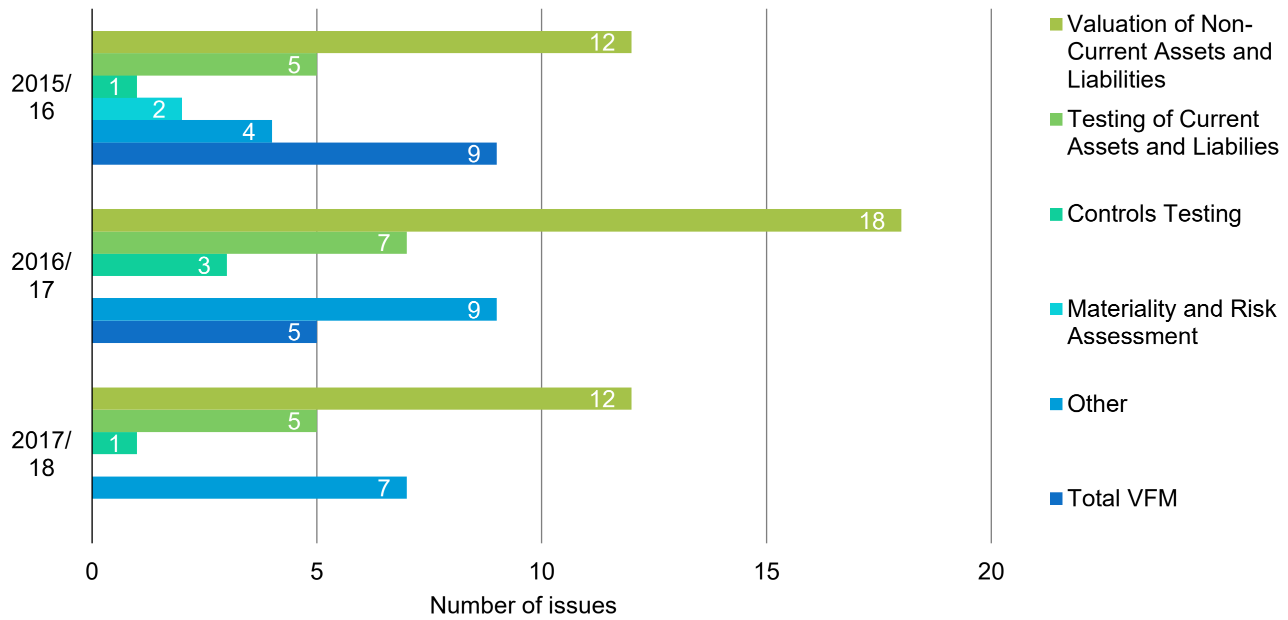
4.3.14 As demonstrated in **Figure 4.2**, valuation of non-current assets and liabilities have been the most common significant financial audit risk category identified in Audit Planning Reports. In addition, irrespective of the risk profile, the amount of detailed testing undertaken on these balances has increased significantly over the past three audit cycles. To manage the risk of regulatory criticism, that more scepticism is needed when assessing non-current assets and liabilities, audit firms are increasingly using their own expert valuers to assess valuations provided by a local authority employed expert. Some audit firms agreed that they would prefer to do less work on asset and pension valuations but explained that these areas of the accounts were given more attention as it was important in the context of securing a positive assessment from the FRC quality assurance processes.

4.3.15 The results of the quality assurance reviews of local authority audit files undertaken between 2015-16 and 2017-18 in **Figure 4.3** demonstrate clear and continuing concerns about the quality of audit work to support fixed asset and pension valuations. The FRC commented that, overall, the local authority audit files it reviewed tended to be of slightly lower quality than the files of corporate sector audits.

Figure 4.3

Issues identified by FRC file reviews conducted on behalf of PSAA

Eight reviews were conducted in 15/16 and 16/17 and 6 were conducted in 17/18



4.3.16 The FRC quality reviews identified far fewer significant issues in VfM audit work. This may be because the current Audit Code gives auditors quite a lot of discretion as to how much work they need to undertake before forming their VfM opinion.

Deliver audits in a cost-effective way

4.3.17 Since 2015, audit fees paid by local authorities have dropped by 42.25% (in cash terms). The decrease in fees has been welcomed by the LGA and by many local authorities. This reduction in fees has been attributed to the following reasons:

- PSAA costs being lower than those of the Audit Commission;
- Improved audit efficiency;
- Reduction in firms' profit expectations; and
- Reduced financial risks for the firms from staff previously TUPEd.

4.3.18 It is difficult to identify the extent to which local authority audits are more efficient than previously. All of the audit firms active in the market have looked to generate efficiencies through making significant investments in digital technology and innovation to equip audit teams with the appropriate tools to deliver a digital audit. However, audit firms note that many local authorities have IT systems that do not lend themselves to the delivery of a digital audit, so some of the anticipated efficiencies have not been realised.

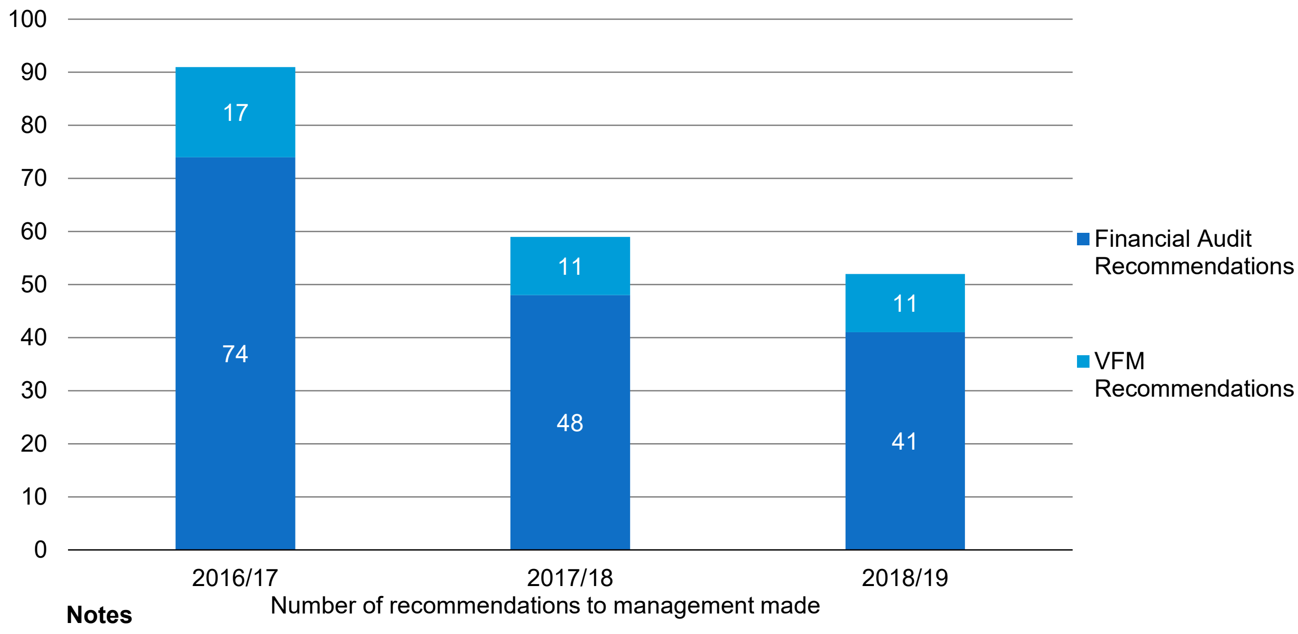
4.3.19 The decrease in fees must be set against the potential impact on quality if audit is considered to be cost effective. Audit firms have raised concerns about whether audit fees are at a sustainable level. One of the registered firms not active in the local authority market said that they had decided not to bid because it was impossible to deliver cost effective and high-quality audits at current fee levels.

4.3.20 Firms have the power to request fee variations where the cost of the work is greater than allowed for by the contract fee. As discussed in **Chapter 3** the fee variation process is an ongoing and increasing source of tension, with auditors concerned that they are not always able to recover legitimate costs. Local authorities are concerned about late notifications and that requested variations are not always supported by evidence of additional work done.

Make sensible recommendations

4.3.21 Auditors can issue recommendations to management through their end of audit communications. These can either be statutory recommendations, which must be copied to the Secretary of State, introduced through the "management letter" recommendations. Eleven statutory recommendations have been issued since 2015.

Figure 4.4
Number of External Audit recommendations given to local authorities



Notes

1 Representative sample of 30 local authorities.

2 Not all audits in 17/18 18/19 have been signed off in this sample.

4.3.22 As demonstrated in **Figure 4.4,** a review of Audit Completion Reports indicates that the number of management letter recommendations issued seems to be declining year on year. The practice on following up management letter recommendations was mixed and Audit Committees were more likely to check progress on implementation of internal audit recommendations rather than external audit recommendations. A majority of the recommendations made relate to technical accounting issues rather than financial control or value for money matters. This is not surprising given the focus of external audit, but it contributes to a perception that the process is not adding as much value as formerly.

Provide useful and timely reports

4.3.23 As demonstrated by **Figure 4.5,** the number of delayed audit opinions has significantly increased over the past three years. For 2018-19, all the audit firms in the market had some outstanding audit opinions as at 30 September 2019, though the extent varied from firm to firm; one firm completed just less than 40% of audits by the deadline while another completed 80%. All firms have made progress in completing these delayed audits although at December 2019, there were still 85 outstanding audit opinions (17.5%); and by July 2020, 42 (8.6%) of 2018-19 audits remained incomplete. These delays are likely to have had a knock-on impact for the 2019-20 timetable.

Figure 4.5
Audit opinions signed off by the statutory deadline for publishing audited accounts

	2018/19	**2017/18**	**2016/17**
Opinions issued by the statutory publication deadline	57% *31 July 2019	87% *31 July 2018	95% *30 September 2017
Opinions issued by 30 September	70%	95%	N/A

*statutory deadline for publishing local authority accounts 30 September in 2016-17; and 31 July thereafter.

4.3.24 PSAA asks audit firms to explain the reason for delayed audits. The four most common reasons provided were:
- poor quality accounts/working papers submitted by the local authority;
- potential qualification issues;
- outstanding objections on the accounts; and
- for the first time in 2019-20, having insufficient qualified individuals to deliver all audits at the appropriate time was included as a reason for some of the delays.

4.3.25 Audits are by their nature backwards looking and the increasing delays in signing off local authority audits have an impact on the timeliness of reports. The more material issues that an auditor finds, the greater the risk that the sign off of the audit opinion is delayed. When a judgement needs to be made about modifying an audit opinion, audit firms are required to undertake enhanced quality assurance procedures, and these take time. In addition, some audits will be delayed if a local authority presents poor quality accounts or if there is an outstanding objection. As a result, a number of local authority audits will inevitably be signed off after the reporting deadline.

4.3.26 In recognition of the increased challenges posed by Covid-19, MHCLG has extended the deadline for signing off 2019-20 audits to 30 November 2020. If a majority of audits are not signed off by this date, there could be a significant impact on MHCLG's ability to run the non-domestic rates system effectively. It is too early to say how many local authority audits will make this target date or whether the extension of the deadline will enable audit firms to complete more of the outstanding 2018-19 audits.

4.3.27 Examples of useful and timely auditor reporting through client communications are relatively few. Some local authority Chief Financial Officers commented that they no longer got the useful and informative advice, challenge and support that they had received from KAPs prior to 2015. Audit Planning Reports tend to be presented in February, March or April, which is rather late in the financial year. This means that local authorities get late notification of audit risks. In addition, it is not possible to undertake interim audit work on management controls if the plan is presented in the last month of the financial year and this increases the pressure on the year end peak.

4.3.28 If an Auditor is assessing a significant issue, which they believe needs to be brought to the attention of elected representatives and the public as soon as possible, the have the power to issue a Public Interest Report (PIR). PIRs can be issued at any time. However, only four PIRs have been issued since 2015. Three of these related to matters identified prior to 31 March 2015 and the fourth, issued on 11 August 2020, related to a wholly-owned local authority company.[10] This means that the opportunity to enhance transparency and accountability by sighting key stakeholders on significant issues in a timely fashion is not often used.

4.3.29 Audit firms have not commented on why there is not a greater use of the statutory powers available to them. The position in which auditors find themselves can relate to a situation where intervention in a local authority may be warranted by the use of statutory powers. It is possible that the legal and reputational risks of using these powers may play a part in their thinking as may the difficulty of recovering the costs of the extra work required to support use of these powers.

4.4 Interactions between external audit and relevant stakeholders

4.4.1 The areas of concern that particularly stood out from interviews with local authorities and through the Call for Views were:

- Senior audit staff not being contactable by clients when issues arose;
- Late notification of audit risks;
- Changes to the audit timetable – without justification given;
- Late notification of fee variations with no justification or breakdown of cost given; and
- The auditor's valuation expert overriding asset valuations provided by client experts with equivalent qualifications sometimes with no justification given.

4.4.2 It is important to note that these concerns are not unreciprocated. Auditors raised concerns about LAs not preparing properly prepared draft accounts supported by high quality working papers or not being available to answer audit questions.

4.5 VfM expectation gap

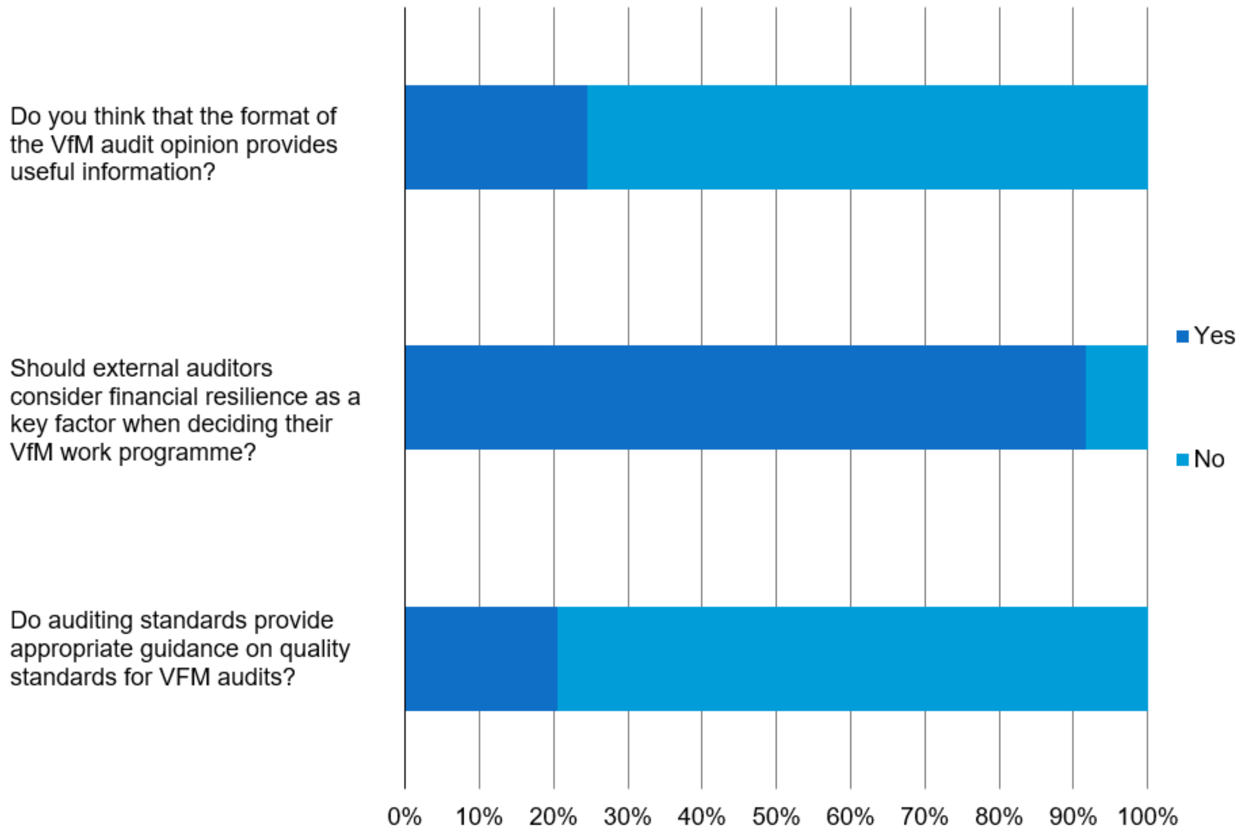
4.5.1 Whilst audit firms feel that the NAO's new code of practice resolves many of the VfM conclusion shortcomings, some local authorities believe that more significant changes need to be made. There is a large expectation gap between what local authorities

[10] https://www.nottinghamcity.gov.uk/publicinterestreport

expect a VfM opinion should provide and what it actually provides. The VfM conclusion is viewed by many local authorities to be an exercise with limited use to them as it is too retrospective and often states what the local authority often already knows. **Chapter 6** includes a more detailed consideration of the extent to which the VfM opinion covers financial resilience risks.

Figure 4.6

Opinions on the VfM opinion and auditing standards



Notes

1 Data from Local Authority Call for Views responses.

4.5.2 As demonstrated in **Figure 4.6**, 74% of the local authority respondents to the Call for Views think the format of the VfM opinion does not provide useful information. Some of these respondents recognised that the opinion is limited to giving assurance only that processes are in place to secure value for money and therefore that the opinion needs to be expanded to provide useful information. 79% of these respondents do not think the standards provide appropriate guidance on quality standards for VfM audits.

4.5.3 91% of respondents think external audit should be required to assess financial resilience. Although 3% of these respondents felt that financial resilience is already covered to an appropriate amount, most of the other respondents thought that financial resilience should be considered in the medium and long term as part of the value for money audit opinion. This included most audit firm respondents to this question, all of whom stated that the updated NAO Code of Audit Practice, effective from 2020-21, would provide a suitable level of coverage. No local authorities specifically mentioned the NAO Code of Audit Practice in their responses, although this may be due to the fact that the updated Audit Code had not been finalised at the time the Call for Views closed. However, 16% of local authority respondents thought the non-statutory CIPFA Financial Management Code (published Oct 2019) could provide a suitable framework for assessing financial resilience and financial management.

4.6 Summary of audit performance

4.6.1 There is an expectation gap that extends across both the financial and the VfM audit. The coverage of the financial and VfM audits is far narrower than many stakeholders expect.

4.6.2 There are questions about the level of audit performance. In addition, although external auditors may be meeting the contract specification by delivering audits that, for the most part, meet the quality standards set out in ISAs and the Audit Code, an increasing number of audits are not being completed by the statutory deadline for publishing audited accounts.

4.6.3 Audit fees paid by local authorities have reduced, whereas, over the same period, they have increased in other sectors. There is some evidence that the reduction in fees has led to a decline in the number of examiners with appropriate skills, knowledge and expertise. This has had an impact on the timeliness of audits, the usefulness of auditor reporting to management and the quality of interactions between external auditors and local authorities.

4.6.4 Underpinning concerns about audit performance is a question of focus. There is a perception amongst many local authorities that an increasing amount of time is spent auditing fixed asset and pension valuations. It is clear that external audit increasingly has a greater focus on these areas, and that this has been driven by the requirement to meet quality standards and comply with relevant statutory guidance. What is less clear is the extent to which this has led to a reduction of audit work in other areas, but given the reduction in audit fees, it is likely to have had some impact.

4.6.5 It is more difficult to summarise audit performance in relation to the VfM engagement. This is partly because the 2015 Audit Code requires minimal documentation unless significant VfM risks are identified. This makes it impossible to assess whether the external audit assessment of VfM risks is complete in all cases. However, given the squeeze on audit fees and the reduction in the number of audit examiners with appropriate skills, knowledge and expertise, this remains a matter of significant concern.

5. Governance arrangements in place for responding to audit recommendations

5.1 Outline of the different frameworks in operation

5.1.1 The effectiveness of audit must, in part, be determined by the arrangements in place within each body subject to audit for considering and acting upon external audit reports. All local authorities are required to set up Audit Committees or the equivalent with responsibility for considering the annual accounts and receiving internal and external audit plans and reports. The specific arrangements vary between different types of local authorities. However, the purpose of an Audit Committee is to provide independent challenge on behalf of the authority in respect of accountability and risk management arrangements.

Arrangements within PCCs

5.1.2 A PCC is an elected official charged with securing efficient and effective policing of a police area. The policing function is delivered by the constabulary, led in large part by Chief Constables. PCCs are required to set up Joint Audit Committees covering the activities of both the PCC and the constabulary. These arrangements appear to work effectively and the findings and conclusions in the rest of this Chapter do not apply to PCCs.

5.1.3 Some PCCs also have responsibility for overseeing the delivery of Fire and Rescue Authorities, which deliver the fire service, in their local area. In other areas, primarily Shire Counties, the fire service is the responsibility of the County Council.

Arrangements within other types of local authorities

5.1.4 Mayoral Combined Authorities[11] are required by statute to have an Audit Committee, although there is no statutory guidance on the membership or remit. Whilst not a requirement for other types of local authorities, in practice most have set up an Audit Committee or equivalent.

5.1.5 Constitutionally, Audit Committees in local authorities are sub-committees of Full Council. This means that a majority of its members will be elected as a councillor or its equivalent. As highlighted in **Figure 5.1,** membership tends to be based on the political balance of the council and the chair is often, but not always, a member of the ruling group.

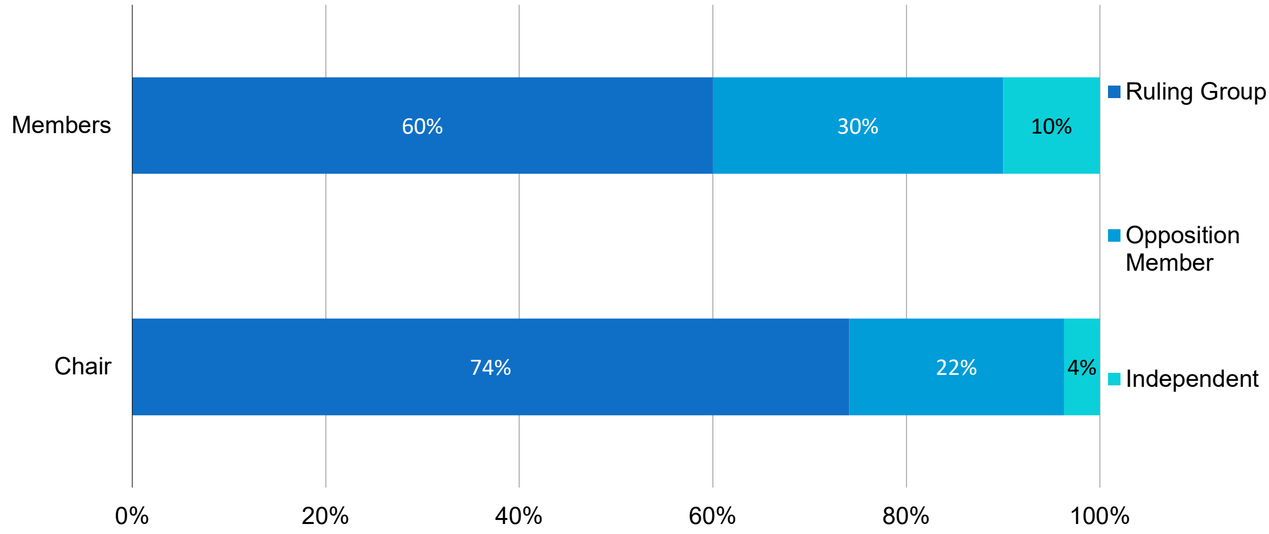
5.1.6 The number of members of Audit Committees varies from four to seventeen, with seven being the most common. This compares to common practice in central government and the private sector, which is to have no more than three or four Audit Committee members. The size of the committee might vary according to the number of councillors an authority has; however, Birmingham City Council, which by expenditure is the largest local authority and has more councillors (99) than any other local authority in England, has eight members on its Audit Committee, whereas the

[11] Combined Authorities are statutory bodies made up of neighbouring local authorities that broadly cover a city-region that have agreed to work together. A Mayoral Combined Authority is where a mayor is the directly elected leader of the combined authority.

Audit Committees of some Shire District Councils have memberships that far exceed this.

Figure 5.1
Composition of audit committees in councils

56% of committees had no independent members



Notes

1 Representative sample of 27 Local Authority Committees (not including FRAs or PCCs).

5.1.7 Local authority accounts are very complex and there appears to be a significant difference between the assurance that external auditors provide and public expectations. Elected members may or may not have relevant skills, expertise or background to fulfil the role of a member of an Audit Committee. Many local authorities provide training for Audit Committee members, but it has not been possible to assess how comprehensive or effective this training is. As a result, it is not possible to conclude whether members are always equipped to provide effective challenge to Auditors or Statutory Officers.

5.1.8 As part of its Audit Quality Reviews of 2018-19 audits, the FRC review teams have met with Audit Committee chairs of 12 selected local authorities. Although the reviews of the related audits are not yet publicly available, a mixed picture was reported, with some chairs being very engaged and informed, but others being less so. As the FRC is responsible only for the quality assurance reviews of the 230 larger local authorities and NHS bodies, the experience provided by their quality reviews may not be fully representative of the sector.

5.1.9 Whilst the vast majority of local authorities interviewed were supportive of the principle of appointing independent members, only about 40% of Audit Committees currently have done so. The reported experience of having independent members on Audit Committees was mixed. In some cases, they provided useful challenge, but some authorities reported that the effectiveness of independent members was hampered by their lack of sector specific knowledge.

5.1.10 A particular challenge for authorities is attracting independent members with the relevant technical experience. This challenge can sometimes be greater depending on an authority's geographical location. Some PCCs have found that the introduction of Joint Audit Committees, which are seen as more prestigious, has made Audit Committee membership more attractive to appropriately qualified independent members, but there is still not an abundance of suitable applicants for vacant positions.

5.1.11 The independent member is often a voluntary position across the local authority sector. This compares to NHS trusts who are more likely to pay independent Audit Committee members, which may make it slightly easier for them to attract applicants with relevant expertise.

5.1.12 Local authorities have a number of statutory officers, three of whom have responsibilities that may be covered by audit work. They are:

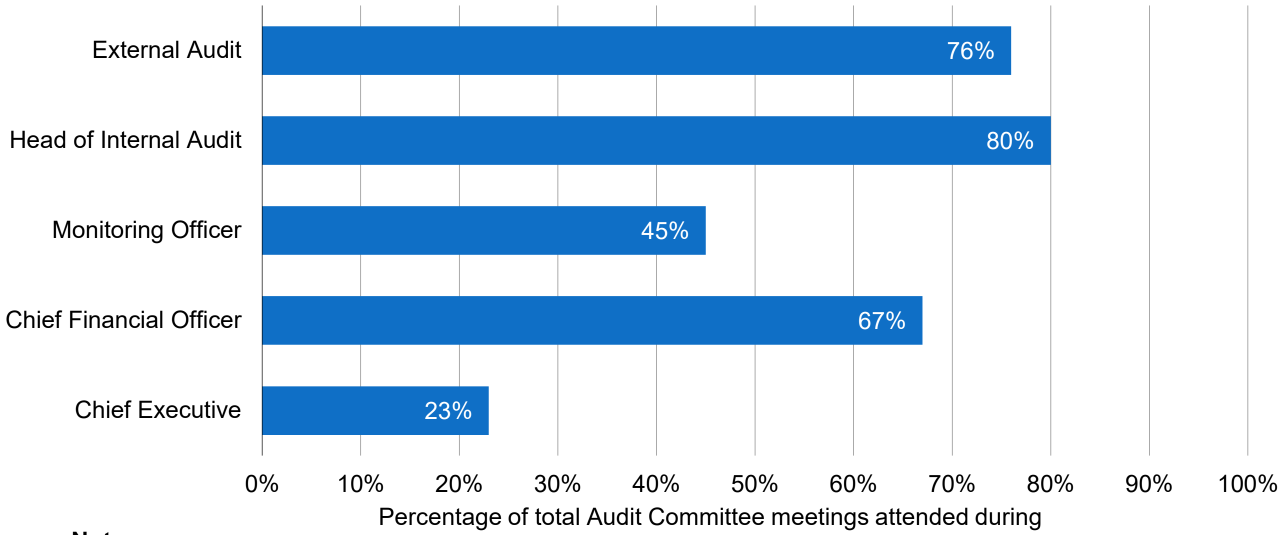
- The **Head of Paid Service** – typically the Chief Executive or Managing Director
- The **Section 151 Officer** – typically the Chief Financial Officer or Finance Director
- The **Monitoring Officer** – typically the Head of Legal Services

5.1.13 As demonstrated by **Figure 5.2** the frequency of attendance of statutory officers at Audit Committee meetings is mixed. Whilst the Chief Financial Officer and Head of Internal Audit attend a majority of meetings, Monitoring Officers attend just under half of the meetings and the Chief Executive attends such meetings less often. Other statutory officers and service heads usually attend Audit Committee meetings if a matter relevant to their service area is discussed.

5.1.14 The Chief Financial Officer is more likely to attend meetings where external audit completion reports are presented. Attendance of the Chief Executive increased by 2% and the Monitoring Officer attendance decreased. This may be reflective of the fact that in local government, the Chief Financial Officer signs the accounts on behalf of the local authority, or it may be indicative of the profile of external audit.

Figure 5.2

Audit Committee attendance: Local Authority Officers and External Audit Representative



Notes

1 Representative sample of 30 local authorities

5.1.15 In local government, representatives of external audit are not expected to attend every Audit Committee meeting. Based on a representative sample, the KAP attended 56% of meetings, rising to 87% of meetings where either external audit papers were tabled or where the final accounts were presented. For the 13% of these meetings where the KAP was not in attendance, external audit was represented by a less senior member of the audit team.

5.2 Scope of audit committees within local government

5.2.1 The scope of Audit Committees also varied between authorities. CIPFA's *Position Statement and supporting guidance on Audit Committees (2013)* says that the Audit Committee should cover:

- The annual governance statement
- The work of internal audit
- Risk management
- Assurance framework and assurance planning
- Value for money and best value
- Countering fraud and corruption
- External audit
- Partnership governance

and may also cover:

- Specific matters at the request of statutory officers or other committees
- Ethical values
- Treasury management

5.2.2 Most of the committees reviewed covered most of the items in the CIPFA position statement. There were two areas which had either minimal or no specific coverage: *partnership governance,* which was considered by only two of the 30 authorities reviewed; and *value for money and best value* which was not considered by any of those 30 authorities. The *CIPFA Survey on Local Authority Audit Committees* (November 2016) also found that Audit Committees were much less likely to consider these two areas. However, the scope of Audit Committees in local authorities is not limited to the areas suggested in the CIPFA guidance.

5.2.3 The scope of committees whose responsibilities included audit varied. The second most common name, after the 'Audit Committee' itself was a name which indicated the combining of audit with the functions of an overview and scrutiny committee. Overview and scrutiny committees are required by statute[12] and are responsible for overseeing and scrutinising the whole range of the Council's functions and responsibilities, as well as other public service providers' work and its impact on the local community. Whilst the functions of these two committees have some synergy, there is a question as to whether it enables the audit responsibilities to be fully addressed.

5.2.4 In one example a local authority had set up an Audit, Resources and Performance Committee. This is a significant concern because the prime purpose of an Audit

[12] Schedule 2, Localism Act 2011

Committee is to review the comprehensiveness and reliability of assurances on governance, risk management, the control environment and the integrity of financial statements and the annual report. The Resources Committee will use financial projections and risk management information to take decisions about use of resources. If the same committee is responsible for using information to take management decisions and providing independent assurance over the reliability of that information, there is no effective segregation of duties. There is also a potential for conflicts of interest.

5.3 Relationship between Audit Committees and Full Council or equivalent

5.3.1 Full Council has a role, ultimately, in responding to audit matters that is beyond receiving Public Interest Reports or qualified audit opinions. Full Council is generally more visible to the public than committees/subcommittees. The Council's public accountability to local taxpayers and service users is best served by having significant matters relating to audit discussed in a transparent and accessible way.

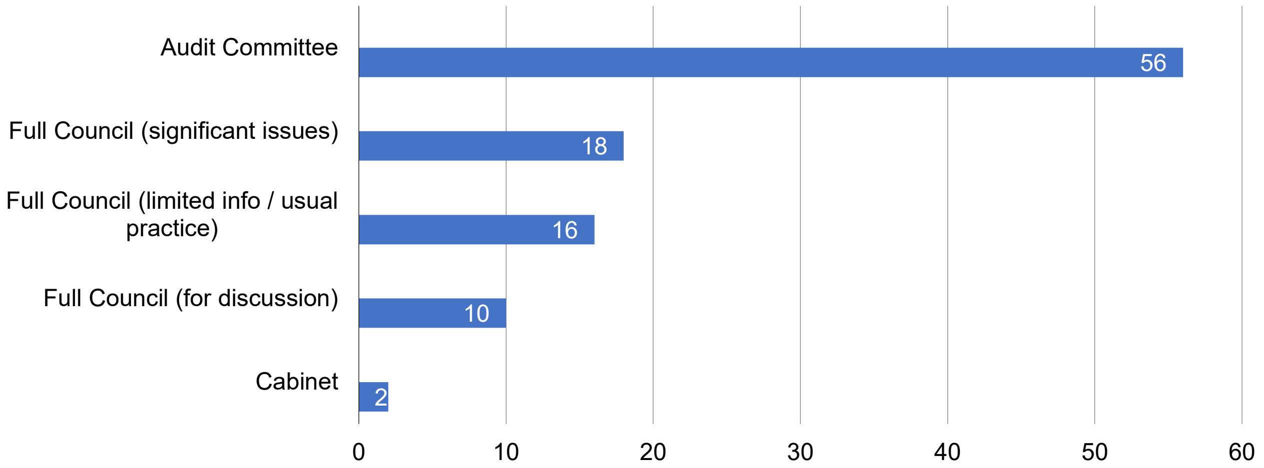
5.3.2 Matters raised at Audit Committee can be referred to Full Council. In addition, the auditor has the power to present some statements, for example an advisory notice that planned expenditure may be unlawful, directly to Full Council.

5.3.3 In practice the auditor tends to present matters to the Audit Committee, which decides if a matter is serious enough to be referred to Full Council. Most local authorities feel that this arrangement is appropriate. It is rare for an Audit Committee to put a substantive item onto the Full Council's agenda. The exception is the Treasury Management Strategy, where some local authorities have a practice of ensuring that it is considered by the Audit Committee before being forwarded to Full Council for approval.

5.3.4 Many local authorities stated that the existing relationship between Audit Committee and Full Council involved either forwarding for information a yearly summary report or meeting minutes and that this was considered to be sufficient. Many also commented that if there were significant recommendations made by the external auditor, such as a Public Interest Report, that then should be a matter for Full Council.

5.3.5 In some cases, some quite serious matters seem not to have been passed onto Full Council. For example, the 'best value' report into Northamptonshire County Council found that when the external auditor reported that appropriate arrangements to deliver best value outcomes were not in place, for the second year in succession, there is no evidence that the Audit Committee forwarded the qualified audit opinion to Full Council.

Figure 5.3
To whom should external auditors present audit reports and findings?



Notes

1 92% of local authorities respondents answered this Call for Views question

5.3.6 If this practice is widespread, there is a significant risk that in many councils, a majority of elected members may not be sighted on serious governance or financial resilience issues. This risk does not fully pertain to PCCs, where the PCC and Chief Constable are expected to attend the Joint Audit Committee and generally do so. There is a question as to whether Audit Committees, including Joint Audit Committees, are sufficiently transparent to local taxpayers and service users. Whilst by default, proceedings of these committees are public, it is not clear that taxpayers and service users are aware that they have a right to attend or to read the papers and the minutes.

5.3.7 As demonstrated in **Figure 5.3** most local authorities felt that external audit reports should be presented to the Audit Committee rather than to Full Council. Reasons given included:

- Full Council only taking items for decision;
- elected members not having the skills, knowledge or experience to understand the report unless they had received Audit Committee training.

5.3.8 Many commented that external audit reports should be reported to Full Council only in exceptional circumstances where there is significant cause for concern. One respondent commented that given the target dates and tight deadlines, there is insufficient time to report to Full Council prior to sign off of the accounts by the external auditors.

Raising the profile of external audit work

5.3.9 The content of the standard suite of external audit reports is mandated by auditing standards. Whilst audit firms have made significant strides in making reports more accessible to clients, much of the required disclosure is highly technical. Given this, it is perhaps understandable that many local authorities do not present such documents to Full Council.

5.3.10 Nevertheless, external auditors may have insights from their work, that could provide assurance to Elected Representatives that their local authority is being run with the best interests of service users and taxpayers in mind. The auditor also has the facility to sight elected representatives on matters that audit work has highlighted as a potential issue.

5.3.11 This suggests that the external auditor should report to Full Council on risks identified and conclusions reached, in a transparent and understandable format. To be of most use, such a report would need to be timely. Given the increase in the number of delayed audits, this report should not necessarily be linked to the certification of the financial accounts as it should be made at the most useful point in the year. Comparatively few local authorities commented on what was the right point in the year to receive audit reports. Two thirds of those who did, expressed a preference for end-September, coming as it does near the start of the following year's annual budget setting planning cycle.

Collating the results of external audit work

5.3.12 Prior to 2015, the Audit Commission published an annual report summarising the results of the audits of local authorities and the NHS. Up to the end of 2017-18 responsibility for preparing this report passed to PSAA. The report summarised the number of audits completed by the statutory deadline and the number of qualified financial audit and value for money opinions, with the latter categorised by theme. It also listed all Public Interest Reports, Statutory Recommendations and Advisory Notices issued in the preceding year. It did not include any details on risks raised by auditors in their Audit Planning Reports or non-statutory recommendations made to local authorities. Just over two thirds of Call for Views respondents think a publication summarising the results of local authority audits adds value.

5.3.13 The responsibility for preparing this report was included in the Memorandum of Understanding between PSAA and MHCLG. When MHCLG decided not to renew the Memorandum of Understanding, PSAA's responsibility for reporting on the results of audit work lapsed. This reinforces the point that no entity currently has the responsibility to collate and report on the results of the work of the external auditors of local authorities and individual NHS bodies.

6 Audit work on the financial resilience of local authorities

6.1 Stakeholders' expectations regarding financial resilience

6.1.1 Reference has been made to the role of external audit in assessing financial resilience and sustainability in local authorities. In England, neither the financial nor the value for money audit includes a specific responsibility to provide an opinion on whether a local authority is financially sustainable.

6.1.2 However, it is legitimate to expect the auditor to examine the ability of the local authority to provide resources sufficient to deliver the statutory services for which it is responsible. It would not be appropriate for this Review to provide a commentary on local government funding, but there are a number of key questions that it would be reasonable to expect the auditor to assess. These could include:

- Has the auditor scrutinised the balance sheet to understand the debt profile of the authority and the level and depletion rate of usable reserves?
- What metrics does the authority use to determine the level of financial risk it faces?
- When the annual budget is approved by Full Council or equivalent, the CFO is required to present a "Section 25" report, providing a view on the reasonableness of financial estimates and the adequacy of reserves. Should the auditor be required to confirm that this report is sound?
- It is good practice for local authorities to prepare a mid-term financial strategy, normally covering a three to five-year period that is presented alongside the budget. Is it reasonable to expect the auditor to consider the assumptions underpinning this strategy or to form a view on its whether it is robust and realistic?
- Local authorities are also required to prepare statutory reports that have implications for financial sustainability and available resources in future years. These include setting a Prudential Borrowing limit, calculating an appropriate provision for repayment of debt (known as "Minimum Revenue Provision"), preparing an Investment Strategy, and potentially preparing a Flexible Use of Capital Receipts Strategy. Is it reasonable to expect the auditor to consider some of these strategies and estimates?

6.1.3 CFOs may have specific expectations of auditors. As previously indicated, many of the CFOs who contacted the Review made it clear that they valued the informal contact and challenge from the KAP. Dialogue between the KAP and the CFO does take place, if not on as wide a scale as it did pre-2015, and there is no doubt this can be beneficial. However, the independence of the auditor must be preserved in the way that advice and guidance may be tendered.

6.2 What does financial resilience mean in a local authority context?

The statutory framework

6.2.1 Financial resilience in a local authority is different to a private sector context. The powers and responsibilities of local authorities along with the financial control framework within which they operate are set by statute.

6.2.2 The services that local authorities are required to provide are set out in legislation along with the accompanying powers and duties. The statutory responsibilities to deliver these services exist even if the local authority's resources may be considered to be insufficient at any given time.

6.2.3 The key financial controls set out in statute are:

- The requirement to calculate an **annual balanced revenue budget** for the upcoming financial year, that must be approved by Full Council or the equivalent. Local authorities are not allowed to run a deficit budget. Instead they are required to calculate a level of Council Tax that equates to the difference between income and expenditure. The increase in the level of Council Tax that can be charged is restricted by a 'referendum principle'. If a local authority wishes to raise Council Tax by more than a percentage specified by Ministers, they are required to put the planned increase to a referendum of local electors. Local authorities can borrow to fund capital investment but are not normally allowed to do so to finance in-year expenditure.
- The CFO's **"Section 25" report** on the robustness of the council's budget estimates and the adequacy of its reserves, which must be presented to Full Council alongside the annual balanced budget.
- The CFO has the power to issue a **"Section 114 notice"** if the CFO believes that the local authority is unable to set or maintain a balanced budget. After a section 114 notice is issued, the local authority may not incur new expenditure commitments, and the Full Council must meet within 21 days to discuss the report. There is no legal provision regarding what action they then must take. There is no procedure in law for a UK local authority to go bankrupt, and none has ever done so.

6.2.4 If a local authority mismanages its budgets over a number of years so that it is unable to recover its financial position, then central government has the choice of intervening under its "best value" powers, providing exceptional financial support, facilitating an offer of leadership and governance support from elsewhere in the sector, or using a mixture of these options.

6.2.5 Intervention on the grounds of lack of financial resilience is very rare. The most recent statutory intervention using best value powers was in Northamptonshire in 2018. Although there have been three other statutory interventions in the intervening years (Doncaster due to pervasive corporate governance failures, Rotherham due to institutional failure in responding to child sexual abuse and Tower Hamlets due to pervasive governance and financial impropriety issues), Northamptonshire was the first statutory intervention primarily due to financial resilience issues since Hackney in 2000.

6.2.6 In both Northamptonshire and Hackney, central government supported the council during the intervention by providing exceptional financial support, primarily by allowing receipts from sale of assets to be used to support revenue expenditure. Northamptonshire was also permitted to raise council tax by 2% more than other authorities for 2019-20 without triggering a referendum.

6.2.7 Whilst this might suggest that financial resilience is not an issue for local authorities, that may not always be the case. Firstly, central government support cannot always be guaranteed and secondly, a local authority experiencing severe financial resilience issues may also be facing governance and service delivery issues, with a consequential impact on those who depend on those services. Furthermore, the impact of financial resilience issues on service delivery is iterative. It must be emphasised here that the system must identify and highlight financial resilience issues at the earliest opportunity in order to avoid negative impact on service. When a service fails, it is likely that that cost of recovery will be greater with a possible consequential impact on financial resilience.

6.2.8 This suggests that in a local authority context, financial resilience means the ability to manage budgets over the medium term whilst continuing to deliver high quality and effective services, that can be accessed by service users. The level of service provided is very important. Local authorities in financial difficulties can seek to cut costs by reducing the level of service. This may be the case for demand led services such as social care where it is more difficult to forecast accurately local demand pressure.

Commercialisation and local authority resilience

6.2.9 One of the most significant sectoral trends since 2015 is the increased commercialisation of local authorities. To simplify, there are two main categories of local authority commercialisation:

- Investment in commercial property, usually through the general fund; and
- Investment in wholly owned companies set up using the "general power of competence". The most common type of wholly owned local authority company is the housing company. Other examples identified include energy companies, recruitment agencies, back office service delivery companies and leisure trusts. PCCs and FRAs do not have a "general power of competence".

6.2.10 The risks commercialisation poses to local authority financial resilience were highlighted in a recent NAO study on *"Local Authority Investment in Commercial Property"*[13] which concluded:

"Buying commercial property can deliver benefits for Local Authorities including both the generation of income and local regeneration. However, as with all investments, there are risks. Income from commercial property is uncertain over the long term and authorities may be taking on high levels of long-term debt with associated debt costs or may become significantly dependent on commercial property income to support services. At the national or regional level, Local Authority activity could have an inflationary effect on the market or crowd out private sector investment."

6.2.11 Although the NAO study focused solely on commercial property, this conclusion is as relevant to investments in wholly owned companies. If a company that is set up using the "general power of competence" gets into difficulty, the parent local authority may ultimately be responsible or may have to write off loans or equity funding, and this can impact financial resilience.

6.2.12 An additional risk with wholly owned companies is a potential lack of transparency. It can be very difficult for a reader to identify a local authority's exposure as a result of

[13] https://www.nao.org.uk/wp-content/uploads/2020/02/Local-authority-investment-in-commercial-property.pdf

investments in or loans to wholly owned companies by looking at the accounts. Unless an investment in, or transactions with, a wholly owned company is material by value, there is no requirement to consolidate the company's income, expenditure, assets or liabilities in the local authority's accounts. Instead, what is required is a disclosure of transactions between the authority and each of its wholly owned companies in what is known as the "Related Parties note". This note is presented less prominently in the annual report and accounts document. In addition, decisions a local authority makes pertaining to its wholly owned companies, including those relating to providing additional finance and awarding contracts, are often held in private on grounds of commercial confidentiality.

Defining local authority financial resilience

6.2.13 CIPFA has attempted to define financial resilience in a local authority context. In *Building Financial Resilience (Jun 2017)*[14]. This publication highlights four pillars of sound financial management and five indicators of financial stress.

Figure 6.1

CIPFA Pillars of Financial Resilience

Pillars of financial resilience	Indicators of financial stress
Getting routine financial management right	Running down reserves
Benchmarking against nearest neighbours – e.g. unit costs, under/overspends by service area, under-recovery of income.	Failure to deliver planned savings
	Shortening medium term financial planning horizons
Clear plans for delivering savings	Increase gaps in saving plans (i.e. where proposals are still to be identified)
Managing reserves over the medium-term financial planning horizon.	Increase unplanned overspends in service delivery departments.

6.2.14 The pillars of financial resilience identified by CIPFA related to process and governance points, so could be covered by the auditor's VfM opinion. Likewise, the indicators of financial stress could be covered by a sector-wide VfM audit framework.

6.2.15 An alternative and more detailed model, mentioned by some local authorities, is the seventeen principles set out in CIPFA's recently published Financial Management Code. Although only three of the seventeen principles are categorised under the heading of sustainability, in practice, all of the principles relate to matters that directly or indirectly contribute to an authority's capacity and capability to deliver sustainable services over the medium term.

6.2.16 A challenge common to both the *Pillars of Financial Resilience* and the *Financial Management Code* is that neither has any statutory basis. Whilst CIPFA requires its members to follow the *Financial Management Code*, compliance cannot be enforced. As a result, auditors may be reluctant to treat non-compliance with either as a matter serious enough on which to report.

[14] https://www.cipfa.org/policy-and-guidance/reports/building-financial-resilience-managing-financial-stress-in-local-authorities

6.2.17 A further challenge with the *Financial Management Code* is that the key principles are fairly detailed. Whilst an auditor could assess compliance with these principles, the costs of doing so in terms of both the auditor and of local authority time could be quite high.

6.2.18 Finally, neither the *Pillars* nor the *Financial Management Code* explicitly cover the impact of commercial activity on a local authority's financial resilience. General fund investments should be considered as part of the audit of financial accounts but wholly owned companies would only be considered if material enough to be consolidated into the accounts.

6.3 Current audit requirements to assess the sustainability and resilience of LAs in England

The Going Concern opinion

6.3.1 An underpinning principle of a financial audit is a 'going concern assumption'. The going concern principle means that readers of a set of accounts are entitled to assume a business will continue in the future, unless there is evidence to the contrary. When an auditor conducts the examination of the accounts, there is an obligation to review its ability to continue as a going concern for the next twelve months.

6.3.2 If the auditor concludes that there is significant doubt that the reporting entity is a going concern, the audit opinion is qualified, and a report explaining the auditor's financial resilience concerns is included with the audit opinion. In addition, if an entity is not a going concern, assets and liabilities must be valued at the amount they can be sold for rather than by assessing their ongoing value to the entity.

6.3.3 This particular way of validating a local authority's financial health has attracted much criticism from respondents. The view of practitioners is that that a local authority cannot face the prospect of bankruptcy/liquidity in the way that a company might.

6.3.4 In addition, local authorities are presumed to be a going concern for the purpose of forming an audit opinion, as the financial reporting frameworks for these bodies dictate a continued service approach, unless there is a clearly expressed Parliamentary intention to discontinue the provision of the services which the entity provides. The NAO has consulted on Supplementary Auditor Guidance, that reinforces this point.

6.3.5 87% of respondents to the Call for Views think the going concern assumption is meaningless in a local authority context. Respondents noted that local authorities would be likely to receive support from Central Government in the wake of a serious event. Many highlighted the example of Northamptonshire remaining a going concern for audit opinion purposes, even when the auditors had issued an advisory notice on what was considered to be an undeliverable budget. as an apparent example of the opinion's flaws. Those who responded that the opinion was meaningful included a majority of audit firms who acknowledged the going concern opinion's flaws and suggested changes but, on the whole, felt that it was still important that this assessment was carried out.

The value for money opinion

6.3.6 The other dimension of audit which could look at financial resilience is through the work required to support what is known as the 'value for money opinion'. The work required to support this opinion is governed by the NAO's Code of Audit Practice ("the Audit Code"). What the auditor is required to do is to form an opinion on the adequacy of the systems in place to support the economy, effectiveness and efficiency of service delivery. Under current practice in England, the auditor may test the adequacy of systems and procedures used to construct the mid-term financial plan but is only required to do so if a significant risk is identified during the audit. The auditor is not required to examine the mid-term financial plan from a sustainability perspective or form a conclusion on the financial resilience of the authority.

6.3.7 The update to the Audit Code, effective from 2020-21, will require auditors to provide a narrative statement on the arrangements in place. The aim of this statement is to provide more useful information to stakeholders, to report in a timelier manner and, through the move away from a binary opinion, encourage auditors to be bolder in highlighting concerns. The updated Audit Code has been broadly welcomed by stakeholders and has the potential to enhance value for money reporting in England.

6.3.8 What the updated Audit Code does not do is specify that auditors consider specific matters or judge local authority systems and performance against specific standards or good practice examples, such as CIPFA's *Pillars of Financial Sustainability* or their *Financial Management Code*. Nor does the updated Audit Code provide any guidance on how to assess whether a value for money risk is material.

Timeliness of the value for money opinion

6.3.9 Less than half of respondents to the Call for Views expressed an opinion on the timing of the VfM opinion. Two thirds of those who expressed an opinion agreed that the statutory reporting deadline of end-September was the right point in the annual cycle to present the VfM opinion, coming as it does near the start of the following year's annual budget setting planning cycle. Many commented that the external audit firms still had the capability to raise any significant VfM concerns outside this process, a process where they were happy with the content.

6.3.10 Those that disagreed included all but one of the audit firms who responded to this question. In addition, many of the local authorities who responded to the Call for Views didn't have strong opinions either way. Some thought that the opinion might be better presented in May, right at the start of the following financial year, but others expressed concern as to whether audit firms would have the capacity to handle a split reporting timetable.

6.3.11 A subsidiary, but still important, factor when considering the timing of the opinion is auditor resourcing. If the full benefits from the revised VfM opinion in the new Audit Code are to be realised, auditors will need to do more work.

6.3.12 Therefore, thinking about how to time the publication of the opinion so that it is of the most use, has the most impact, and can be supported by timely audit work must be a matter for serious consideration.

6.4 Practice in other jurisdictions

6.4.1 Audit requirements in other jurisdictions, for example Scotland, Wales and New Zealand provide alternative models, all of which provide practices that could help bridge the expectation gap between what auditors are required to do and what stakeholders expect them to do to assess financial resilience. The Review has explored New Zealand as it has a different model that is worthy of consideration.

6.4.2 Scotland and Wales have different models of value for money reporting, with Scotland's model requiring the auditor to assess future plans and Wales' model including the option for the auditor to undertake more focussed work on financial resilience as a separate engagement.

6.4.3 In New Zealand, there is no VfM opinion, but instead the financial audit opinion has been extended to cover a large number of pass/fail service delivery and financial resilience metrics. The financial resilience metrics are common to all authorities, allowing comparisons to be made.

6.4.4 Care needs to be taken when assessing the appropriateness of these models. There are currently 32 unitary authorities in Scotland, 22 unitary authorities in Wales and 78 local, regional and unitary councils in New Zealand compared to 343 local authorities in England. It may not be possible to scale-up practices that are appropriate in these jurisdictions to England in a coherent way or to do so at a reasonable cost.

Practice in Scotland

6.4.5 When scoping, planning, performing, and reporting on their 'best value' work, auditors in Scotland are required to consider four audit dimensions. The first of these, financial sustainability, interprets the short term going concern opinion and requires auditors to look *"forward to the medium (two to five years) and longer term (longer than five years) to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered."*

6.4.6 The results of VfM audits of Scottish local authorities tend to produce quite rich reports, which the Accounts Commission, the public spending watchdog for local government in Scotland, uses to identify and highlight key trends and risks across the sector. For example, the *Local Government in Scotland, Financial Overview Report 2018-19 (Dec 2019)*[15] found that Scottish councils were increasingly drawing down on their revenue reserves; and whilst all councils had medium term financial planning covering the next three to five years, long term financial planning had not improved since the last report.

[15] https://www.audit-scotland.gov.uk/uploads/docs/report/2019/nr_191217_local_government_finance.pdf

Practice in Wales

6.4.7 The value for money audit opinion an auditor of a Welsh local authority is required to provide is the same as that in England; that is an opinion on the "arrangements for securing economy, efficiency and effectiveness in its use of resources". However, the Welsh Code of Audit Practice requires auditors to review significant arrangements in place irrespective of whether material risks have been identified.

6.4.8 Where an auditor identifies notable financial resilience or other value for money concerns, the Auditor General for Wales has the statutory power[16] to publish a separate substantive report. These reports are publicly available on the Wales Audit Office's website and provide an in-depth assessment of the issues identified and the appropriateness of the plans that the local authority has to address these.

Practice in New Zealand

6.4.9 Local authorities in New Zealand are required to report performance in the Annual Report and Accounts against a range of financial prudence benchmarks specified in legislation. The auditor is required to report on the completeness and accuracy of the local authority's disclosures against these benchmarks. As all of the benchmarks have pass/fail thresholds, they lend themselves to a binary audit opinion.

6.4.10 The purpose of this statement is to disclose the Council's financial performance in relation to required benchmarks in order to assess whether the Council is prudently managing its revenues, expenses, assets, liabilities and general financial dealings. Although the benchmarks are backwards looking, five-year trend information is presented which helps the user of the accounts to understand how effective the local authority is in managing its financial resilience.

6.5 The audit of financial resilience – a new model for England?

Introduction

6.5.1 There is a significant gap between the reasonable expectations of many stakeholders and what the auditor is required to do when assessing the financial stability and resilience of local authorities.

6.5.2 To help bridge the expectation gap, the scope of audit should include a substantive test of a local authority's financial resilience and sustainability. Care and attention will need to be taken to define how the auditor should address historical, current and future financial sustainability issues, so that the engagement does not become overly burdensome or provide false comfort to stakeholders. In addition, expanding the scope of the audit will increase costs, and there needs to be a balance between those costs and the potential benefits of additional audit coverage and reporting.

6.5.3 However, cost should not be a deterrent in and of itself. The expansion of the opinion to encompass financial resilience and sustainability would, potentially, provide comfort to the authority and to council taxpayers that the finances are in good order. This

[16] under Section 17 of the Public Audit (Wales) Act 2004 and section 18 of the Local Government Wales Measure 2009

would represent a genuine demonstration of public accountability both from a local authority and from an audit perspective.

Form of the opinion

6.5.4 The revised narrative opinion proposed in the new NAO code should lead to a significant enhancement in the usefulness of auditor reporting. The 2020 Audit Code sets out three reporting criteria (para 3.10)[17]:

- Financial sustainability: *how the body plans and manages its resources to ensure it can continue to deliver its services;*
- Governance: *how the body ensures that it makes informed decisions and properly manages its risks; and*
- Improving economy, efficiency and effectiveness: *how the body uses information about its costs and performance to improve the way it manages and delivers its services.*

6.5.5 These criteria are not dissimilar to the four reporting pillars in the Scottish model. The pillar that auditors of English local authorities are not explicitly required to report on is financial management. It is unclear why this has been omitted but a possible reason is that an auditor would normally be expected to review material financial management controls as part of financial audit work.

6.5.6 The reporting requirements contained within the 2020 Audit Code will take time to settle down and embed and there will be a role for the regulator in identifying and promoting good practice. However, if practice develops as the NAO intends, the new reports should provide more useful information to stakeholders.

Work required to support an assessment of financial resilience

6.5.7 The 2020 Audit Code requires auditors to do less work to assess financial resilience than is required in either Scotland or Wales.

6.5.8 Specifically, auditors in England will not be required to test whether the body is planning effectively to continue to deliver its services or the way in which they would be delivered over the medium or longer time horizon as in Scotland. Nor will auditors be requested to review the design of significant arrangements to secure value for money, and, where appropriate given the assessment of risk, test the operating effectiveness of those arrangements as in Wales.

6.5.9 In addition to the factors mentioned in the Code, auditors could use the indicators of financial stress in the CIPFA publication, *Pillars of Financial Resilience*, as a key element of the risk assessment.

6.5.10 To support such an assessment the auditor could be required to critically assess and, in cases where significant risks are identified, test the CFO's Section 25 report along with any other statutory reports or management estimates that have an impact on medium or long term financial resilience. This testing could include an assessment

[17] https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2020/01/Code_of_audit_practice_2020.pdf

of whether there are clear plans for delivering savings, the usage rate for non-ringfenced revenue reserves and whether the local authority benchmarks its costs against nearest neighbours and takes appropriate action in response to variances, as set out in accordance with CIPFA's *Pillars of Financial Resilience*.

6.5.11 In addition, the auditor could explicitly be required to assess whether the local authority has complied in practice, and in spirit, with statutory guidance that it is required to "have regard to".

6.5.12 CIPFA's *Financial Management Code* is another model that provides a set of standards against which auditors could assess value for money and financial resilience. However, it is too detailed to assess without a considerable amount of additional audit work. Nevertheless, the principles in the *Financial Management Code* would enhance the consistency of local authority financial management. MHCLG could take the opportunity to give it statutory status when the opportunity arises and require local authorities to report on their compliance with it in their Annual Governance Statement. Since auditors are required to read the Annual Governance Statement to ensure it is consistent with their knowledge of the business this, combined with the enhanced resilience testing recommended, would require auditors to report material breaches.

6.5.13 Consideration has also been given to whether it would be appropriate to require a specific investigation. A more detailed report would enable specific VfM or financial resilience issues to be identified, as in the Welsh model. This is not recommended, as this element of the Welsh model is not applicable due to scale.

7. Financial reporting in local government

7.1 The purpose of financial reporting in the local authority sector

7.1.1 Financial reports provide information to people who seek to understand the performance of an entity. As most of the money that local authorities receive is provided from general or local taxation, it is reasonable to expect people outside the body who are interested in a local authority's financial performance to want to know how the money being managed is being spent. This includes knowing whether the local authority is performing effectively to achieve what was intended with this money.

7.1.2 Local taxpayers and service users do not have the power to require a local authority to produce bespoke financial information for them. Instead, they have to rely on the financial statements. They can inspect the financial statements and the underlying accounting records for a 30-day period that must comprise the first ten days in June. This means that to be relevant the information produced in local authority financial statements must meet the accountability and/or decision-making needs of users and be sufficiently transparent and understandable to allow them to ask appropriate questions.

7.2 Introduction to the framework

7.2.1 When producing financial reports, local authorities are required to have regard to the Statutory Code of Local Authority Accounting Practice ("the Accounting Code"), issued by the CIPFA. The Accounting Code is based on private sector accounting standards other than where they have been adapted for the specific circumstances of local authorities or where these are overridden by specific statutory requirements. As set out in **Figure 7.1**, Government retains the power to use secondary legislation either to override normal accounting practices or to require local authorities to include additional disclosures in their accounts.

Figure 7.1
Hierarchy of the Local Authority Accounting Framework

Primary Legislation	**Local Government Act 2003** Allows SoS to make provision about accounting practices that local authorities must follow.
Secondary Legislation	**Capital Finance and Accounting Regulations 2003** Gives CIPFA the power to produce a statutory accounting code. Introduces statutory overrides to private sector accounting practices; which must be reflected in the accounting code.
Statutory Code of Practice	**CIPFA Accounting Code of Practice** Statutory code setting out proper practices for local authority accounting in England.

7.2.2 When implementing, adapting or interpreting accounting standards, the Code seeks to maintain consistency with other parts of the UK public sector. Preparation of the Code is overseen by the CIPFA/LASAAC Accounting Code Board, which comprises representatives of all the key stakeholder groups. MHCLG has observer status on this Board.

7.2.3 This Accounting Code board does not act in isolation. Its decisions are reported to the Financial Reporting Advisory Board (FRAB), which advises HM Treasury on public sector accounting. In practice, both the annual update to the Accounting Code and any amendments or adaptations to accounting standards for the local authority sector need to be considered at FRAB as well as at the CIPFA/LASAAC Board.

7.2.4 The Accounting Code applies to Principal Councils, PCCs, Chief Constables, FRAs, the GLA, Mayoral Combined Authorities, Passenger Transport Executives and National Park authorities in England. It also applies to similar authorities in Wales, Scotland and Northern Ireland, although the legislative framework for these authorities is different and they are outside the scope of this Review. The Code does not normally apply to subsidiary companies consolidated into local authority accounts. Such companies use the applicable private sector accounting framework.

7.2.5 The Accounting Code is updated annually, and a new edition is published each financial year. Purchasing the 2019-20 Code from CIPFA costs £340 (hard copy) or £710 (online copy). CIPFA's sales numbers demonstrate that at least one third of local authorities do not purchase an Accounting Code in any given year.

7.2.6 The Accounting Code does not apply to smaller authorities, for example Parish Councils, Ports Authorities or Independent Drainage Boards with gross income or expenditure of less than £6.5m per annum (which is currently all but one of them). The accounting and governance framework for these authorities is set by an organisation called the Joint Panel on Accountability and Governance (JPAG), which comprises representatives of all of the key stakeholder groups. Smaller Parish Councils fill in a simplified financial return on a receipts and payments basis. Further discussion of smaller authorities is included in **Chapter 8**.

7.3 Format of local authority accounts

7.3.1 Local authority accounts are very lengthy compared to accounts in other sectors, typically numbering in excess of 50 pages for shire districts and more than 80 for upper and single tier local authorities. They have more primary statements than central government and private sector accounts. **Figure 7.2** shows the primary statements and supplementary accounts that the user can expect to find in a set of local authority accounts.

7.3.2 Local authority accounts are arguably more complex and more challenging for a service user to understand than accounts produced by other parts of the public sector. This is primarily because there is a difference between the budget analysis of information for council tax purposes and the statutory basis of year end accounts.

Figure 7.2

Local Authority Accounts – Primary Statements and Supplementary Accounts

Statement	Purpose
Comprehensive Income and Expenditure Statement (CIES)	Summary of the resources generated and consumed by the council on an accruals basis. Shows gross and net expenditure by service area and other income and expenditure incurred by the council.
Movement in Reserves Statement (MIRS)*	Shows how the movement in reserves in the Balance Sheet is reconciled to the CIES deficit and what adjustments are required to be charged to the general fund balance for Council Tax setting purposes.
Balance Sheet	Sets out the Council's financial position at the year end.
Expenditure and Funding Analysis (EFA)*	Summarises the annual expenditure used and funded by the Council together with the adjustments between the funding and accounting basis to reconcile with the CIES.
Cashflow Statement	Summarises the inflows and outflows of cash for revenue and capital transactions during the year.
Collection Fund Account* • Billing authorities	Agent's statement that reflects the statutory obligation for billing authorities to maintain an account showing collection of Council Tax and National Non-Domestic Rates (NNDR) and the distribution of these taxes to precepting authorities.
Housing Revenue Account (HRA)* • LAs with social housing stock	Local authorities are not allowed to cross subsidise provision of social housing from general taxation or vice versa. The HRA shows the major elements of expenditure on social housing and how these costs are met.

** Statements unique to local authority accounts*

7.3.3 Local authorities calculate their annual council tax requirement through setting a "balanced budget". The balanced budget calculation that local authorities are required to make is specified in primary legislation and is undertaken on a receipts and payments basis. Following the adoption of accruals accounting[18] by the local authority sector and as IFRS have continued to develop, successive governments have sought to protect council taxpayers from accruals movements that do not have an immediate impact on the costs of service delivery. They have done this through introducing statutory overrides.

7.3.4 The most significant of these statutory overrides relates to depreciation. Local authorities are required to charge depreciation on assets in the same way as any other entity. They then reverse out the depreciation charge in the Movement in Reserves statement (MIRS) and replace it with a prudent provision for the debt taken out to acquire assets (Minimum Revenue Provision).

[18] Accruals accounting is a form of accounting where you recognise the economic cost of assets and liabilities over the period when benefits accrue. For example, if you are using accruals accounting and buy a car that you expect will last five years you would split the purchase cost of that car over five years. By comparison if you are accounting on a receipts and payments basis you would recognise the full cost of the car in the year you pay for it.

7.3.5 The adjustments process has two consequences. Firstly it substantially increases the length of local authority accounts as the financial statements report some transactions on both an accruals basis (through the CIES) and a funding basis (through the EFA and MIRS) and include notes reconciling the two; and secondly, unlike for financial statements produced by other sectors, neither the CIES nor the Balance Sheet shows the true financial position of a local authority. To understand that position it is necessary to understand how the outturn reported in these statements reconciles to the basis on which the balanced budget calculation is made.

7.3.6 In addition to the statements in **Figure 7.2**, those local authorities who are also "administering authorities" for local authority pension funds are required to publish full Pension Fund accounts in the same document as their local authority accounts. The Pension Fund accounts are audited as a separate audit engagement. This further lengthens the document and means that the audited accounts cannot be published as final until both the local authority audit and the pension fund audit have been completed. The sector has asked MHCLG to look at decoupling the local authority and pension fund accounts. However, it is not possible to do this without primary legislation.

7.4 Usefulness, understandability and transparency of local authority accounts

7.4.1 The Annual Accounts that each local authority must prepare are prescribed in detail and relevant standards must be observed in the preparation of the statutory accounts and financial report. IFRS cover both the public and private sectors so auditors seek to adhere to those principles when auditing local authority accounts. There is widespread agreement that the resultant accounts are not transparent or easily understandable.

7.4.2 Local government practitioners argue that the extent and nature of asset valuations, very relevant in a commercial setting, undertaken by auditors, have limited significance in local government where assets are more often than not critical to service delivery and "market value" is not a consideration. Time allocated to the asset valuation process for property and pensions, it is agreed, is considerable and increases the cost of audit as well as, in some cases, leading to delays in the audit being finalised. Underlying this point is the question of whether IFRS should continue to be a key element of local authority statutory accounts.

7.4.3 An issue related to the concern in local government about the complex local authority accounting arrangements is the capacity of the external auditor to test and validate technically intricate accounting treatment without a familiarity with local authority finance and accounting. Such an assertion by local government is not universal but it is a concern of many. However, the audit community, whilst recognising that there has been depletion in the number of auditors who served in the District Audit Service, is confident it has necessary skills and resources to fulfil the role.

7.4.4 As highlighted in **Chapter 4**, there is evidence of market stress in the supply of appropriately experienced and qualified local authority auditors. Some auditors have also argued that local government itself does not always have accounting staff with the technical expertise to complete the final accounts without guidance and support from external audit.

7.4.5 That the local authority accounts are very complex is not in dispute. There is wide acknowledgment from all stakeholder groups that the annual financial statement of accounts is understandable only to those with the necessary technical and professional knowledge of local authority accounts. When asked whether local authority accounts allow the user to understand an authority's financial performance and its financial resilience, 93% of respondents said no.

7.4.6 Whilst some local authority respondents argued that the understandability of the accounts is not an issue, because service users and taxpayers can take assurance from the fact that they are prepared and audited to internationally recognised standards, it is questionable whether this is a defensible position.

7.4.7 The lack of transparency and understandability of local authority accounts raises a fundamental and serious challenge in terms of transparency and public accountability. Potential users extend beyond councils, government and auditors. Key stakeholders include council taxpayers/service users, the general public, academia, the media and local authority partners and contractors. Without an appropriate level of transparency these users may not have the information to challenge their local authority effectively. The rigour underpinning local authority accounting and auditing may not be at issue but the accounts, as currently structured and presented, do not enable the public to understand how local authorities are stewarding public funds.

7.5 Options for reform

7.5.1 There are three broad options for enhancing the transparency and usefulness of local authority financial statements, so that they better serve the needs of a wider group of stakeholders. These are:

- Review of IFRS as a basis for the preparation of local authority accounts.
- Expansion and standardisation of the current narrative statement.
- Introduction of a new summary statement presented alongside the IFRS accounts.

7.5.2 The underlying purpose of all three options is to strengthen financial transparency and accountability by providing a simplified presentation that is more relevant to stakeholders. All options have costs associated with them but these need to be set against the benefits of that increased transparency.

Review basis on which accounts are prepared

7.5.3 CIPFA could be asked to review the basis of accounts, with the aim of updating the Accounting Code so that the transactions presented in the annual financial statements are prepared on the same basis as the annual budget approved by Full Council.

7.5.4 If followed to its logical conclusion, this would allow local authorities to prepare simplified accounts that could be easily reconciled to the annual budget. If accounts are presented on a funding basis, the reconciliations between the funding and accounting basis would no longer be required. In addition, many of the lengthier notes to a set of financial statements, such as the financial instruments disclosures, are mainly required to support IFRS disclosures and could be removed or simplified. This would lead to much shorter documents.

7.5.5 There are some issues that would have to be addressed with this recommendation. Firstly, designing and implementing a new accounting framework would be challenging. CIPFA could go back to the pre-2010 near cash accounting framework, but it is questionable whether this would be appropriate. Many local authorities are far more commercial in their operations and have far more leveraged balance sheets than in 2010, so removing much of the accounting for long term assets and liabilities could present a misleading picture of financial resilience to service users. It could lead to local authorities to leveraging their balance sheet yet further, storing up potential financial problems for future years.

7.5.6 Secondly, there is the perception risk of such a step. There could be a perceived disconnect if local authorities reverted to cash accounting at the same point that some are becoming more commercial, taking on more debt to invest in assets acquired solely or partially to generate a return.

7.5.7 Thirdly, moving away from IFRS accounting would create consistency problems between various parts of the public sector. The Accounting Code applies to Scotland, Wales and Northern Ireland as well as to England. If English local government moved to a near cash accounting framework, the other UK jurisdictions would face the decision of mirroring that move or else the Accounting Codes would need to diverge. In addition, the results of UK local government bodies are consolidated into the Whole of Government Accounts, which are prepared on an IFRS basis. If English local authority accounts moved to a near-cash accounting basis, those authorities would in practice be required to maintain financial records and prepare accounts on two bases: on a near-cash basis for their own accounts and an IFRS basis for consolidation into WGA. This would impose considerable additional cost.

7.5.8 Finally, the UK public sector is held up as applying a gold standard of accounting, primarily because it is one of the few to apply IFRS fully. If part of the sector moved away from this it could generate considerable reputational risk. As a result, HM Treasury and FRAB may well oppose any significant modification of the English local authority accounting framework.

Expansion and standardisation of the narrative statement

7.5.9 The framework for local authority annual reports and accounts is unusual in that, although local authorities are required to prepare an annual report, it does not include any mandatory disclosures. In 2015 CIPFA launched the “Telling the Story” initiative, which encouraged local authorities to use the annual report to accurately reflect financial and service performance. Some local authorities have produced innovative and informative annual reports following the launch of this initiative, but performance varies, with other authorities making minimal disclosures. In addition, because “Telling the Story” does not include mandated standards or disclosures it is not consistent across authorities.

7.5.10 By comparison, the UK Central Government Financial Reporting Manual (the "FReM") requires all central government reporting entities to prepare a Performance Report and an Accountability Report, both of which are based on Companies Act requirements as adapted for the public sector and contain mandated disclosures.

7.5.11 A similar approach could be adopted for local authority accounts. In this model, local authorities could be required to include a Performance Report in their annual report and accounts containing a reconciliation between the approved budget and year-end service expenditure, along with explanations for significant variances and the impact of the variances on revenue reserves, prepared on a budget setting basis whilst being reconcilable to the statutory accounts. Potentially this could be supplemented with standardised service delivery metrics and an explanation of longer-term risks and mitigations linked to key financial management strategies such as the Mid-Term Financial Plan, as appropriate.

7.5.12 The proposed Performance Report could be a transparent element of a local authority's Annual Report and Accounts, which discloses what the local authority planned to spend on each major service area, what it actually spent, where there were significant variances between the two what the reasons were, and what impact that has had on the reserves available to support the following year's expenditure. With the addition of service delivery metrics, the Report could also start to give an indication of what service users and taxpayers have got for their money. If the financial information and performance metrics are prepared to common standards, this could start to bring a degree of comparability between authorities, which could promote improvements in the effectiveness and efficiency of service delivery.

7.5.13 Finally, if the reconciliation between budget and outturn is presented in the Annual Report, it may be possible to remove or reduce the MIRS, the EFA and supporting disclosures. This could offset the increased work required to produce the new Performance Report.

7.5.14 There are some challenges with this approach:

- it would mean extending the scope of the audit engagement, particularly if the auditors are required to form an opinion on non-financial information.
- if non-financial service delivery metrics are subject to audit they will need to be prepared and disclosed on a consistent basis. It will be necessary to identify appropriate metrics across a range of service areas, a process that could take time. In addition, including metrics for all of the services that a local authority provides would require very lengthy disclosures.
- if included in a long Annual Report and Accounts document, there is no guarantee that this statement would be any more visible to the general public than the current financial statements are.
- there is a risk that some local authorities use the narrative element of such a statement to present an overly positive view of their achievements and finances.

Introduction of a new summary statement

7.5.15 A variation in part, and a replacement of the enhanced narrative statement, is to leave the current local authority accounts largely unaltered and instead require the production of Summarised Accounts, prepared on the budget setting basis. As with the enhanced narrative statement, the Summarised Accounts would need to be reconcilable to the Statutory Accounts and be subject to audit to have credibility.

7.5.16 Statutory Guidance would need to be developed to set out the form and content of the Summarised Accounts. Potentially they could contain:

- A statement of service information and costs prepared in a standard format and to a standardised framework. The most appropriate framework would probably be the statutory Service Reporting Code of Practice (SERCoP).
- Comparison between budget setting information and outturn performance.
- A degree of detail to encompass all key service expenditure heads; where appropriate this could be extended to present unit cost information. A simplified balance sheet, including some form of assurance relating to non-ringfenced revenue reserves and debt levels and borrowing plans, with the latter linked to the Prudential Framework disclosures, could also be produced.
- A brief narrative. This could be limited to a financial commentary comprising explanations of significant variances between budget and outturn along with an assessment of the impact on medium term financial sustainability. It may also be possible to include a brief description of outcomes though this would need to be linked back to the objectives set when the annual budget was approved.

7.5.17 The aim of this document would be to present a statement aimed at the local community rather than as a basis for compiling national statistics. Because of differences between local authorities, comparability would be difficult and potentially misleading. Local authorities could be asked to think about a range of communication methods to reach their local communities more effectively.

7.5.18 The summary accounts would be a vehicle to increase transparency. As this would be a short stand-alone document, it would be much more accessible to taxpayers and service users.

7.5.19 Local authorities would have to reconcile outturn between the funding basis and IFRS accounting basis. However, the value of disclosing these reconciliations could be reassessed, potentially allowing the MIRS, the EFA and supporting disclosures to be discontinued. This could allow the statutory financial statements to be prepared on an IFRS basis without statutory adjustments.

7.5.20 Finally, consideration would need to be given as to the level of audit required for the Simplified Statements, and the agreed procedures that auditors would be required to undertake to provide assurance over reconciliations between the IFRS Financial Statements and the Simplified Financial Statements, that are not disclosed in either.

8. Smaller authorities

8.1 Introduction

8.1.1 Smaller authorities are defined in the 2014 Act as an authority where the higher of gross annual income or expenditure does not exceed £6.5 million for three years (or one or two if the authority has not existed for three years). Currently there are just under 10,000 smaller bodies, only one of which has to prepare a full set of IFRS compliant accounts and undergo a full audit.

8.1.2 There are different types of smaller authority with a varied range of responsibilities and powers:

- Local councils including Parish, Town, Village and Community Councils and parish meetings. Some common responsibilities can include, but are not limited to, commons and open spaces, car parks, lighting, footpaths, leisure and sports facilities, litter bins, and tourism activities. Some of these services are delivered on behalf of the unitary and district councils.
- IDBs which are responsible for managing water levels including managing flood risks and land drainage.
- Other smaller authorities such as charter trustees, port health authorities, conservation bodies and crematorium boards.

Smaller authorities are financed primarily through a precept which is collected as part of council tax by the unitary or district council. They can also apply for grants and awards.

8.1.3 Governance arrangements depend on the type and size of the authority. All local authorities are required to have a clerk; however, for small authorities, this could be their only employee or may be a volunteer or part-time worker. Roughly two-thirds of smaller authorities have a single employee, and some don't have any employees. The clerk is analogous, in part, to a CFO in a principal authority, as there is a requirement to give guidance to councillors, in many cases carrying out the role of the Finance Officer. Smaller authorities must publish the statement of accounts together with any certificate or opinion provided by the local auditor[19].

8.2 Scale of audit

8.2.1 Smaller authorities are not required to produce IFRS based accounts but instead produce a simplified statement of account on a receipts and payments basis. Some larger Parish Councils present accruals-based accounts alongside this, although these are unaudited. As set out in **Figure 8.1**, smaller authorities are either exempt from audit or undergo a 'limited assurance engagement'. As the name suggests, this provides less assurance than a full-scale audit.

8.2.2 While most authorities with an income or expenditure of up to £25,000 are exempt from audit, a request can be made for a 'limited assurance engagement' from SAAA who will then appoint an auditor to undertake this work. More than 100 bodies have chosen to do this.

[19] The Accounts and Audit Regulations 2015
https://www.legislation.gov.uk/uksi/2015/234/pdfs/uksi_20150234_en.pdf

Figure 8.1

Table of audit thresholds and associated requirements for smaller authorities [20]

Level of income or spending	Form of external assurance to be provided from 2017-18 onwards	% of smaller authorities in each band
More than £6.5 million.	'Full audit' under international auditing standards.	0.01%
Up to £6.5 million but more than £200,000 (accounts on income and expenditure basis)	Limited assurance engagement but may opt for 'full audit'.	11%
Up to £200,000 but more than £25,000 (accounts can be on either receipts and payments or income and expenditure basis)	Limited assurance engagement but may opt for 'full audit'.	31%
Gross income or gross expenditure up to £25,000	Exempt from audit and limited assurance engagement in most cases, subject to the authority certifying that it is exempt. Work by an auditor may still be needed in certain circumstances – notably if there are objections to the accounts.	58%
No financial transactions and no accounts	Exempt from audit and limited assurance engagement in most cases, subject to the authority certifying that it is exempt.	

8.2.3 Smaller authorities are also required to undertake an internal audit to evaluate the effectiveness of its risk management, control and governance processes[21]. Quality of internal audit staff is said by some respondents to be variable, which has the potential to cause issues for the external audit.

8.2.4 One of the trends in recent years has been the transfer of assets and associated running costs to Parish Councils. If smaller authorities are given more responsibility, or if the spending of smaller authorities were to change to where many such authorities approach the £6.5 million threshold, the current accountability arrangements may no longer be appropriate. The assurance levels may need to be reviewed by MHCLG. This is especially pertinent as smaller authorities are not bound

[20] NAO AGN02 Specified Procedures for Assurance Engagements at Smaller Authorities https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2015/03/Auditor-Guidance-Note-02-Specified-Procedures-for-Assurance-Engagements-at-Smaller-Authorities.pdf

[21] The Accounts and Audit Regulations 5(1) 2015https://www.legislation.gov.uk/uksi/2015/234/made#:~:text=5.,internal%20auditing%20standards%20or%20guidance.

by council tax referendum rules[22] and can raise their precept by the amount they consider necessary.

8.2.5 In 2020, one IDB met the threshold for preparing full statutory accounts. Available evidence suggests that this is the first occasion of this happening. The cause of the IDB's increase in income and expenditure was the capital grants it received and, as such, the requirements for a full code audit may be temporary. PSAA and the Association of Drainage Authorities (ADA) have worked with the authority to find a new auditor as the previously appointed auditor does not qualify under the statutory framework to undertake full audits. This also resulted in an increased audit fee, from less than £5,000 to £40,000. Producing full IFRS accounts will considerably increase the amount of internal work required by the IDB and this is likely to represent a challenge to its available skills and infrastructure.

8.3 Procurement of audit

8.3.1 Prior to 2017, smaller authorities were included in the audit contracts let by the Audit Commission in 2014 that were taken over by PSAA through the transitional arrangements. SAAA was designated as an appointing person under legislation[23] by the Secretary of State to take over this role from 2017-18. SAAA is an independent, not for profit company. SAAA was set up by the National Association of Local Councils (NALC), Society of Local Council Clerks (SLCC) and the Association of Drainage Authorities (ADA). Although smaller authorities have the same power to appoint their own auditors as principal authorities, in practice, all smaller authorities opted in to SAAA's procurement. SAAA has appointed external auditors for a 5-year period from 1 April 2017.

8.3.2 SAAA's procurement comprised 17 equally sized lots. Other than for IDBs, which were grouped together, lots were geographically based. The SAAA procurement was based on price once a supplier had met a minimum quality threshold. There were five firms that met this threshold. The result of this exercise was that 15 were awarded to a single audit firm and two other firms won one lot each. This met SAAA's declared objective of having a minimum of three firms in the market. Of the three firms, two had previously held contracts with PSAA and one re-joined the market. With regard to the quality and price ration for appointing auditors, SAAA believes that once a certain threshold is reached, it is very difficult to differentiate between firms on the basis of quality.

Fee scale

8.3.3 SAAA's fee scale is based on 15 bands of income or expenditure (whichever is higher). Audit Commission and then PSAA, through the transitional arrangements, also used this fee scale. Exempt authorities do not pay an audit fee. Authorities with income or expenditure of between £25,000 and £50,000 pay an audit fee of £200. Fees rise in stages up to a maximum of £3,600 in cases where income or expenditure is more than £5 million but less than £6.5 million.

[22] The Local Authorities (Conduct of Referendums) (Council Tax Increases) (England) Regulations 2012 https://www.legislation.gov.uk/ukdsi/2012/9780111519035/regulation/3
[23] The Local Audit (Smaller Authorities) Regulations 2015 https://www.legislation.gov.uk/ukdsi/2015/9780111126103

8.3.4 The scale fees paid by smaller authorities for their audit have remained unchanged for the past 12 years. There have been savings for those smaller authorities that, from 2017, could declare themselves as exempt and, therefore, did not have to pay for an audit.

8.3.5 This audit fee model relies on larger authorities supplementing the cost of audit work for smaller authorities. As there are 15 bands of fees, there may be councils receiving the same level of audit work whilst paying different amounts. Although this may offer the most efficient method of payment to ensure audit is affordable for all smaller authorities, the banding system may warrant review.

8.3.6 Overall, smaller authorities seem content with the level of audit fees they pay. The only area of concern raised related to capital grant funding. Two Parish Councils raised concerns that the impact of the rising scale fee could be a deterrent for local authorities investing in future capital schemes in the local community.

Fee variations

8.3.7 Smaller authorities may be subject to variations to the scale fees set out above if additional work is needed. Some of this work is costed as a fixed supplement of the fee scale and some is charged at fixed hourly rates. SAAA agreed a maximum hourly rate for additional work and this is published on their website. Examples of where fee variations may be charged include the auditor considering objections to the accounts from local electors, and where special investigations are undertaken.

Quality

8.3.8 There is no indication that the smaller authority audit market is encountering delayed audit opinions, as is the case for larger authorities. SAAA use trackers completed by the firms to collate and analyse key management information to track and report on the management, delivery and the outcomes of limited assurance reviews. SAAA also reviews the underlying data quality and system interfaces on a light touch risk basis.

8.3.9 In carrying out its quality assurance role, as set out in the Appointing Person Legislation, SAAA review and test the firms' internal quality assurance processes and contract compliance systems (quality aspects) to ensure the delivery of good quality reviews. An overall rating for both quality of limited assurance review work and contract management, compliance and data quality is provided. The findings of this process are reported to each firm and to SAAA's Board. They do not publish these findings, though they maintain the right to do so.

8.3.10 A very small number of smaller authorities responded to the Call for Views; therefore, it must be stressed that the following comments are not necessarily reflective of the sector. One Parish Council commented that the arrangement with SAAA made it feel that the auditor didn't consider the council to be its customer. Similar feedback has been received concerning PSAA's role. It also commented that it felt the quality of their audit was very poor and that it added no value. This may be in part due to the framework of limited assurance audit for smaller authorities and a resulting 'expectation gap'. The Review is unable to corroborate whether this is a commonly held view.

8.3.11 Two other Parish Councils questioned whether auditors provided the right level of assurance. One commented that larger Parish Councils should be held to the same standards for financial reporting, transparency and accountability as those applied to principal authorities of equivalent size. The council linked this to the fact that some councils are playing an increasingly significant role in their communities. It is true that there are currently three smaller authorities that have an annual income or expenditure of over £5 million which is similar to the smallest Category 1 authority which is subject to a full audit. However, there are not many Category 1 authorities that are this small. The other respondent was specifically concerned about governance and financial transparency within the council and the lack of clarity on spending.

8.4 Accountability

8.4.1 In addition to producing a financial return, most smaller authorities are subject to transparency requirements. There are two Transparency Codes; authorities with an income or expenditure of £200,000 or more are included in the same mandatory Transparency Code[24] as principal authorities. Exempt authorities are subject to a specific smaller authority Transparency Code[25], made mandatory in April 2015, that:

"will enable local electors and ratepayers to access relevant information about the authorities' accounts and governance".

8.4.2 Authorities with income and expenditure under £200,000 but above £25,000 are expected to follow the same requirements but it is not mandatory. As these authorities are subject to audit, the transparency code was not considered to be applicable. Such difference in approach may warrant further attention. However, Commitment 8 in the governments UK National Action Plan for Open Government[26], sets out the government's plan for local transparency which includes MHCLG developing proposals to:

"help and encourage councils to publish all the information they can".

Objections

8.4.3 Local objections can be made to an item of expenditure in a smaller authority's finance return. It is very difficult to ascertain how many objections to the accounts smaller authorities receive, as the auditor is required to respond, by statute, only to the objector. As a result, most objections are never made public, the exceptions being if an objector choses to publish a response or the investigation leads to a Public Interest Report. However, one authority reported over 100 objections in a single year. NALC commented that several authorities at the smaller end of the income and expenditure level are consistently subject to objections, sometimes by the same individual or group of objectors.

[24] Local Government Transparency Code 2015
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/408386/150227_PUBLICATION_Final_LGTC_2015.pdf

[25] Transparency Code for Smaller Authorities
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/388541/Transparency_Code_for_Smaller_Authorities.pdf

[26] 2019-2021 UK National Action Plan for Open Government
https://www.opengovernment.org.uk/resource/uk-national-action-plan-for-open-government-2019-2021/

8.4.4 The auditor is responsible for reviewing all objections that meet the statutory requirement. In deciding whether to investigate, the auditor has to review the objection, which will result in a cost to the authority (not exceeding the maximum hourly rates as specified by SAAA) even if they do not subsequently pursue an investigation.

8.4.5 The auditor can refuse to investigate an objection[27] if:

- the cost of dealing with the complaint would be disproportionate to the underlying sum;
- the objection is frivolous or vexatious; or
- it is a repeat of a complaint made in a prior year of account.

8.4.6 A number of smaller authorities receive repeat or vexatious complaints. Where an authority receives such a complaint, it can choose to terminate communication with the complainant. However, if that individual raises an objection, an auditor must consider it to see if it is something to be pursued. This work incurs a supplement to the scale fee as set out by the SAAA. Given the size of many smaller authorities, objections can be proportionately very costly, both in terms of additional fees paid to auditor firms and in terms of resources that the authority requires to support, appropriately, the objection process. As with larger authorities, outstanding objections can cause a delay in issuing the audit opinion

8.4.7 The objections regime does provide a solid basis of accountability and ensures the auditor investigates potential issues further, to supplement the 'limited assurance' audit. There may be cases where the system is misused. Consideration should be given to provide more support to auditors to enable them to identify repeat or vexatious objectors in a more efficient manner.

Public Interest Reports

8.4.8 External auditors have a duty under the 2014 Act to consider whether to issue a report where there has been a significant matter identified that needs to be addressed in the interests of the public. There are more PIRs issued for smaller authorities than there are for larger authorities. SAAA publishes reports from the 17/18 financial year on their website, and previous financial years are available on the archived PSAA website.

Figure 8.2

Smaller Authorities - Reasons why a PIR was issued

	16/17	17/18	19/20
Failure to produce an annual return (for 16/17) or an AGAR (from 17/8 onwards)	16	22	23
Criteria submitted for exemption not all satisfied	N/A	0	8
Other	6	1	0
Total	22	23	31

The "other" category includes issues relating to governance, fraud, employment law, and non-compliance with VAT regulations.

[27] NAO Local Authority accounts: A guide to your rights https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2015/03/Council-accounts-a-guide-to-your-rights.pdf

8.4.9 One authority had a PIR issued for all three years for failure to produce an annual return or annual governance and accountability returns (AGAR), and a further seven authorities had a PIR issued in two of the three years for the same reason. Failure to produce an AGAR from 2017/18 triggers a statutory recommendation to the authority from the external auditor that it should submit an approved AGAR within 42 days. A public interest report is then issued if the authority fails to do so.

8.4.10 Out of the six PIRs issued in 16/17 that were *not* due to a failure to produce an annual return, four of them related to work carried out by auditors in response to objections raised by a local elector. In one authority's case, it received objections on a multitude of issues with one issue (ineffective internal audit and other governance failings) receiving a number of objections.

8.4.11 If a smaller authority chooses not to engage with external audit recommendations or PIRs, there is no mechanism, other than through local elections, to hold smaller authorities to account. The LGSCO investigates complaints against larger local authorities, but this does not extend to Parish Councils. If MHCLG wishes to devolve more powers to smaller authorities or smaller authorities increase their spending considerably, MHCLG should consider further accountability arrangements for smaller authorities.

8.5 Financial Reporting in Smaller Authorities

8.5.1 Smaller authorities that are able to declare that they have had had no financial transactions in the year of account do not need to prepare accounts. Instead they can send a declaration that they are exempt to their auditor.

8.5.2 Smaller authorities that cannot declare themselves exempt have to prepare an Annual Governance and Accountability Return (AGAR). The AGAR, which is freely available and updated annually is prepared by an organisation known as the Joint Panel on Accountability and Governance (JPAG).

8.5.3 JPAG is responsible for issuing proper practices about the governance and accounts of smaller authorities. Its membership consists of sector representatives from the National Association of Local Councils, the Society of Local Council Clerks and the Association of Drainage Authorities, together with stakeholder partners representing MHCLG, the Department of Environment, Food and Rural Affairs, CIPFA, the NAO and a representative of the external audit firms appointed to smaller authorities.

8.5.4 The AGAR has a number of sections. In order these are:

a. Guidance notes on how to complete the template and what information needs to be published on the authority's website.
b. The Annual Internal Audit Report.
c. Section 1: The Governance Statement.
d. Section 2: The Accounting Statement, which is prepared on a receipts and payments basis.
e. The External Auditor Report and Certificate.

8.5.5 Each non-exempt smaller authority is required to complete parts b, c, and d of the AGAR and send it together with a bank reconciliation and an explanation of any variances between the budget and the outturn to the auditor. The template itself is quite short, but fairly busy, with detailed guidance included in each section.

8.5.6 Under the Accounts and Audit Regulations 2015, authorities must publish the following information on a publicly accessible website. Before 1 July, smaller authorities must publish:

- Notice of the period for the exercise of public rights and a declaration that the accounting statements are as yet unaudited;
- Section 1 - Annual Governance Statement, approved and signed; and
- Section 2 - Accounting Statements, approved and signed.

8.5.7 Not later than 30 September, smaller authorities must publish:

- Notice of conclusion of the audit;
- The External Auditor Report and Certificate: and
- Sections 1 and 2 of AGAR including any amendments as a result of the limited assurance review.

9. Conclusions

9.1 During the course of this Review it has become increasingly apparent that the current local audit arrangements fail to deliver, in full, policy objectives underpinning the 2014 Act. As a result, the overriding concern must be a lack of coherence and public accountability within the existing system. For local audit to be wholly effective it must provide a service which is robust, relevant, and timely; it must demonstrate the right balance between price and quality; and be transparent to public scrutiny. The evidence is compelling to suggest that the current audit service does not meet those standards.

Key Factors Determining the Outcomes of The Review

9.2 In reaching the outcome and recommendations for this Review the following key factors have been taken into account:

- providing clarity of purpose in local audit;
- giving emphasis to performance and accountability in local audit framework;
- maintaining and improving the stability of the local audit market;
- reaffirming the importance of the auditing and accounting staff having the requisite skills, training and experience to fulfil their roles;
- improving and strengthening the governance arrangements underpinning effective local audit;
- developing coherence and coordination in the procurement and effective delivery of audit performance within a clear and consistent accountability framework;
- engaging key stakeholders in regular dialogue as an aid to maintaining an effective local audit service; and
- providing transparency in financial and external audit reporting to reinforce public accountability.

Local Audit

9.3 As currently configured the local audit market is vulnerable, due in no small part to the under-resourcing of audit work required to be undertaken within the contract sum. In addressing this weakness, a fundamental review of the fee structure is necessary. Evidence suggests that audit fees are at least 25% lower than is required to fulfil current local audit requirements effectively. Concerns reported about variable levels of knowledge and experience of local government finance and accounting demonstrated by auditors must also be addressed. The skills and competencies of auditors must also be paramount if the full extent of audit requirements are to be delivered satisfactorily. The current audit deadline of 31 July is viewed as unrealistic and in the light of the evidence presented by the Call for Views, there is a compelling argument to change this date to 30 September. The procurement arrangements must acknowledge these factors and it is essential that the audit performance regime offers assurance to the public that true accountability has been served.

9.4 Attention has been given to whether the existing local audit framework might be improved to achieve these objectives. The roles and responsibilities of all relevant bodies should be reviewed to respond to the concerns expressed in this report. However, the key challenge is the underlying weakness of the current arrangements where there is no coordination and regulation of local audit activity. This is a role best discharged by a single overarching body.

9.5 A single body would embrace all aspects of local audit incorporating procurement, contract management, the code of local audit practice, accountability for performance, oversight and regulation. Clarity of purpose, consistency and public accountability would be essential features of this approach and the expertise and skills of those currently providing these services would be harnessed and maintained in the new body.

9.6 The Review has highlighted a potential weakness in the way in which audit outcomes are considered and presented to both the local authority and the public. The ability of Audit Committees, which mostly lack independent, technically qualified members, to consider, effectively, audit reports has been challenged in responses to the call for views. In addition, transparency and accountability of audit reports, from a public perspective is lacking and there is considerable scope for the Key Audit Partner to present a report on the principal issues arising from the audit to Full Council at least annually.

9.7 The situation facing PCCs and FRAs is many ways similar to those for principal councils in that audit quality and price are in need of review. Governance here, however, is somewhat different in terms of reporting lines and public accountability as these are currently more transparent than those applying in Principal Authorities.

9.8 Parish Councils, Meetings, IDBs and other smaller authorities operate on a much smaller scale and procurement/contractor arrangements are overseen by SAAA where no serious concerns have been identified. However, there is scope here to improve public reporting of local audit outcomes and attention should be given to 'turnover' thresholds in order to ensure a proportionate level of resource is utilised in fulfilling audit requirements.

9.9 An area that has generated considerable comment is the perceived gap between the reasonable expectations of many stakeholders and what auditors are required to do relating to the financial stability and resilience of local authorities. There is a compelling argument to extend the scope of audit to include a substantive test of financial resilience and sustainability. The scope of this audit needs to be clearly defined and focused to ensure there is a balance between cost and the potential benefits of such additional audit coverage and reporting. This would represent a genuine demonstration of public accountability.

9.10 The new NAO code includes a revised narrative audit opinion and sets out three reporting criteria relating to financial sustainability, governance and improving economy, efficiency, and effectiveness. This approach, once fully established, will provide a very important statement to stakeholders regarding a local authority's financial health. In effecting this scrutiny of financial sustainability, the auditor would also undertake an assessment of the risks identified in the CFO's annual Section 25 report of the budget. This could be further assisted by a review of the local authority's observance of CIPFA's Financial Management Code which provides a set of statements including value for money and financial resilience. To ensure that the Auditor's work is genuinely transparent and accessible to local taxpayers an Auditor's Report should be presented to the first Full Council meeting after 30 September every year, irrespective of whether the financial accounts have been certified.

Transparency of Financial Reporting

9.11 This report has highlighted the inability of the general public to understand the annual statutory accounts presented by local authorities. The technical complexity of the accounts means that service users/council taxpayers have little or no opportunity to comprehend what is being said or to challenge expenditure and income relating to a specific service and how the local authority has performed.

9.12 Three options have been explained in this report as a possible response to this problem. A review of the existing IFRS based accounts could be undertaken, but, given the requirement to observe international reporting standards, it may not yield the simplicity in presentation and terminology that is sought here. An alternative detailed in this report would entail adapting the existing narrative report produced by local authorities as an addendum to the statutory accounts where discretion would be afforded to each local authority regarding style, content and presentation. The third and final option relates to a new simplified statement of service information and costs as a means of enabling each local authority to communicate, in a standardised format, the key information relating to the budget and council tax setting compared to actual financial performance. If transparency and consistency of financial reporting are to be achieved this last option best meets these objectives although the experience developed in the production of narrative reports may be beneficial in its design.

9.13 A draft of a simplified statement is included as an annex to this report which incorporates the key features of simplicity and transparency. Observance of IFRS based accounts remains an important ingredient in ensuring proper accountability for financial performance, so the current statutory accounts should still be produced. This requirement is underpinned by a Code of Accounting Practice produced by CIPFA. Many local authorities have not purchased the most recent copy of the Accounting Code. Consideration should be given to this being freely available, given its importance in the construction of statutory accounts.

10. List of Annexes

1. What are auditors required to do?
2. Roles and duties of Statutory Officers
3. Functions of the Office of Local Audit and Regulation
4. Illustrative Simplified Financial Statements
    a. District Council
    b. Fire and Rescue Authority
    c. Police and Crime Commissioner
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5. Potential impact of recommendations made by other reviews of audit
6. Approach of other state auditors to performance audit
7. Terms of Reference
8. Call for Views respondents

Appendix – Glossary of Key Terms, Acronyms and Abbreviations

ACCA – Association of Chartered Certified Accountants
Professional accounting body offering the Chartered Certified Accountant qualification

Accounting Officer
Normally the Permanent Secretary of a government department who is personally responsible for the regularity and propriety of expenditure, robust evaluation of different mechanisms for delivering policy objectives, value for money, the management of risk, and accurate accounting for the use of resources

Accounts and Audit Regulations 2015
Statutory Instrument that sets the deadlines for publishing unaudited local authority accounts for inspection and for publishing audited local authority accounts; requires local authorities to have an internal audit; and details the information that must be included in local authority annual report and accounts.

Adverse Opinion
An audit opinion - a conclusion that an authority's accounts are not true and fair/proper arrangements to secure the economy, effectiveness and efficiency of service delivery are not in place.

AGN – Auditor Guidance Notes
Guidance produced by the National Audit Office to support external auditors in their work and to facilitate consistency of approach between auditors of the same types of entity. These have the same status as the NAO Audit Code of Practice

ALB – Arm's Length Body
A body which has a role in the processes of national government but is not a government department or part of one, and which accordingly operates to a greater or lesser extent at arm's length from ministers.

Annual Audit Letter – also known as Audit Completion Report or ISA260 Report
The annual audit letter summarises key findings from the auditor's yearly audit; often includes management recommendations.

AQR – Audit Quality Review team
The part of the Financial Reporting Council that monitors the quality of the audit work of statutory auditors and audit firms in the UK that audit Public Interest Entities (PIEs). Since 2018-19 AQR has been responsible for the quality assurance of larger local authority audits.

ARGA – Audit, Reporting and Governance Authority
A planned independent regulatory body to replace the Financial Reporting Council. This was recommended by Sir John Kingman in his review of the Financial Reporting Council and supported by Sir Donald Brydon in his review into the quality and effectiveness of audit

Audit Commission
A now disbanded independent public corporation that had the responsibility for appointing auditors to a range of local public bodies in England. They set the standards for auditors and had oversight their work

Audit Scotland
The body responsible for supporting the Auditor General for Scotland in providing independent assurance to the people of Scotland that public money is spent properly, efficiently and effectively.

BEIS – Department for Business, Energy & Industrial Strategy
Has policy responsibility for statutory audit, including taking forward the recommendations made by the Kingman and Brydon reviews.

Best Value
A local authority should make arrangements to secure continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness. Under the Duty of best value, therefore, authorities should consider overall value, including economic, environmental and social value, when reviewing service provision. Central government may use its best value powers to intervene in a local authority in exceptional cases where that best value duty has not been met.

Brydon Review
Independent Review into the Quality and Effectiveness of PIE Audits led by Sir Donald Brydon (published December 2019).

C&AG – Comptroller and Auditor General
An independent officer of the House of Commons who leads and is supported by the National Audit Office. Has the statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively and with economy. Responsible for preparing, maintaining, and developing the Code of Audit Practice for local authority auditors (the Audit Code).

Capital Finance and Accounting Regulations 2003 (as amended)
Regulations governing local authority capital finance and investment. Include the statutory overrides to GAAP that local authorities in England are required to apply.

Category 1 Authority
A relevant authority that either: (a) is not a smaller authority; or (b) is a smaller authority that has chosen to prepare its accounts for the purpose of a full audit in accordance with regulation 8 of the Smaller Authorities Regulations. All local authorities with income or expenditure of more than £6.5m are Category 1 authorities. The Council of the Isles of Scilly and Shire Districts with income and expenditure of less than £6.5m are also Category 1 authorities.

Category 2 Authority
A relevant authority that is a smaller authority (that is a parish council, parish meeting or internal drainage board) and has annual income and expenditure of less than £6.5m

CFO – Local Authority Chief Financial Officer / Head of Finance (also referred to as the S151 Officer)
A local authority officer, who has statutory responsibility for the proper conduct of that local authority's financial affairs.

CIAA – Chartered Institute of Internal Auditors
A representative body of internal auditors

CIPFA – Chartered Institute of Public Finance and Accountancy
A professional public finance accountancy body. Maintains four statutory codes that local authorities are required to 'have regard to'.

Clean opinion – also known as an "unqualified opinion"
An audit opinion – that the accounts are true and fair, free from material misstatement and have been properly prepared in accordance with the applicable accounting framework.

Code of Audit Practice
The "Audit Code" sets out what local auditors are required to do to fulfil their statutory responsibilities under the Local Audit and Accountability Act 2014. The Comptroller and Auditor General is responsible for the preparation, publication and maintenance of the Code of Audit Practice.

Code of Practice on Local Authority Accounting
Public sector organisations responsible for locally delivered services are required by legislation to prepare their accounts in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom (the Accounting Code)

CIPFA/LASAAC
A partnership between CIPFA (England, Northern Ireland and Wales) and the Local Authority (Scotland) Accounts Advisory Committee (LASAAC). Responsible for preparing, maintaining, developing and issuing the Accounting Code.

CMA – Competition and Markets Authority
A non-ministerial government department responsible for strengthening business competition and preventing and reducing anti-competitive activities

CMA Markets Study - Audit
The CMA carried out a study into the statutory audit market, to see if the market is working as well as it should. (published October 2018)

County councils – also known as Shire Counties
Upper tier authority responsible for services across the whole of a county such as: education; transport; planning; social care.

CQC – Care Quality Commission
An executive non-departmental public body responsible for monitoring, inspecting and regulating health and social care services.

DHSC – Department for Health and Social Care

District Audit Service
Set up in 1844, and originally part of HMT, was the Audit Commission's in-house audit practice until all local authority audits were outsourced for the 2012-13 financial year. Most staff working in the DAS at that time transferred to the private sector accountancy firms who took on responsibility for local authority audits.

District Council – also known as Shire District
Lower tier authority, responsible for services over a smaller area than county councils such as: rubbish collection; recycling; Council Tax collections; housing; planning applications

EFA - Expenditure and Funding Analysis
Summarises the annual expenditure used and funded by the Council together with the adjustments between the funding and accounting basis to reconcile with the CIES

Except for opinion
An audit opinion - a conclusion that in all material respects the accounts are true and fair/proper arrangements are in place except for the matters detailed in the audit certificate and report OR a conclusion that the supporting evidence provided by the authority is so deficient that the auditor is unable to conclude whether one or more material items in the accounts are true and fair/a material element of proper arrangements are in place

Financial Reporting
Financial reporting uses financial statements to disclose financial data that indicates the financial health of an entity over during a specific period of time. These reports provide information to people who wish to understand the performance of an entity

FRA – Fire and Rescue Authority
A supervisory body which ensures that a local fire service performs efficiently and in the best interest of the public and community it serves. FRAs can be part of a another type of local authority or can be stand-alone entities.

FRAB – Financial Reporting Advisory Board
The role of the board is to ensure that government financial reporting meets the best possible standards of financial reporting by following Generally Accepted Accounting Practice as far as possible.

FRC - Financial Reporting Council
An independent regulatory body which regulates auditors, accountants and actuaries and sets the UK's Corporate Governance and Stewardship Codes. Currently transforming into a new body the Audit, Reporting and Governance Authority.

FReM - UK Central Government Financial Reporting Manual
The technical accounting guide to the preparation of financial statements, prepared after consultation with the Financial Reporting Advisory Board. It complements guidance on the handling of public funds published separately by the relevant authorities in England and Wales, Scotland and Northern Ireland

General Fund
The main revenue account that local authorities are required to maintain. The majority of income goes into the general fund account and most service expenditure is funded from it.

General Power of Competence
Introduced by the Localism Act 2011 and took effect in February 2012. In simple terms, it gives councils the ***power*** *to do anything an individual can do provided it is not prohibited by other legislation. Most wholly-owned local authority companies are set up under the General Power of Competence.*

Generally Accepted Accounting Practice/Principles (GAAP)
A collection of commonly-followed accounting rules and standards for financial reporting. The acronym is pronounced "gap." GAAP specifications include definitions of concepts and principles, as well as industry-specific rules.

Going Concern Test
An element of the audit report certifying that readers of a set of accounts are entitled to assume a business will continue in the future, unless there is evidence to the contrary. Going concern reporting is very specifically about ensuring that the correct accounting basis is being used, not about confirming whether an authority is running out of resources.

Greater London Authority (GLA)
A type of local authority. The GLA regional authority, with powers over transport, policing, economic development, and fire and emergency planning in Greater London. The GLA is unique in the British devolved and local government system, in terms of structure elections and selection of powers.

Head of Paid Service
The Head of Paid Service has statutory responsibility for the management and coordination of the employees appointed by the Council. Although the roles are separate, frequently the Chief Executive or Managing Director of a local authority.

HMICFRS - Her Majesty's Inspectorate of Constabulary and Fire & Rescue Services
Inspectorate responsible for independently assessing the effectiveness and efficiency of police forces and fire & rescue services.

HMT – Her Majesty's Treasury

HOFMCP - Home Office Financial Management Code of Practice
The financial management code of practice provides clarity around the financial governance arrangements within policing

Housing Revenue Account
Legislation prohibits social housing expenditure from being subsidised by general fund expenditure and vice versa. Therefore, local authorities with social housing stock are required to maintain a separate "housing revenue account", which must be self-financing.

ICAEW - Institute of Chartered Accountants of England and Wales
A professional membership organisation that promotes, develops and supports chartered accountants and students in the UK, Wales and globally. Responsible for maintaining the register of firms and KAPs qualified to sign off audits of local authority accounts.

ICAS - Institute of Chartered Accountants of Scotland
A professional membership organisation that promotes, develops and supports chartered accountants and students in Scotland.

IFRS – International Financial Reporting Standard (set by the International Accounting Standards Board)
A public interest organisation which has developed and maintains a single set of globally accepted accounting standards.

Internal Drainage Board
A type of local authority which is established in areas of special drainage need in England and Wales with permissive powers to undertake work to secure clean water drainage and water level management within drainage districts. The area of an IDB is not determined by county or metropolitan council boundaries, but by water catchment areas within a given region.

ISA - International Standards on Auditing
Standards for audits of financial statements, which include objectives for the auditor, together with requirements and related application and other explanatory material. ISAs(UK) are issued by the FRC.

KAP – Key Audit Partner
A senior member of staff within an audit firm who is registered to sign off a set of local authority accounts. Does not need to be a partner in the firm.

Kingman Review
Independent Review of the Financial Reporting Council led by Sir John Kingman (published December 2018). Included commentary and recommendations for local audit.

KPI – Key Performance Indicator
A performance measurement which helps evaluate the success of an organisation or of a particular activity in which it engages.

LGA – Local Government Association
The national membership body for local authorities.

LGSCO – Local Government and Social Care Ombudsman
A service that investigates complaints from the public about councils, registered adult social care providers and other select bodies providing public services in England

Limitation in Scope
An audit opinion - a conclusion that the supporting evidence provided by the authority is so deficient that the auditor is unable to conclude whether the accounts are true and fair and/or proper arrangements are in place to deliver economy, efficiency and effective services.

Local Audit and Accountability Act 2014
Abolished the Audit Commission and established the current arrangements for the audit and accountability of the local public audit system

Local Audit Delivery Board
Consultative board chaired by MHCLG, which compromises of representatives of relevant departments and framework bodies to facilitate sharing of information about the operation of the local authority accounting framework. Meetings are held in private and it has no formal powers or remit.

Local Government Act 2000
An Act to make provision with respect to the functions and procedures of local authorities

London Borough
A single tier of local authority that provides all the services that a county and district/borough/city council would usually provide. Some services, like fire, police and public transport, are provided through the Greater London Authority.

Mayoral Combined Authority
A type of local authority created in areas where they are considered likely to improve transport, economic development and regeneration. MCAs are led by metro mayors who make decisions about policy and spending in conjunction with council leaders from each constituent council. Both the metro mayor and each of the council leaders have a single vote and must approve or oppose decisions.

Metropolitan borough – also known as Metropolitan District
A single tier of local authority that provides all the services that a county and district/borough/city council would usually provide. Some services, like fire, police and public transport, are provided through 'joint authorities

MHCLG – Ministry of Housing, Communities and Local Government
The government department with policy responsibility for the local audit framework.

MIRS - Movement in Reserves Statement
Shows how the movement in reserves in the Balance Sheet is reconciled to the CIES deficit and what adjustments are required to be charged to the general fund balance for Council Tax setting purposes

Monitoring Officer
A local government officer with three main roles: to report on matters he or she believes are, or are likely to be, illegal or amount to maladministration; to be responsible for matters relating to the conduct of councillors and officers; and. to be responsible for the operation of the council's constitution.

NAO – National Audit Office
The UK's independent public spending watchdog. The NAO support Parliament in holding government to account and they work to improve public services through their audits. They are led by the Comptroller and Auditor General

NHSI(E) – NHS England and NHS Improvement
The umbrella body for the NHS in England. From 1 April 2019, NHS England and NHS Improvement have worked together as a new single organisation to better support the NHS to deliver improved care for patients.

Ofsted - Office for Standards in Education
Office for Standards in Education, Children's Services and Skills. Inspect services providing education and skills for learners of all ages. Also inspects and regulate services that care for children and young people including those delivered by local authorities.

Parish Council – can also be known as community councils
A civil local authority found in England and is the lowest tier of local government. They are elected corporate bodies, have variable tax raising powers. Responsibilities of parish council's vary considerably but can include allotments, bus shelters, burials and maintenance of common land and rights of way.

Parish Meeting
A meeting to which all the electors in a civil parish are entitled to attend. In some cases, where a parish or group of parishes has fewer than 200 electors, the parish meeting can take on the role of a parish council, with statutory powers, and electing a chairman and clerk to act on the meeting's behalf.

PCC – Police and Crime Commissioner
An elected official in England and Wales charged with securing efficient and effective policing of a police area. Commissioners replaced the now-abolished police authorities.

PIE – Public Interest Entity
A listed company or an entity with listed debt. Under EU Law, entities are designated by Member States and are usually defined as having undertakings that are of significant public relevance because of the nature of their business, their size or the number of their employees.

PIR – Public Interest Report
When an Auditor considers there to be a matter that is sufficiently important enough to be publicly brought to the notice of the council or the public they can make a report in the public interest.

PSAA - Public Sector Audit Appointments Ltd
Public Sector Audit Appointments is a company limited by guarantee wholly owned by the Local Government Association. PSAA are specified as an appointing person for local authority under provisions of the Local Audit and Accountability Act 2014. The functions of PSAA are specified in statute.

Qualified Audit Opinion
When an external auditor concludes that financial records have not been maintained in accordance with the Generally Accepted Accounting Principles. There are three types of qualified opinion; an except for; adverse; and limitation in scope opinion

SAAA - Smaller Authorities' Audit Appointments Ltd
The sector-led limited company appointed as the specified person to procure and appoint external auditors to smaller authorities and to manage the ongoing smaller authority audit contracts.

SERCoP - Service Reporting Code of Practice
A statutory code that sets out the proper practices with regard to consistent financial reporting for services; all local authorities in the UK are expected to adopt its mandatory requirements and recommendations and use them when reporting statistical data to central government.

Smaller Authorities - parish, community and town councils and internal drainage boards
These operate at a level below district and borough councils and in some cases, unitary authorities. They sometimes deliver additional services on behalf of the district council.

SOLACE – Society of Local Authority Chief Executives
Members' network for local government and public sector professionals throughout the UK

TUPE - Transfer of Undertakings (Protection of Employment)
Regulations to protect employees if the business in which they are employed changes hands. The two types of transfer protected by TUPE regulations are business transfer and service provision changes

Unitary Authorities
A single tier of local authority that provides all the services that a county and district/borough/city council would usually provide.

Unqualified Audit Opinion
When an external auditor concludes that the financial statements of an entity present fairly its affairs in all material aspects

VfM Conclusion – Value for Money Conclusion
A requirement that external auditors undertake sufficient work to be able to satisfy themselves as to whether the audited body has put arrangements in place that support the achievement of value for money. In carrying out this work, the auditor is not required to satisfy themselves that the audited body has achieved value for money during the reporting period

Welsh Audit Office
The Wales Audit Office provides staff and other resources for the Auditor General's work, and monitors and advises the Auditor General for Wales.

Agenda item 6
AGS/78/20

Report title: Internal Audit and Counter Fraud Progress Report	
Report to: Audit, Governance and Standards Committee	
Report author: Paula Clowes – Head of Assurance	
Date: 28 September 2020	**For:** Discussion
Enquiries to: Paula Clowes – Head of Assurance paula.clowes@essex.gov.uk	
County Divisions affected: All Essex	

1. Purpose of Report

1.1 This report provides the Audit, Governance and Standards Committee with the current position regarding Internal Audit and Counter Fraud activity in relation to the 2020/21 Internal Audit Plan (approved by the Audit, Governance and Standards Committee in July 2020). It reflects the situation as at 31 August 2020.

2. Recommendation

2.1 That the report be noted**.**

3. Key Issues

3.1 The following matters are of particular note:

- No reports with 'no assurance' have been issued during the period
- One audit has been completed that received limited assurance – Accounts Receivable. This report has been issued to members in full and the service will attend the committee to provide explanation and an update.
- As at 8 September 2020 there were four Critical and fifteen Major recommendations open, of which six Major recommendations have moved beyond their latest agreed due date.
- Fraud Referrals are significantly lower than the same period last year, due to the Covid-19 pandemic.
- Using the NFI data hub £185,054.23 has been recovered related to overpayments to Residential Care Homes.

4. Details of Internal Audit and Counter Fraud Activity

4.1 Final Internal Audit Reports Issued

4.1.1 When Internal Audit issues a report it gives an overall assurance rating which is either 'Good' 'Adequate' 'Limited' or 'No' Assurance. The final reports issued since the March 2020 Audit, Governance and Standards Committee are listed below.

Executive Summaries for those reports receiving 'Limited Assurance' are set out in Appendix 1.

Full internal audit reports are available to Members on request.

No Assurance	• None
Limited	• Accounts Receivable • IT Major Incident Management – follow up review
Satisfactory	• Control Account Reconciliations • Cyber Security • Journals and Virements • Supplier Resilience • Risk Management – follow up review • Deprivation of Assets and Deferred Payments • Schools Income • South East Local Enterprise Partnership • Coroners • Office 365 • Payroll • The Corporate System (TCS) – Change Management • Country Parks Income
Good	• Workforce Strategy Planning • Approval Management Engine ("AME") • Essex Pension Fund - Administration • Essex Pension Fund – Funding and Investments • Members Locality Funds – phase 1
Other	• Troubled Families Grant • EU Interreg Grant – SPONGE (preventing flooding) • EU Interreg Grant - PROFIT (promoting tourism to the Essex coast) • EU Interreg Grant - EMPOWER • SELEP Growth Hub Grant • Covid-19 Bus Services Support Grant • DfT Blue Badge New Criteria Implementation (No 31/2936) • M11 Junction 7A Business Case Costings • Ongoing support to the Oracle Fusion Programme

4.2 Implementation of Internal Audit Recommendations

4.2.1 Whenever any recommendations are made in an audit report, Managers are asked to agree what activity they will undertake to address the recommendations and to agree timescales for implementation.

4.2.2 Progress on the implementation of recommendations is monitored by the Internal Audit service.

4.2.3 Critical or Major recommendations which have not been implemented within the agreed timescale are reported to the Audit, Governance and Standards Committee. Outstanding recommendations are provided to Functional Leadership Teams (FLT) quarterly.

4.2.4 As at 8 September 2020 there were 4 Critical and 15 Major recommendations open, of which 6 Major recommendations have moved beyond their latest agreed due date. See Appendix 3 for further detail.

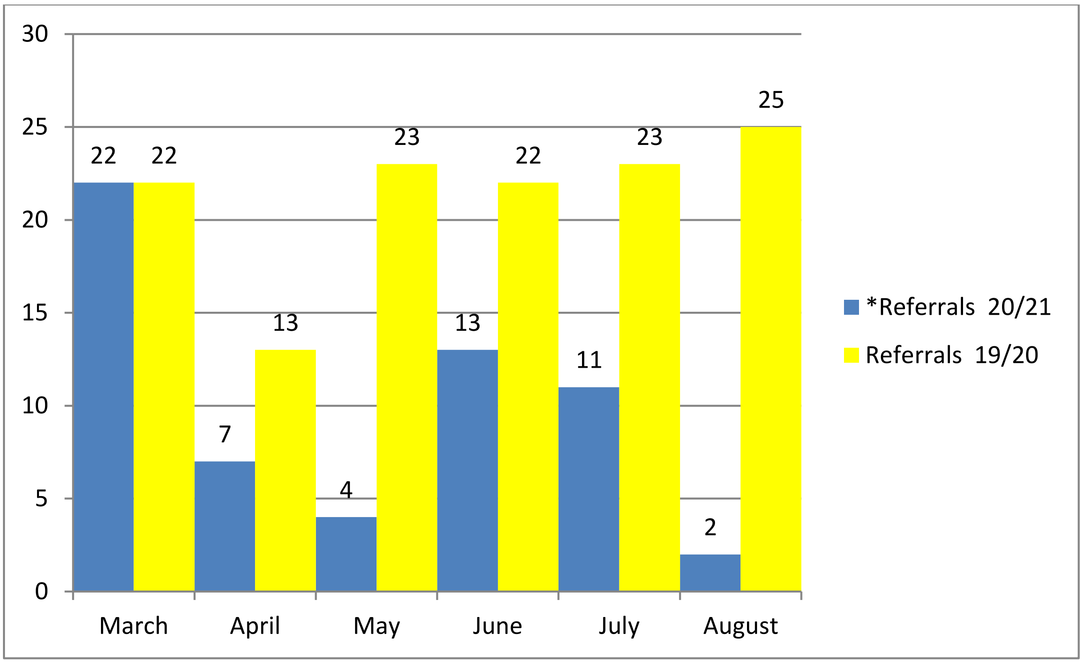
4.2.5 The current assessment rationale for grading the priority of recommendations made and the level of assurance (audit opinion) for each individual audit review is attached at Appendix 2.

4.3 Counter Fraud Activity

4.3.1 The Counter Fraud Team has a remit to prevent, detect and investigate fraud. This includes proactive work utilising data matching and analytical work. In some cases we will pursue sanction through the civil or criminal courts and where possible seek to recover lost/stolen monies.

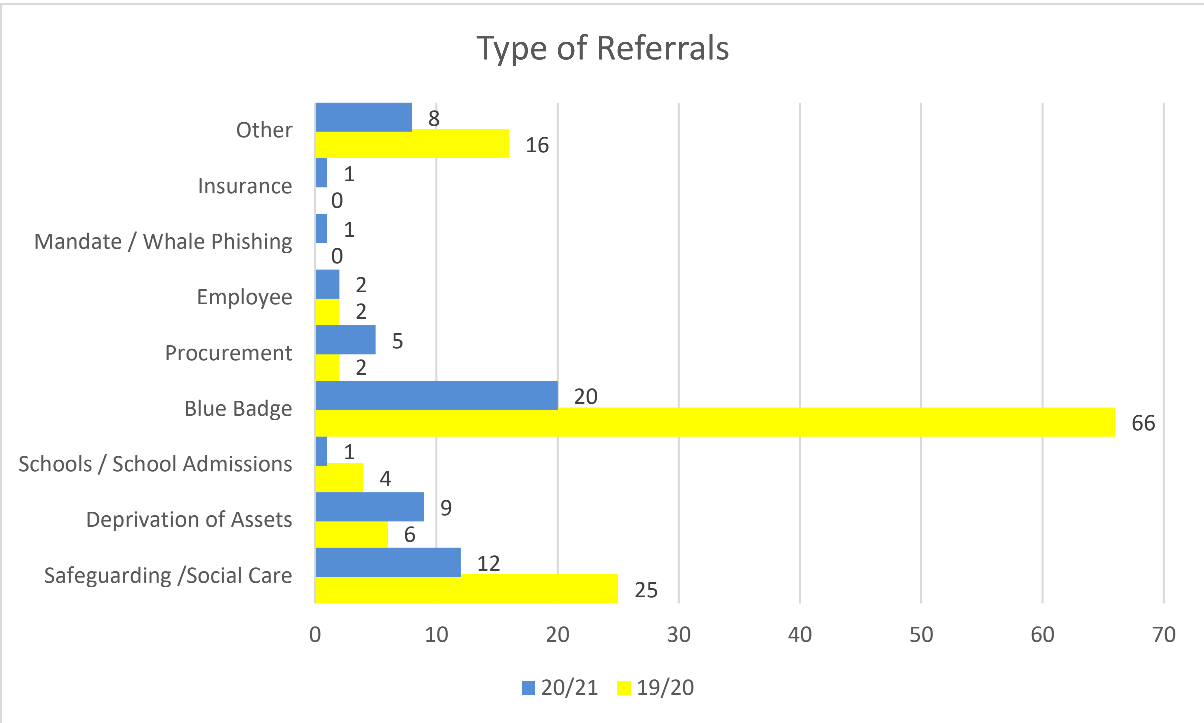
Fraud Referrals

4.3.2 During the 6 month period 1 March 2020 to 31 August 2020, 59 referrals were received (including blue badge referrals). The table below shows how this compares to the same period last year and demonstrates that the number of referrals received this year is lower than the same reporting period last year (128 referrals were received during the same period last year). This is largely due to the impact of the Covid-19 pandemic, the fact that blue badge enforcement was suspended for the first 3 months of the reporting period and referrals in relation to social care were reduced as Adult Social Care re-prioritised their resources during the pandemic. Face to face monitoring reviews have been suspended; although a new team, the Direct Payment Monitoring Team, has been established who will review Direct Payment accounts. It is envisaged that referrals in relation to adult social care will increase once this team is fully operational.



Types of Referrals

4.3.3 The bar chart below demonstrates the type of referrals received, with a comparison to the referrals received last year.



Internal Data Matching

4.3.4 The Counter Fraud team now includes a Data and Intelligence Specialist. Data matching / analytical work has been completed during the 6 month period in the following areas:

- payroll and expenses to identify potential erroneous, duplicate or fraudulent or unusually high payments;
- adult social care, predominantly to cleanse data between the social care case management system and the payment system. The latest review resulted in some 79 records being highlighted for update.
- Adult social care – an analysis of care packages to identify where domiciliary and residential care packages overlap and may not have been fully closed down on the system – testing is currently underway.

Essex Council Tax Data Matching Initiative

4.3.5 The Council is supporting an Essex-wide data matching project that involves all councils providing data to ensure that income received from council tax is maximised. ECC provides data sets to support the data matching which is now undertaken on a monthly basis and the Counter Fraud Team provides support to districts in dealing with the output. Total cumulative savings recorded as at August 2020 (from July 2017) are **£1,943,529**.

National Fraud Initiative Data Matching Exercise and NFI Fraud Hub

4.3.6 The National Fraud Initiative is a biennial exercise overseen by the Cabinet Office. This is a mandatory exercise which all public sector bodies participate in, submitting prescribed data sets to the Cabinet Office to facilitate a national data matching exercise to be completed. The Counter Fraud Team are due to submit datasets to the Cabinet Office in October 2020. Matches are scheduled to be returned for investigation during February and March 2021.

4.3.7 In addition to the mandatory data matching, the Counter Fraud Team subscribed to the NFI Fraud Hub in March 2020. Discretionary data matching is permitted on an ad hoc basis, using the same prescribed data sets as submitted as part of the national exercise. Data sets relating to Adult Social Care and Pensions have been uploaded and matched to the mortality listing. These matches have been investigated and where ECC had not been notified of the respective death, records have been updated and further payments have been prevented. This reduces the reputational damage to ECC by making payments after the date of death and also trying to pursue monies paid in error. The following savings to ECC during the last 5 month period:

Data Set	Number of matches	Financial Savings
Residential Care Home to Deceased	47	£185,054.23 - all recovered
Personal Budgets to Deceased	4	£19,404.24 – (recovery not yet calculated)
Pensions to Deceased	73	£57,040.88 (£35,107.38)

Note – the Cabinet Office are currently investigation the legislation regarding patient data. We are unable to submit adult social care datasets for matching purposes pending the results of this review.

Cifas Pilot

4.3.8 ECC joined the Cifas data matching pilot in early 2019. To date, data sets from ECC have been submitted for matching in relation to adult social care, pensions and insurance claims. Although several matches to mortality records were identified, there has been limited use in the service. We are currently in negotiation with Cifas regarding the future of the scheme.

Fraud Awareness Training

4.3.9 At present, 85% of all ECC staff have completed the e-learning modules relating to:

- Anti-fraud and corruption
- Anti-bribery and money laundering.

4.3.10 In addition, the Counter Fraud Team have completed bespoke fraud awareness sessions for the following:

- Direct Payment Monitoring Team
- Social Work Team – Local Delivery South

4.3.11 During the Covid-19 pandemic, the Counter Fraud Team have worked with several service areas to provide advice and guidance as new processes and procedures were put in place to deal with changing circumstances and the need to distribute additional funding to providers in a prompt and efficient way, whilst still maintaining a robust control framework with minimal exposure to fraud and error. The Counter Fraud Team have supported the following functions during this period:

- ELS Deputyship Service – procedures to send cash to clients
- Operation Shield – procedures to distribute supplies and support to Essex residents
- Procurement – distribution of Adult Social Care (ASC) funding

Outcomes

4.3.12 During the period 1 March to 31 August 2020, the following outcomes and sanctions have been achieved:

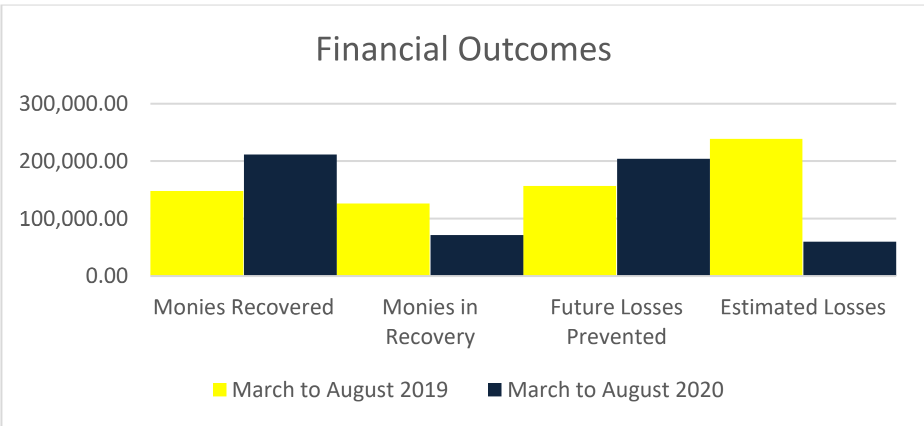
Outcome Type	March to August 2019	March to August 2020
Prosecutions	2	0
Dismissals	1	0
No fraud established	14	14
Phishing / Referred to third party	0	1
Blue Badges – **Misuse letter issued**	11	0
Blue Badges - Seized	15	1
ASC - Financial recovery	10	9
ASC - PB terminated	2	6
*Other	14	10

**Other outcomes include:*

- *Referrals to the Deputyship Team where Power of Attorney not in place,*
- *Revision of financial assessments where non-disclosure of assets or deprivation of assets identified,*
- *Additional guidance & support provided where potential misuse of personal budgets,*
- *Reduction of Personal Budgets.*

Financial Recoveries

4.3.13 In addition to the savings identified during the data matching exercise, this period, the following financial outcomes have been achieved:



The future losses prevented mainly related to personal budgets (adult social care) which have been reduced or terminated during the year due to fraud or misrepresentation of circumstances, such as care needs have been overstated, misuse of funds, deprivation of assets. Future losses are estimated as the annual value of a personal budget (i.e. the cost to ECC if the personal budget had continued to be paid until the next social care review).

4.3.14 In addition, notional savings of £575 have been identified as 1 expired blue badge has been taken out of circulation, each badge being attributed a value of £575 (figure determined by the Cabinet Office).

Annual Assessment against the Fighting Fraud & Corruption Locally (FFCL) Checklist

4.3.15 The Counter Fraud Team have completed an annual assessment of the Councils position in relation to the robustness and effectiveness of their fraud arrangements and culture, using the revised FFCL Checklist. The checklist is attached at Appendix 4 and demonstrates that ECC is almost 95% compliant.

5. Financial Implications

5.1 There are no financial implications as the Internal Audit and Counter Fraud activity 2020/21 will be met within existing resources.

6. Legal Implications

6.1 Internal Audit is a key way in which councillors can be assured that the Council is using its resources effectively and that the Council is discharging its fiduciary duties concerning taxpayers' money. It helps services to design systems which have appropriate controls and also helps identify and respond to breaches if they occur. This report seeks to update the Audit, Governance and Standards Committee on the activities of the Council's Internal Audit and Counter Fraud service for the purposes of providing further assurance.

7. Equality and Diversity Implications

7.1 Section 149 of the Equality Act 2010 creates the public sector equality duty which requires that when ECC makes decisions it must have regard to the need to:

(a) Eliminate unlawful discrimination, harassment and victimisation and other behaviour prohibited by the Act
(b) Advance equality of opportunity between people who share a protected characteristic and those who do not
(c) Foster good relations between people who share a protected characteristic and those who do not including tackling prejudice and promoting understanding.

7.2 The protected characteristics are age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation. Equality and diversity matters have been considered in the production of the progress report.

8. List of Appendices

Appendix 1 Executive Summaries for Limited Assurance Reports
Appendix 2 Current assessment rationale for grading the priority of recommendations in Internal Audit reports.
Appendix 3 Critical and Major Recommendations which are overdue for implementation as at 31 August 2020
Appendix 4 Completed Assessment against the Fighting Fraud and Corruption Locally Checklist

9. List of Background Papers

Internal Audit reports

Appendix 1

Accounts Receivable 2019/20
Final Internal Audit Report

Audit Plan Ref: CC1

Audit Opinion:

Limited Assurance

Date Issued: 8 July 2020
Function: Finance and Technology
Audit Sponsor: John Delgado – Head of Finance, Transactional Services

Distribution List: Nicole Wood – Executive Director, Finance and Technology; **Stephanie Mitchener** – Director, Finance; **John Delgado**; **Bola Odunsi** – Service Manager (Income and Assessments); **Gavin Jones** – Chief Executive; **Cllr. Finch** – Leader of the Council; **Cllr. Whitbread** – Cabinet Member for Corporate, Customer, Culture and Communities; **Barry Pryke** – External Audit; **Neil Woodcock** – Senior Finance Officer; **Jo Cook** – Senior Finance Officer, **Vicky Hotson** – Service Manager; **Mark Hibbitt** – Financial Analyst

Essex County Council

Assurance Opinion	No	Limited	Satisfactory	Good
		X		

Number of Issues	Critical	Major	Moderate	Low
		2 But one - risk tolerated	5	

Audit Objective

The objective of the audit was to assess whether an adequate control framework is in place to ensure debt collection activity is:

- correct
- complete
- authorised
- valid
- timely
- efficient

Scope of the Review and Limitations

The scope of the review covers the processes only to chase both Adult Social Care (ASC) and sundry debts once they are past the due date.

This review covered the period 2019/20 to January 2020 and so was conducted prior to Covid - 19.

The processes around deprivation of assets and deferred payments has been reviewed separately (ECC 1920 CC6) and is not in the scope of this audit.

Key Messages

There has been close oversight of debt management and a sustained focus on improving collection processes and outcomes, supported by senior management and Members.

It has been acknowledged by management that throughout 2019/20 the income recovery processes have needed further improvements as in particular the current IT systems do not currently have some key functionality to provide consistent, timely and easy to produce assurance over the end-to-end debt collection process. Work was planned with Fujitsu to improve this, but given cost and resources to do so and the time until the new corporate systems are implemented, this risk will be tolerated until then.

There is limited assurance that the ongoing collection activity needed when debts are not received by due dates is consistently happening as required by the Income Recovery and Debt Collection Strategy and such actions are being taken in the most effective and timely manner. During the year, additional and improved manual processes and reporting have been introduced to direct and oversee the performance of debt collectors but not all recommendations from last year have yet been fully implemented.

Management information in the monthly income performance packs shows that targets for collection of Adult Social Care debt within 60 and 90 days are generally not being met (there is a good reported performance for sundry debts). But there has been progress towards reducing the overall debtor balance, particularly Adult Social Care debts during the year.

Given the Council’s wider financial pressures and need to find ongoing savings, and the value of debts, the importance and benefit of effective debt recovery action is increased.

Direction of Travel

The opinion is the same as last year.

There have been some process improvements introduced, and progress is being made to address the fundamental, system-based process limitations

Final Internal Audit report
Major Incident Management follow up
Audit plan ref: ECC 1920 CC10

Follow up outcome:
Limited progress has been made to implement the recommendations

Follow up results:
- ***Three recommendations have been implemented***
- ***Three major recommendations are not yet fully implemented***

Date Issued: 11 May 2020

Function: Finance and Technology

Audit Sponsor: Melanie Hogger, Director, Technology Services

Distribution List:

Tracey Kelsbie, Chief Operations Officer, Technology Services; **Nicole Wood**, Executive Director, Finance and Technology (Section 151 Officer); **Gavin Jones**, Chief Executive; **Cllr. Finch**, Leader of the Council; **Cllr. Barker**, Cabinet Member for Corporate, Customer, Culture and Communities; **Barry Pryke** (external audit)

Essex County Council

1. Executive Summary

Follow up outcome	Critical	Major	Moderate	Low
Number of recommendations followed up	0	4	1	1
Number of recommendations implemented	-	1	1	1
Number of recommendations with further actions required	-	3	-	-

Review objective

The Major Incident Management report issued in March 2019 gave a limited assurance opinion. This review's objective is to assess whether the six recommendations made have now been implemented effectively and are now embedded as business as usual.

Scope of the review

This review is limited in scope to following up the six recommendations made in the March 2019 report.

As a follow up, **this work did not assess the current design and or operation of all controls previously identified or present.** Therefore, this follow up should not be taken as a wider assurance over the overall control environment regarding major incident management.

Key Messages

Three of the six recommendations are judged to be now implemented and therefore the identified risks associated with those recommendations now satisfactorily managed. Two major priority recommendations are partially implemented, and the associated risks remain at major. One major priority recommendation is substantially implemented, and the associated risk is now low.

When fieldwork was completed at the beginning of March 2020, it was concluded more work was needed to fully implement the major priority recommendation to ensure the major incident management process aligns with, and meets the requirements of, an updated and corporately agreed assessment of the most strategically critical technology and applications. This recommendation is therefore dependent on the wider work to refresh the council's business continuity arrangements which is in progress.

Since the Covid-19 outbreak there has been a major incident as the network has again struggled to cope with mass working from home which has impacted on the performance of a large number of critical applications, including social care systems.

There has been an ongoing and significant major incident management response, and this has accelerated the development of temporary capability to manage this type of incident to enable priority users to access critical technology and restricting non-priority staff to applications which are accessed through the internet rather than ECC network. This is very recent, and the ongoing effectiveness of the new arrangements for all applications and all staff has not been fully assessed.

More work is also needed to implement the major priority recommendation to improve the post-incident reporting on major incidents to provide clearer understanding and contextualise major incidents (individually and collectively) to reduce the risk or severity of incidents in future.

Appendix 2

Current assessment rationale for grading the priority of recommendations in Internal Audit reports

Risk rating	Assessment rationale
Critical	Critical and urgent in that failure to address the risk could lead to one or more of the following occurring: ▪ Significant financial loss (through fraud, error, poor value for money) ▪ Serious safeguarding breach ▪ Life threatening or multiple serious injuries ▪ Catastrophic loss of service ▪ Failure of major projects ▪ Critical Information loss leading to Information Commissioner's Office (ICO) referral ▪ Reputational damage – Intense political and media scrutiny i.e. front-page headlines, television coverage. ▪ Possible criminal, or high profile, civil action against the Council, Members or officers. ▪ Intervention by external agencies ***Remedial action must be taken immediately***
Major	Major in that failure to address the issue or progress the work would lead to one or more of the following occurring: ▪ High financial loss (through fraud, error, poor value for money) ▪ Safeguarding breach ▪ Serious injuries or stressful experience requiring medical treatment, many work days lost. ▪ Significant disruption to service (Key outcomes missed, some services compromised. Management action required to overcome medium term difficulties) ▪ Major Information loss leading to internal investigation ▪ Reputational damage – Unfavourable external media coverage. Noticeable impact on public opinion. ▪ Scrutiny required by external agencies ***Remedial action must be taken urgently***
Moderate	Moderate in that failure to address the issue or progress the work would lead to one or more of the following occurring: ▪ Medium financial loss (through fraud, error or poor value for money) ▪ Significant short-term disruption of non-core activities ▪ Scrutiny required by internal committees. ▪ Injuries or stress level requiring some medical treatment, potentially some work days lost ▪ Reputational damage – Probable limited unfavourable media coverage. ***Prompt specific action should be taken***
Low	Low in that failure to address the issue or progress the work would lead to one or more of the following occurring: ▪ Low financial loss (through error or poor value for money) ▪ Minor errors in systems/operations or processes requiring action or minor delay without impact on overall service delivery schedule. Handled within normal day to day routines. ▪ Reputational damage – Internal review, unlikely to have a wider impact. ***Remedial action is required***

Assurance Level	Description
Good	***Good assurance –*** there is a sound system of internal control designed to achieve the objectives of the system/process and manage the risks to achieving those objectives. Recommendations will normally only be of Low risk rating. Any Moderate recommendations would need to mitigated by significant strengths elsewhere.
Adequate/ Satisfactory	***Adequate/satisfactory assurance –*** whilst there is basically a sound system of control, there are some areas of weakness, which may put the system/process objectives at risk. There are Moderate recommendations indicating weaknesses but these do not undermine the system's overall integrity. Any Critical recommendation will prevent this assessment, and any Major recommendations relating to part of the system would need to be mitigated by significant strengths elsewhere.
Limited	***Limited assurance –*** there are significant weaknesses in key areas in the systems of control, which put the system/process objectives at risk. There are Major recommendations or a number of moderate recommendations indicating significant failings. Any Critical recommendations relating to part of the system would need to be mitigated by significant strengths elsewhere.
No	***No assurance –*** internal controls are generally weak leaving the system/process open to significant error or abuse or reputational damage. There are Critical recommendations indicating major failings

Appendix 3

Overdue Critical and Major Internal Audit Recommendations as at 8 September 2020

Audit Review Title	Function	Recommendation	Latest Target Date	Last Status Update	Owner	Rating
Essex Child and Family Well-being Service (1819 CF4)	Children, Families and Education	Safeguarding: assurance reporting and escalation processes	31/03/20	No update provided since January 2020.	Director, Strategic Commissioning & Policy	Major Risk
Building Security (1920 PPH5)	Place and Public Health	Partner Organisation Leaver Process	31/08/19	**Update as at 6 January 2020:** Suggestions put forward from the service to improve the control weaknesses identified, these have recently been approved by Internal Audit and are in the process of being implemented.	Contract Manager, Corporate	Major Risk
Facilities Management (1819 IE5)	Place and Public Health	Ongoing assurance reporting over Mitie's procurement processes	30/11/19	**Update as at 17 February 2020:** Procurement are currently in process of auditing Mitie's PMO procurement process. Reverting back to the previous areas of concern.	Contract Manager, Corporate	Major Risk
Absence Management (1718 COR5)	Organisation Development and People	Completeness of Return to Work Action	09/03/20	**Update as at 29 July 2020:** Reporting completed on a six monthly basis by exception. The need for this to be automated has been fed into the Corporate Systems Programme which has now fully started, and we will know more as this progresses. Oracle have confirmed that these requirements can be delivered, should ECC select them.	Head of People, Insight and Technology	Major Risk
Absence Management (1718 COR5)	Organisation Development and People	Notifications to Line Managers/ Management Information on Compliance	09/03/20	**Update as at 29 July 2020:** Absence management at Unit level upwards has continued to be part of the Management Information Tool sent to Managers. Reporting of individual employees reaching absence triggers completed on a six monthly basis by exception. Line Managers receive email notifications once their employee hits specific absence triggers. The Corporate Systems Programme has now fully started, and the need for this area to be automated has been fed into the ODP requirements. Oracle have confirmed that these requirements can be delivered, should ECC select them.	Head of People, Insight and Technology	Major Risk
Accounts Receivable	Finance and Technology	Management Information does not help compliance with the Collection	31 July 2020	None provided but audit only finalised in July 2020.	Service Manager, Income	Major

Audit Review Title	Function	Recommendation	Latest Target Date	Last Status Update	Owner	Rating
(1920 CC1 AR)		Strategy and prioritise activity				

Appendix 4

Fighting Fraud & Corruption Locally Checklist

ECC fully compliant with this statement   ECC partially compliant with this statement

	Statement	ECC Position - September 2020 review
	The local authority has made a proper assessment of its fraud and corruption risks, has an action plan to deal with them and regularly reports to its senior Board and its members.	Fraud Risks reviewed annually and Fraud Risk Register updated accordingly. High risk areas are identified and incorporated in annual Internal Audit & Counter Fraud Plan which is presented to the Audit, Governance and Standards (AGS) Committee for approval.
	The local authority has undertaken a fraud risk assessment against the risks and has also undertaken horizon scanning of future potential fraud and corruption risks. This assessment includes the understanding of the harm that fraud may do in the community.	An annual fraud risk assessment is completed, which incorporates emerging risk areas and the potential exposure to these risk areas.
	There is an annual report to the audit committee, or equivalent detailed assessment, to compare against FFCL 2020 and this checklist.	Annual assessment completed, using either the CiPFA\FFCL checklist. Any areas to address are identified and included in the progress reports presented to the AGS committee
	The relevant portfolio holder has been briefed on the fraud risks and mitigation	Head of Assurance provides monthly reports to Finance Portfolio holder.
	The audit committee supports counter fraud work and challenges the level of activity to ensure it is appropriate in terms of fraud risk and resources	Annual report and quarterly progress reports presented to AGS Committee. This includes details of resources.
	There is a counter fraud and corruption strategy applying to all aspects of the local authority's business which has been	Updated Counter Fraud Strategy in place, which is reviewed biennially and presented to the AGS Committee for approval.

	Statement	ECC Position - September 2020 review
	communicated throughout the local authority and acknowledged by those charged with governance.	
	The local authority has arrangements in place that are designed to promote and ensure probity and propriety in the conduct of its business.	The authority has a range of policies and procedures in place underpinned by mandatory e-learning modules.
	The risks of fraud and corruption are specifically considered in the local authority's overall risk management process.	*Partial Compliance* - Fraud risks are considered by each service and incorporated in the **fraud risk register** as appropriate. Risk workshops are held with service areas to review fraud risks and mitigation.
	Counter fraud staff are consulted to fraud-proof new policies, strategies and initiatives across departments and this is reported upon to committee.	*Partial Compliance* - Internal Audit and Counter Fraud are consulted on **some** new projects to advise on fraud/control risks and mitigation. Support provided is included in regular reports to AGS committee.
	Successful cases of proven fraud/corruption are routinely publicised to raise awareness.	*Partial Compliance* - Consideration is given to reporting\publicising all prosecuted case of fraud. Outcomes of all investigations are reported to AGS committee which is in the public domain.
	The local authority has put in place arrangements to prevent and detect fraud and corruption and a mechanism for ensuring that this is effective and is reported to committee.	These arrangements are considered as part of the fraud risk assessment and internal control framework which is subject to regular review and reported to the AGS committee.
	The local authority has put in place arrangements for monitoring compliance with standards of conduct across the local authority covering: – codes of conduct including behaviour for counter fraud, anti-bribery and corruption – register of interests – register of gifts and hospitality	ECC has the appropriate policies in place including register of interests and gifts and hospitality which are subject to regular review and monitoring.

	Statement	ECC Position - September 2020 review
✓	The local authority undertakes recruitment vetting of staff prior to employment by risk assessing posts and undertaking the checks recommended in FFCL 2020 to prevent potentially dishonest employees from being appointed.	Pre employment vetting undertaken as part of the recruitment process
✓	Members and staff are aware of the need to make appropriate disclosures of gifts, hospitality and business. This is checked by auditors and reported to committee.	All staff and members are prompted annually to make the appropriate declarations and this process is subject to regular review by internal audit. All audit reports are reported to the AGS committee.
✓	There is a programme of work to ensure a strong counter fraud culture across all departments and delivery agents led by counter fraud experts.	Annual programme of work approved by AGS committee and mandatory online learning available to all staff.
✓	There is an independent and up-to-date whistleblowing policy which is monitored for take-up and can show that suspicions have been acted upon without internal pressure.	Whistleblowing policy in place and regularly reviewed. Independent external whistleblowing hotline in place which is routinely monitored on a monthly basis.
✓	Contractors and third parties sign up to the whistleblowing policy and there is evidence of this. There should be no discrimination against whistleblowers.	Whistleblowing policy applies to contract staff. Third party whistleblowing policy reviewed as part of the procurement process.
✓	Fraud resources are assessed proportionately to the risk the local authority faces and are adequately resourced.	Regular benchmarking reviewed to ensure that fraud resources are commensurate with other similar local authorities.
✓	There is an annual fraud plan which is agreed by committee and reflects resources mapped to risks and arrangements for reporting outcomes. This plan covers all areas of the local authority’s business and includes activities undertaken by contractors and third parties or voluntary sector activities.	Annual Internal Audit & Counter Fraud plan is agreed by AGS Committee and resources directed as appropriate, considering the fraud risk assessment.
✓	Statistics are kept and reported by the fraud team which cover all areas of activity and outcomes.	Statistics maintained and reported to AGS Committee quarterly.

	Statement	ECC Position - September 2020 review
✓	Fraud officers have unfettered access to premises and documents for the purposes of counter fraud investigation.	Unfettered access granted to internal audit & counter fraud staff.
✓	There is a programme to publicise fraud and corruption cases internally and externally which is positive and endorsed by the council's communications team.	*Partial Compliance* - All outcomes are reported to the AGS committee and details are recorded on the ECC intranet, which is accessible to the majority of ECC staff.
✓	All allegations of fraud and corruption are risk assessed.	All allegations assessed and actioned as appropriate.
✓	The fraud and corruption response plan covers all areas of counter fraud work: – prevention – detection – investigation – sanctions – redress.	Incorporated in the annual internal audit and counter fraud plan, counter fraud strategy. Agreed by AGS committee and circulated to all senior staff.
✓	The fraud response plan is linked to the audit plan and is communicated to senior management and members.	See above
✓	Asset recovery and civil recovery are considered in all cases.	Recovery considered in all cases as appropriate.
✓	There is a zero tolerance approach to fraud and corruption that is defined and monitored and which is always reported to committee.	The approach is documented within the Counter Fraud strategy, and is reported to the AGS Committee.
✓	There is a programme of proactive counter fraud work which covers risks identified in assessment.	This is included in the annual internal audit and counter fraud plan.

	Statement	ECC Position - September 2020 review
✓	The counter fraud team works jointly with other enforcement agencies and encourages a corporate approach and co-location of enforcement activity.	The counter fraud team works jointly with other agencies where appropriate.
✓	The local authority shares data across its own departments and between other enforcement agencies.	Data shared as part of local data matching initiatives (pan Essex), and national exercised (NFI fraud hub etc)
✓	Prevention measures and projects are undertaken using data analytics where possible.	Data analyst in the internal audit and counter fraud team and annual fraud plan includes a program of analytical work.
✓	The counter fraud team has registered with the Knowledge Hub so it has access to directories and other tools.	The members of the CFT are registered with the knowledge hub.
✓	The counter fraud team has access to the FFCL regional network.	The CFT has access to the FFCL regional network
✓	There are professionally trained and accredited staff for counter fraud work. If auditors undertake counter fraud work they too must be trained in this area.	All CFT staff are professionally trained. If auditors undertake counter fraud work they are overseen by the CFT.
✓	The counter fraud team has adequate knowledge in all areas of the local authority or is trained in these areas.	The CFT has a detailed knowledge of all areas of the authority.
✓	The counter fraud team has access (through partnership/ other local authorities/or funds to buy in) to specialist staff for: – surveillance – computer forensics – asset recovery – financial investigations.	The CFT has access to other specialist staff either in house e.g. Financial Investigator or via external contract.

	Statement	ECC Position - September 2020 review
✓	Weaknesses revealed by instances of proven fraud and corruption are scrutinised carefully and fed back to departments to fraud-proof systems.	Control weaknesses considered in all cases and recommendations made to improve control where appropriate. All recommendations tracked and reported to the AGS committee.

Agenda item 7
AGS/79/20

Report title: Counter Fraud and Corruption Strategy	
Report to: Audit, Governance and Standards Committee	
Report author: Paula Clowes – Head of Assurance	
Date: 28 September 2020	**For:** Decision
Enquiries to: Paula Clowes – Head of Assurance paula.clowes@essex.gov.uk	
County Divisions affected: All Essex	

1. Purpose of Report

1.1 This report asks the Committee to adopt the new Counter Fraud and Corruption Strategy which has been reviewed following the recent publication of a new national strategy called 'Fighting Fraud and Corruption Locally'.

2. Recommendation

2.1 That the Counter Fraud and Corruption Strategy is adopted in the form at appendix 1.

3. Background

3.1 The Counter Fraud and Corruption Strategy is reviewed by the committee every two years. The last review was in January 2020 but it was agreed that the Strategy would be subject to further review once the revised national strategy 'Fighting Fraud and Corruption Locally' had been published.

3.2 The national strategy has now been published and a new draft of the ECC Strategy has now been reviewed to align it with the national strategy. The revised draft, which the Committee are asked to adopt, is at appendix 1.

4. Summary of Changes

4.1 The main changes resulting from the review are:

(a) The approach and principles have been revised, adding two further 'pillars of activity', 'govern' and 'protect'
(b) A section has been added to reflect the monitoring and review responsibilities.
(c) The appendices have been removed and replaced with links to external facing documents where appropriate (eg the Fraud Act 2006, FFCL checklist)

5. Financial Implications

5.1 Fraud losses to Local Authorities can be significant if prevention and detection activity is not carried out appropriately.

6. Legal Implications

6.1 Counter Fraud and Internal Audit is a key way in which councillors can be assured that the Council is using its resources effectively and that the Council is discharging its fiduciary duties concerning taxpayers' money. It helps services to design systems which have appropriate controls and also helps identify and respond to breaches if they occur.

6.2 The Council has a duty to consider the need to prevent and reduce crime in the exercise of its functions under section 17 of the Crime and Disorder Act 1998.

7. Equality and Diversity Implications

7.1 Section 149 of the Equality Act 2010 creates the public sector equality duty which requires that when ECC makes decisions it must have regard to the need to:

(a) Eliminate unlawful discrimination, harassment and victimisation and other behaviour prohibited by the Act
(b) Advance equality of opportunity between people who share a protected characteristic and those who do not
(c) Foster good relations between people who share a protected characteristic and those who do not including tackling prejudice and promoting understanding.

7.2 The protected characteristics are age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation. Equality and diversity matters have been considered in the production of the progress report.

8. List of Appendices

Appendix 1: Updated Counter Fraud and Corruption Strategy.

9. List of Background Papers

- Fighting Fraud and Corruption Strategy

Counter Fraud and Corruption Strategy

DRAFT

September 2020

Contents

Foreword – TO BE ADDED

Introduction

Whilst it is notoriously hard to quantify, fraud and corruption has been estimated by the National Fraud Authority as costing UK Local Government at least £2.2 billion a year - money which, today more than ever, is desperately needed to safeguard valuable frontline services. This is why it is vital that as a leading Local Authority Essex County Council has a comprehensive strategy in place to guide our Counter Fraud and Corruption culture, prevention and response. Through its members and officers, the Council works hard to establish a reputation as a responsible guardian of public funds, but we need to be vigilant to ensure that this reputation is safeguarded.

We will do our utmost to foster a culture in which fraud and corruption are kept to a minimum, and any attempt to conduct illegal activity, either internally or externally, against the Council will be robustly investigated. We have clear channels of reporting and transparent procedures to ensure that anyone, whether members of the public or employees, can have full confidence that any concerns raised, or reports made will be treated promptly, thoroughly and appropriately. If fraud is detected, these policies will ensure that internal controls are strengthened, safeguards are improved, and perpetrators

Fraud

Fraud can be broadly described as acting dishonestly with the intention of making a gain for themselves or another, or inflicting a loss (or a risk of loss) on another; including:

- Dishonestly making a false representation
- Dishonestly failing to disclose to another person, information which they are under a legal duty to disclose
- Committing fraud by abuse of position, including any offence as defined in the Fraud Act 2006

The Fraud Act 2006 can be found here.

Bribery and Corruption

The Bribery Act 2010 defines bribery as “the inducement for an action which is illegal, unethical or a breach of trust. Inducements can take the form of gifts, loans, fees, rewards or other advantages whether monetary or otherwise”.

Corruption is the abuse of entrusted power for private gain. It affects everyone who depends on the integrity of people in a position of authority.

Section 7 of the Act created the offence of failure by an organisation to prevent a bribe being paid for or on its behalf. It is possible to provide a defence by implementing adequate procedures to prevent bribery occurring within the organisation. If these cannot be demonstrated and an offence of bribery is committed within the organisation senior officers of the County Council can be held accountable.

Aim of the Counter Fraud and Corruption Strategy

The aim of this strategy is to protect the public purse, Essex residents and ECC assets and ensure that fraud and corruption both within ECC and perpetrated against ECC are kept to an absolute minimum. In instances where fraud and corruption cannot be prevented, effective measures are taken to ensure that a consistent approach is taken to tackling fraud and error. We aim to ensure that robust investigations are conducted and where necessary appropriate sanctions are applied.

By adopting this strategy the council commits to:

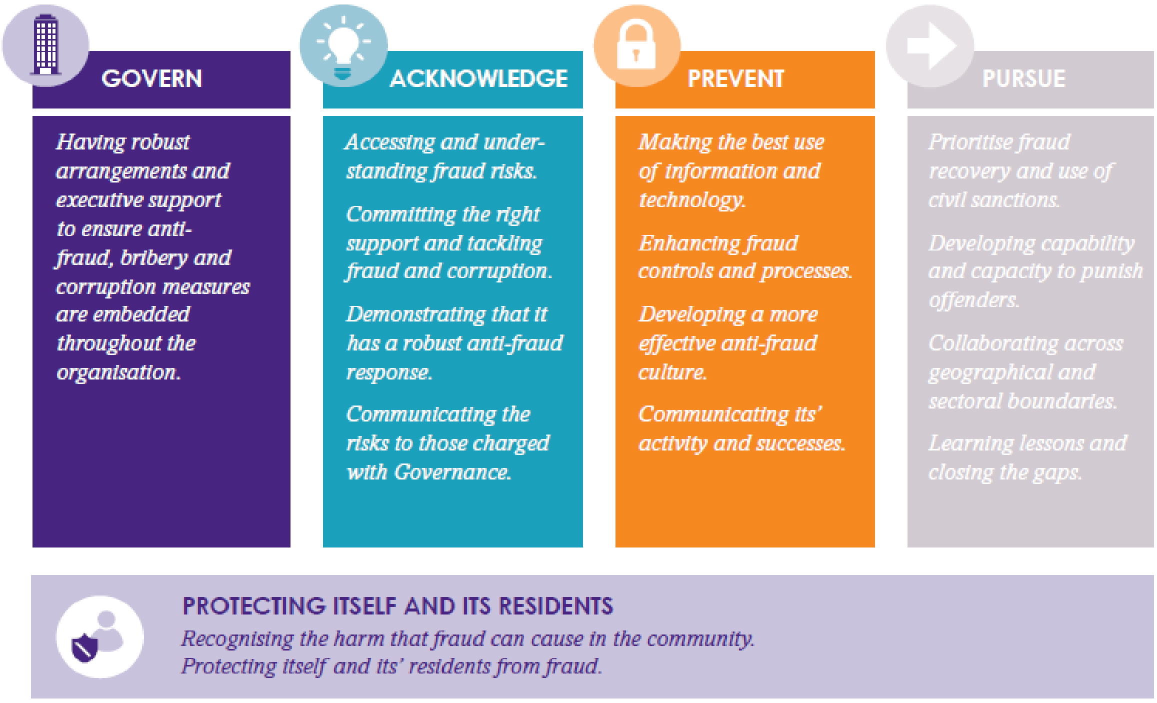
- Develop and maintain a culture in which fraud and corruption are unacceptable
- Continually asses and monitor our fraud risks and control framework
- Continually improve the effectiveness of fraud prevention
- Use technology in the fight against fraud
- Share information effectively via data matching and analysis to help prevent and detect instances of fraud and error
- Maximise the detection of fraud loss and robustly recover losses
- Bring fraudsters to account quickly and efficiently
- Work collaboratively to safeguard vulnerable service users who may be subject to financial abuse.

Our Principles

In compiling the strategy, we have incorporated guidance and best practice in combatting fraud within local government, devised from a number of different sources, as follows:

- Fighting Fraud and Corruption Locally (FFCL) a strategy for the 2020s
- Ministry of Housing, Communities and Local Government - Review into the risks of fraud and corruption in local government procurement
- The CiPFA Counter Fraud Centre

The FFCL strategy highlights the following pillars of activity that local authorities should focus its efforts on to tackle the threat of Fraud.



Protect

The Council takes the threat of fraud and bribery seriously, in that it has the necessary dedicated and specialist resource, comprising of the Counter Fraud and Internal Audit team. These teams are focused on coordinating the approach that the Council takes in protecting its assets and finances from fraud and bribery. The Counter Fraud and Internal Audit teams work closely together to ensure that the Council has a robust control framework in place to reduce the risk of fraud and error.

The overarching objective of the strategy is to recognise the damage that fraud can do to the Council and the residents it aims to serve and protect. We are mindful that every pound lost to fraud and error is one which cannot be spent on Essex residents.

Govern

The bedrock of the strategy is that those who are charged with governance support the activity by ensuring that there are robust arrangements and executive support to ensure counter fraud, bribery and corruption measures are embedded throughout the organisation.

New staff are made aware at induction of their responsibilities and standards of behavior required, which is documented within the Code of Conduct. The Council also promotes the seven principles of public life put forward by the Committee on Standards in Public Life and expect all our staff, contractors, and councillors to make themselves aware of and to follow these principles and all legal rules, procedures and practices, and to protect our legitimate interests at all times.

The Council is committed to the highest ethical standards; high standards of corporate and personal conduct are a requirement throughout the Council. The three fundamental public service values are:

Accountability	• Counter Fraud activity is reported to the Audit, Governanve & Standards Committee on a quarterly basis. Effectiveness reviews of the counter fraud arrangements within the Council are also considered and reviewed on annannual basis.
Probity	• Absolute honesty and integrity should be exercised in dealing with assets, employees, suppliers and customers. ECC maintains a Gifts & Hospitality Register and ensures that Declarations of Interest are regularly captured and reviewed.
Openness	• The Council's actions should be sufficiently public and transparent to promote confidence between Essex County Council, our employees and the public.

Staff are made aware of how to report concerns via the Whistle-blowing Policy. Anonymous referrals may also be made via the Council's external line, Expolink.

Acknowledge

Anti-Fraud Response - Essex County Council accepts that no authority is immune from the risk of fraud or bribery. It is for this very reason that we have implemented a bespoke work programme based on an assessment of risk, to undertake proactive work to protect the assets and finances of the Council.

Training and Awareness - the Council is also committed to providing all employees with sufficient training to enable them to identify and report fraud in a timely manner. This is achieved via e-learning modules at induction. The Counter Fraud Team offer bespoke training packages for key staff within the Council.

The Council also informs councillors of their responsibilities at the induction and reminds them of their responsibilities and update them on developments regularly. Details are also included within the documents published on the Members' portal. These include rules on declaring and registering any possible areas of conflict between a councillor's duties to the County Council duties and any other area of their personal or professional life.

Understanding Fraud Risks - the Council regularly reviews its approach to tackling fraud, with a focus on emerging risks and current themes and trends which occur across the Council, or wider across other local government areas. A fraud risk register is maintained and regularly reviewed by the Counter Fraud team to identify the key fraud risks that the Council is exposed to.

Collaboration - The Counter Fraud Team liaise with colleagues from other authorities to keep abreast of new challenges and emerging risk areas. The Team work closely with service areas to understand fraud risks in their operational areas. A fraud risk register is maintained and updated on an annual basis and used to inform a schedule of proactive work.

Prevent

Prevention is the best and most efficient way to tackle fraud and prevent losses to the Council. Effective prevention will adopt a range of activities to achieve the best outcome.

Enhancing fraud controls and processes - the Counter Fraud Team work closely with Internal Audit colleagues to ensure that a robust control framework is in place within the Council, and recommendations to rectify any system weaknesses are recorded and monitored via our centralised tracking system.

Making the best use of information and technology - a collaborative approach is adopted, working with colleagues in other authorities on data matching initiatives to help prevent fraud throughout Essex. We participate in mandatory National initiatives, for example the National Fraud initiative (NFI) on a biennial basis and also subscribe to other data matching initiatives to help identify any errors or fraudulent activity.

Data analytics - the Counter Fraud Team has a dedicated Data Analyst who completes a programme of internal data matching initiatives to help to identify erroneous or fraudulent transactions and take remedial action as necessary.

Developing a more effective anti-fraud culture – the culture of an organisation can represent one of its greatest defences against fraud and corruption. All Members and employees have a responsibility for promoting a culture of good governance by ensuring that effective measures are in place to prevent fraud and corruption and by promptly identifying and reporting potential instances for investigation. We have a Whistleblowing Policy in place to ensure that suspicions of fraud and error may be reported and robustly investigated.

Communicating its activity & successes - The Council will make best use of its communications strategy to highlight instances of fraud, for the purposes of seeking the maximum deterrence effect. We proactively share with key staff fraud alerts and emerging risks.

Pursue

We have established a robust enforcement response to pursue fraudsters and deter others.

Developing capability and capacity to punish offenders - The Counter Fraud Team is fully resourced and staffed by qualified Counter Fraud Specialists. The team works collaboratively with peers to keep abreast of emerging fraud risks. The Counter Fraud Team also work closely with colleagues in Essex Legal Services to pursue investigations to prosecution, where appropriate and proportionate.

Prioritise fraud recovery and use of civil sanctions - We are aware of and make the best use of legislation, for example the Proceeds of Crime Act 2002, to ensure that funds are recovered where possible by the Council.

Collaborating across geographical and sectoral boundaries - We will continue to work with colleagues in other authorities to understand emerging fraud risk areas and, where possible, take a proactive approach to tackling the risk of fraud and error.

Learning lessons and closing the gap - We will investigate how fraud and error has occurred, understand where weaknesses exist in the system and consider where improvements are required to strengthen the control framework and prevent or reduce the risk of fraud and error reoccurring.

Staff and Stakeholders

Our staff are our first line of defence against most acts of attempts of fraud, corruption or bribery. We expect and encourage them to be alert to the possibility of acts of fraud, corruption or bribery and to raise any such concerns at the earliest opportunity.

Staff have a duty to protect the assets of the Council, including information, as well as property. When an employee suspects that there has been fraud or corruption, they must report the matter to the Counter Fraud Team.

The table below provides further details of these principles and responsibilities of stakeholders.

Group/Stakeholder	Responsibility
Audit, Governance and Standards Committee	• Approve the Counter Fraud Strategy and receive reports of the Counter Fraud activity • Approve the Internal Audit Plan (including counter fraud activity and resource) • Promotes the strategy and ensures that resources are focussed to the Councils high risk areas.
Councillors	• Support and promote the ECC anti-fraud culture • Work within: ✓ The rules around disclosable pecuniary interests in the Localism Act 2011 and associated regulations. ✓ The ECC Code of Member Conduct, the Regulations relating to disclosable pecuniary interests; and our regulatory framework, including the Constitution, Financial Regulations and Procurement Rules and Procedures.
Section 151 Officer	• Has a statutory duty, under Section 151 of the Local Government Act 1972 to ensure that there are proper arrangements in place to administer the Council's financial affairs.
Monitoring Officer	• Has a statutory duty, under section 5 of the Local Government and Housing Act 1989 to report on unlawful activity by the Council. • Responsible for the Internal Audit and Counter Fraud Team
Head of Assurance	• Responsible for the Internal Audit and Counter Fraud Team • Report the results of any fraud or bribery cases to the Audit, Governance and Standards Committee • Act as the Bribery Act Compliance Officer • Act as the nominated Money Laundering Officer.
Senior Managers	• Establish an anti-fraud culture in their functional area(s) • Ensure staff are aware of and promotion of all relevant policies and procedures relating to anti-fraud and bribery, Code of Conduct etc • Adopting a robust control environment, ensuring all internal recommendations are implemented promptly.
Counter Fraud Team	• Deliver a quality investigative service with the objective of preventing, detecting and deterring fraud throughout the Council, thereby securing the "public purse". • Regularly report to the Audit, Governance and Standards Committee on the progress of proactive work undertaken across the Council and on the investigation of actual or suspected bribery; • Liaise with the Police and other enforcement bodies where appropriate and that relevant crimes are reported to the appropriate body. • Ensure that the Council incident and losses reporting systems are followed; • Ensure that system weaknesses identified as part of any investigation are followed up with management or Internal Audit and recommendations made to improve the control framework.
Internal Audit	• Developing an annual risk based approach to internal audit coverage (with consideration of fraud risk) • Reviewing and appraising the adequacy, reliability and effectiveness of the Council's systems of internal control and reporting to Senior Managers • Following up internal audit recommendations to confirm that these have been implemented by Senior Managers in accordance with agreed timescales • Ensure fraud risks are adequately considered in all internal audit assignments
Staff	• Staff must work within: ✓ the Code of Conduct for ECC Employees; ✓ ECC regulatory framework including Financial Regulations and Procurement ✓ Rules and Procedures (for buying any item or service); and ✓ relevant codes of conduct including the standards of appropriate professional organisations and associations. • Have a responsibility to report suspicious of fraud or corruption via the appropriate channels • Must comply with control frameworks within areas of work.

Contractors	Must ensure they have adequate systems and controls to ensure the prevention and detection of fraud and corruption.

Monitoring & Review

This strategy will be owned and approved by the Audit, Governance and Standards Committee on an annual basis.

The effectiveness of this strategy will be subject to regular review by the Head of Assurance and the Audit, Governance and Standards Committee.

Progress reports of Counter Fraud activity will be presented to and monitored by the Audit, Governance & Standards Committee. On an annual basis the effectiveness of the Counter Fraud arrangements will be assessed against the following themes, utilizing tools such as the Fighting Fraud and Corruption Locally Checklist. and the 6 themes (referred to as the 6 Cs) identified in the FFCL strategy, which are:

- Culture
- Capability
- Capacity
- Competence
- Communication
- Collaboration

This information is issued by
Essex County Council, Counter Fraud Team
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The information contained in this document can be translated, and/or made available in alternative formats, on request.

Published September 2020

recycle for Essex

Agenda item 8

	AGS/80/20
Report title: Task and Finish Groups	
Report to: Audit, Governance and Standards Committee	
Report author: Paul Turner, Director, Legal and Assurance	
Date: 28 September 2020	**For:** Approval
Enquiries to: Paul Turner, paul.turner@essex.gov.uk or Paula Clowes – Head of Assurance paula.clowes@essex.gov.uk	
County Divisions affected: All Essex	

1. Purpose of Report

1.1 As part of the effectiveness review undertaken by the Committee in March 2020, the Committee agreed to introduce the facility for it to operate using task and finish groups. This report asks Committee to agree how an action plan following the effectiveness review undertaken in March 2020.

2. Recommendation

2.1 Agree the protocol on the use of task and finish groups as at appendix 1.

2.2 Agree to establish a task and finish group to look at the transforming corporate systems programme.

3. Background

3.1 As part of the effectiveness review undertaken by the Committee in March 2020, supported by the Chartered Institute of Public Finance and Accountancy, the Committee agreed to introduce the facility for it to operate using task and finish groups.

3.2 A protocol at appendix 1 has been developed which says At the last meeting of the Committee, it was agreed that we would commission to support the Committee to undertake a review of its effectiveness. This is in line with recommended practice.

3.2 Accordingly a CIPFA facilitator sent a questionnaire to all committee members and attended County Hall to interview the Chairman, a member of the committee and a number of ECC officers, including the Executive Director for Corporate and Customer Services, the Section 151 Officer, the Monitoring Officer and the Head of Assurance. He also listened to recordings of the Committee meeting.

3.3 On 9 March 2020 a workshop took place facilitated by CIPFA. All members of the committee were invited and eight members attended. Officers were not present as it was agreed that it is important for the committee to say what they want.

3.4 As a result of notes taken by the facilitator and the Chairman of agreed actions, an action plan has been produced. This is appended to this report.

3.5 If adopted we will see changes to the operation of the committee. Given the number of actions in the plan and that the implementation of some of them will need detailed consideration by the committee, it is proposed to phase in the actions over the next year or so.

3.6 One action is that covering reports will include a summary of key points. Key items in the action plan include:

- A pre-meeting before every committee meeting so that members can plan lines of enquiry etc
- Briefings before each meetings on subjects of interest to the committee
- An annual skills audit to be undertaken by the committee
- The addition of a co-opted independent member of the committee
- An effectiveness review to be undertaken annually
- Short term working groups to look at particular topics in detail
- Production of an annual report to council
- Services which receive a ‘no assurance’ audit be automatically invited to attend committee and services which receive a ‘limited assurance’ audit will be considered for invitation by the Chairman

3.7 The commitment to undertake further effectiveness reviews provides a basis for the committee to continue to reflect on its own performance and build on and, if necessary, change what is being agreed today. It is important that the committee ‘owns’ the action plan.

4. Financial Implications

4.1 It is likely that there will be an increased requirement for officer support to the committee but officers believe that this can be met within existing resources.

5. Legal Implications

5.1 The Audit Committee is a key way in which the Council provides assurance that it is providing value for money and has proper systems of control. Without effective assurance Councillors will not know that the Council is effectively carrying out its statutory duties. Whilst the effectiveness review is not a legal requirement it seems a good idea in order to maximise the investment made by councillors into the work of the Committee.

6. Equality and Diversity Implications

6.1 Section 149 of the Equality Act 2010 creates the public sector equality duty which requires that when ECC makes decisions it must have regard to the need to:

(a) Eliminate unlawful discrimination, harassment and victimisation and other behaviour prohibited by the Act
(b) Advance equality of opportunity between people who share a protected characteristic and those who do not
(c) Foster good relations between people who share a protected characteristic and those who do not including tackling prejudice and promoting understanding.

6.2 The protected characteristics are age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation. Equality and diversity matters have been considered in the production of the progress report.

7. List of Appendices

Appendix: Draft action plan

8. List of Background Papers

None.

Meeting	Topic	Author	Notes
16 November 2020	**Internal Audit and Counter Fraud progress report**	Paula Clowes, Head of Assurance	
	To Approve the Statement of Accounts 2019/2020 and the Annual Governance Statement	Nicole Wood, Executive Director, Finance and Technology and Christine Golding, Chief Accountant.	
	2019/2020 Audit Completion Report for the Essex Pension Fund (from external auditor)	Nicole Wood, Executive Director, Finance and Technology and Christine Golding, Chief Accountant.	Annual report
	2019/2020 Audit Completion Report for Essex County Council (from external auditor)	Nicole Wood, Executive Director, Finance and Technology and Christine Golding, Chief Accountant.	Annual report
	Updating of Risk Management Strategy 2017-2021	Paula Clowes, Head of Assurance	Annual report

	Annual Audit Letter – 2019/20 To formally present the External Auditor's Annual Audit Letter for the year ending 31 March 2020	External Auditors	Annual report
	Annual report on the work of the AGS committee	Paul Turner, Director, Legal and Assurance	To thereafter be reported to Council
	The co-opting of at least one independent member to the AGS Committee To provide expertise and steer the members to ask the challenging questions.	Paul Turner, Director, Legal and Assurance	Subject to Council approval July 2020
	To note the inclusion of an AGS Page on the ECC Internet To increase the committee's visibility with officers and members and provide guidance to auditees,	Paul Turner, Director, Legal and Assurance	The page to be on the Intranet by the date of this meeting.

Meeting	Topic	Author	Notes
22 March 2021	**Internal Audit and Counter Fraud progress report**	Paula Clowes, Head of Assurance	
	Arrangements for the closure of the 2020/2021 Accounts	Nicole Wood, Executive Director, Finance and Technology and Christine Golding, Chief	

	Accountant.	
2020/21 Audit Plans for Essex County Council and the Essex Pension Fund	Nicole Wood, Executive Director, Finance and Technology	
Regulation of Investigatory Powers Act 2000 - review of activity on use of Directed Surveillance and Covert Human Intelligence Sources (CHIS)	Paul Turner, Director, Legal and Assurance	
Approval of annual Internal Audit and Counter Fraud Plan for 2021/22	Paula Clowes, Head of Assurance	
Annual skills and knowledge self-assessment To determine where skills and knowledge need to be enhanced on an annual basis	Paul Turner, Director, Legal and Assurance	No later than this (March 2021) meeting.