

# Local Government Audit Committee Briefing

Quarter 3, September 2019





# Contents at a glance



Government and  
economic news **2**

---

Accounting,  
auditing and  
governance **4**

---


Regulation News **6**

---

Key Questions  
for the Audit  
Committee **7**

---

Find out  
more **7**



This sector briefing is one of the ways that we support you and your organisation in an environment that is constantly changing and evolving.

---

It covers issues which may have an impact on your organisation and the Local Government sector as a whole.

Our national Government and Public Sector (GPS) team have produced this briefing using our public sector knowledge, and EY's wider expertise across UK and international business.

This briefing brings together not only technical issues relevant to the Local Government sector but also wider matters of potential interest to you and your organisation.

You can find out more about any of the articles featured by following the links at the end of the briefing.

We hope that you find the briefing informative and should this raise any issues that you would like to discuss further please contact your local audit team.



## Government and economic news

### Spending Review and Tax Reform

A local government think-tank, Local Government Information Unit, has warned the new prime minister has 100 days to save local government finance. Currently local authorities are facing a financial cliff edge because funding for local government beyond 31 March 2020 has not been finalised by central Government. This has hindered the ability of local authorities to effectively budget for the 2020/21 financial year. This may result in decisions being made based on a worst-case scenario such as redundancies, reducing services or selling valuable public assets. The research conducted by the think-tank was based on evidence provided by 254 senior local government figures, and its recommendation are that the new prime minister provides a one-year emergency settlement to enable local authorities to definitively plan for future years.

On the 8 August 2019, the new Chancellor of the Exchequer announced a one-year Spending Review of government departments. Usually Spending Reviews cover three year periods; however, the Chancellor stated that this one-year round will 'clear the ground' for government departments to focus on Brexit. The County Council's Network chairman-elect has called for the spending review to include emergency injection of resources to help councils plug the funding gap across the sector. The Local Government Association (LGA) has calculated the scale of the funding gap for the 2020/21 financial year to be £5bn, rising to £8bn by 2025.

The chief Executive of the Chartered Institute of Public Finance and Accountancy (CIPFA) commented that the Spending Review period of one year was too short to provide the certainty required for medium term financial planning that is critically required to alleviate the fiscal pressures faced by the sector. Reform of the Business Rates and Council Tax systems are seen as critical to achieving long term financial sustainability with the sector. Research conducted by the Institute for Public Policy reported that today's Council Tax resembles a poll tax that is regressive and inefficient. London Assembly member, Tom Copley, commented that the council tax system is 'out of control' to the extent that it is unfit for purpose. The research concluded that an official commission should be established to review and encourage a rethink of the council tax system.

In light of the Spending Review it is now thought unlikely that the fair funding review will be introduced in time to be implemented for the 2020/21 financial year.

## Children's Services and Social Care Pressures

Analysis conducted by the LGA has shown that local authorities overspent on children's social care during the 2018/19 financial year by £800m. This is despite an increase in the children's social care budgets by 6.8% compared to the prior year. The LGA commented that the demand and cost for child protection services is increasing at a faster rate than budgets and funding allow. In order to keep children at risk safe, many councils have been forced to find savings from non-statutory budgets, which include valuable early intervention and prevention support which ultimately stops families and children from reaching the crisis point and requiring child care protection services.

The government has yet to confirm whether grants previously given to local authorities to assist in funding social care will continue in 2020/21. Three temporary grants worth £2.4bn of social care funding, including the Better Care Fund grant, are due to finish at the end of the 2019/20 financial year. These temporary grants have allowed local authorities to bolster care services and help address pressures felt by the NHS. The Council County Network (CCN) has asked the Chancellor to confirm urgently whether this funding will continue as part of the Spending Review that is due to take place. Until confirmed, local authorities may need to plan to decommission services that are directly funded by these grants in order to present a balanced budget.

It is therefore unsurprising that, according to CIPFA's CFO Confidence Survey, 70% of respondents said they were either slightly less or much less confident in their Authority's financial position for 2020/21 compared to 2018/19. A similar percentage of respondents also said that they were less confident in their ability to deliver the same level of public services compared to 2018/19. The survey showed that the greatest pressure for top tier authorities remained children's social care, with adults' social care second place. For district authorities the greatest pressures were housing, environmental services and cultural services. CIPFA has stated that it wants to spend the next 12 months exploring the issues of long-term sustainable funding solutions, and to consider how the local government sector can come together to address the challenges of effective services delivery.

## Value of PWLB loans rises by 75%

The Public Works Loan Board (PWLB) is responsible for lending money to local authorities for capital projects at low rates of interest. According to the PWLB's annual report, the value of loans to local authorities has increased by 75% from £5.2bn at 31 March 2018 to £9.1bn at 31 March 2019. The increase was driven not only by the increased value borrowed, but also by an increase in the number of loans.

Over the last seven years the value of these loans has increased by 84% (£3.2bn 2012/13 to £9.1bn 2018/19). This amplified reliance on PWLB compares to central government funding falling by almost 50% since 2010/11.

### PWLB borrowing by local authorities

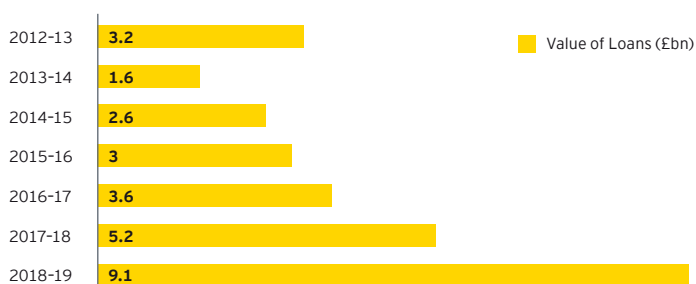
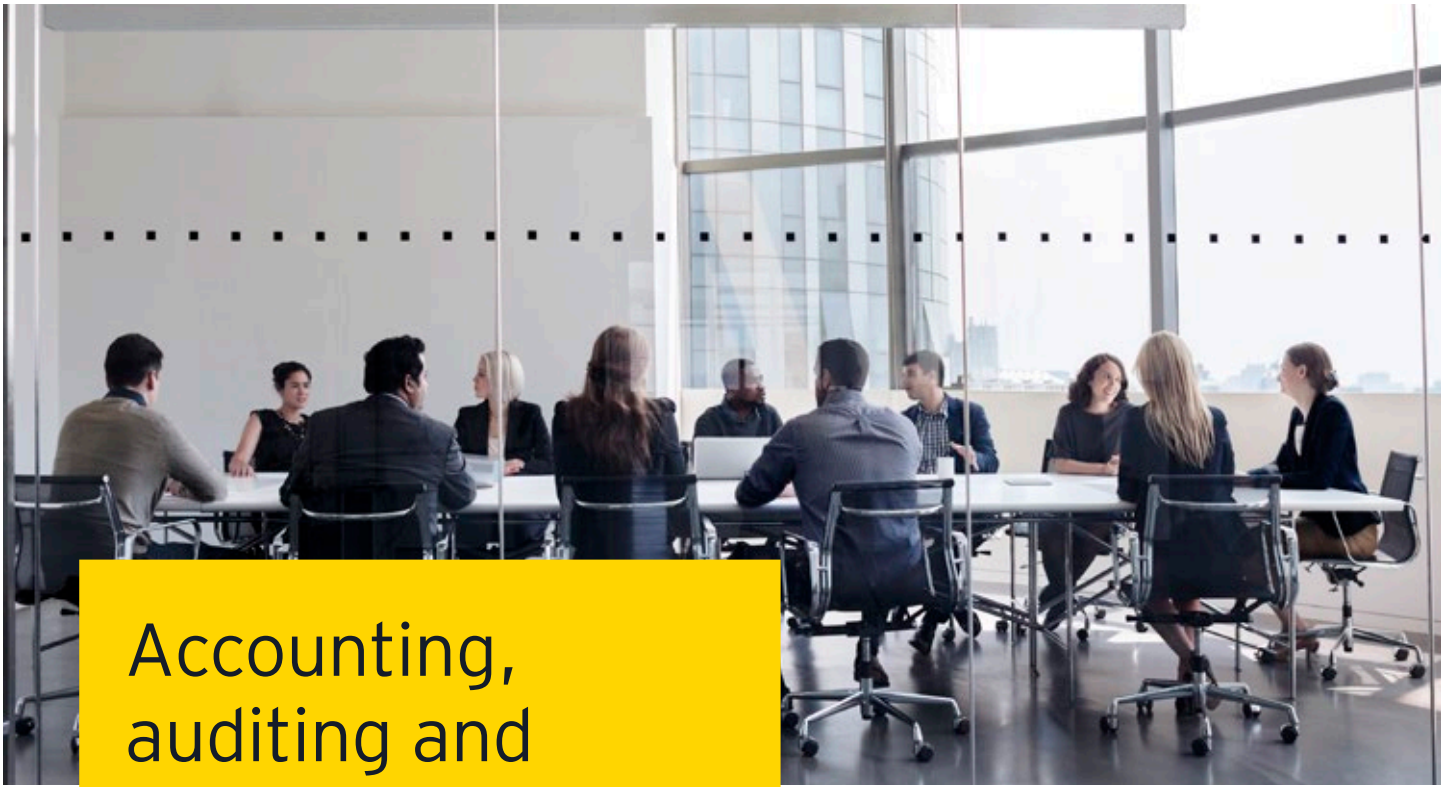


Chart: Dbrady; Source: PWLB annual accounts; Get the data; Created with Datawrapper

Another contributing factor to the increase in PWLB loans is the redemption of Lender Option Borrower Option (LOBO) loans. LOBO loans were popular following the financial crisis and meant that local authorities, including fire and rescue authorities, could take out loans with even lower rates of interest than the PWLB offered. However, lenders could alter the interest rates at certain points in the future. Local authorities, including fire and rescue authorities, refused to pay the higher interest rates and therefore had to pay the loan back in full. These were then replaced with PWLB loans.



# Accounting, auditing and governance

## NAO consultation on the Code of Audit Practice: Phase Two

Under the 2014 Local Audit and Accountability Act (the Act), a review of the Code of Audit Practice (the Code) is required every five years. The Code sets out what local auditors are required to do to fulfil their statutory responsibilities under the Act. This encompasses how audits of a local body's financial statements are conducted, including reporting, and also how assurance is gained on a local body's value for money arrangements. The current form of the Code came into force on 1 April 2015, so a revised Code will be required to take effect from 1 April 2020 for the audit of a local body's financial statements for 2020/21.

The National Audit Office (NAO) is responsible for the Code of Audit Practice and has launched Phase Two of its consultation. The key proposed key changes relate to value for money and include:

- ▶ Enhanced auditor reports on the financial statements. The Code includes the potential for audit reports to include more information on risks and key audit matters, mirroring the audit reports for NHS Foundation Trusts and large corporate entities.
- ▶ Separation of reporting on the audit of the financial statements and value for money and removing the conclusion on value for money arrangements. The Code proposes that the auditor will issue the audit report on the financial statements and then by no later than 30 September issue a separate Annual Auditors Report which will include a commentary on value for money.
- ▶ Revised Value for Money criteria, to cover:
  - ▶ Financial Sustainability – how the local authority plans and manages its resources to ensure it can deliver its services
  - ▶ Governance – how the local authority ensures that it makes informed decisions and manages its risks and finances
  - ▶ Improving economy, efficiency and effectiveness – how the local authority uses cost and performance information data to improve service delivery
- ▶ Mandatory procedures for the auditor to carry out an initial review of value for money arrangements. These procedures will enable the auditor to identify any risk based work and also provide a commentary at any emerging issues at a local body.

- ▶ Revised Value for Money reporting, including the timescales of reporting. Where a significant weakness in VFM arrangements are identified, the revised Code will require auditors to issue a recommendation to the body, setting out judgements made and evidence to support those judgements.
- ▶ Expectations on the speed auditors take on responding to formal objections to a local authority's accounts.

The consultation recognises that the proposed changes will likely alter the work needed to be done by auditors, the resources and skills auditors need to deploy and therefore possibly the fees required to fund the work.

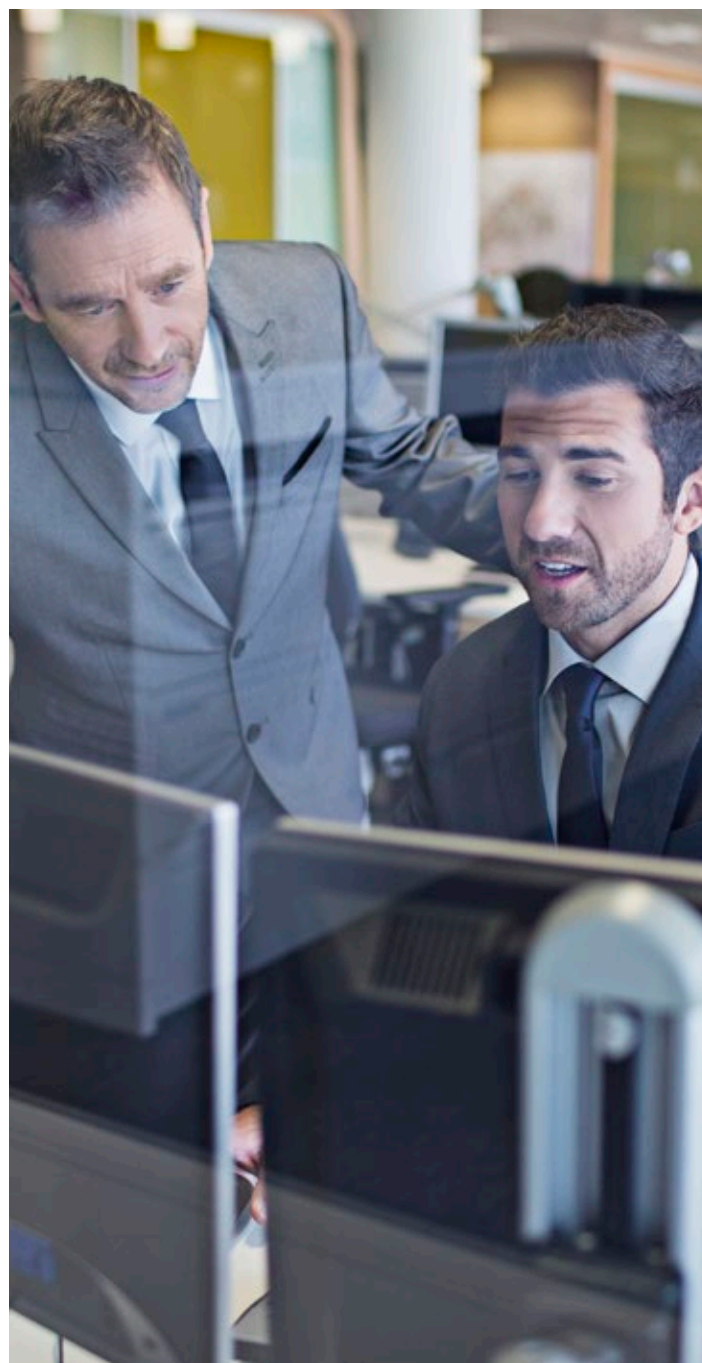
External auditors provide independent assurance that local bodies are properly accounting for spending and that adequate value for money arrangements are in place to manage their affairs. This review of the Code is a valuable opportunity to shape the future of local authority audit. This second phase of the NAO's consultation of the Code is open until 22 November 2019. For more information on how to contribute to the NAO's Code consultation refer to the NAO website.

EY will be contributing to this consultation and playing its part to help shape the future sustainability of public sector audit. We believe the NAO has a critical role to lead and shape the future of local audit and through that role help to secure the future sustainability of the public audit profession. The Code and supporting auditor guidance notes present a significant opportunity to reform local public audit. We also recognise that the consultation comes at a time of significant scrutiny of the UK audit market and profession. We believe it is crucial that the Code is closely aligned with the outcome from various reviews.

### **PSAA records rise in delayed audit opinions**

Public Sector Audit Appointments Limited (PSAA) has released information that 40% of local authorities under its remit did not receive audit opinions on their 2018/19 accounts by 31 July. This is an increase of 27% in comparison to the prior year.

PSAA acknowledge a number of factors have led to the deterioration in performance, posing challenges for both auditors and local authorities across the country. They have called for the issues to be worked through and solutions implemented which will ensure a sustainable supply of audit services in the long term.





# Regulation News

## Independent Audit Quality Review

On 10 July 2019, at the CIPFA annual conference, the Communities Secretary, Rt Hon James Brokenshire MP, announced the launch of an independent review of the quality of local authority audits. This review will examine the effectiveness of the local authority financial reporting and audit regime, including whether auditors are using their reporting powers correctly and if local authorities are appropriately responding to recommendations raised. The review will also look at the expectation gap between what taxpayers believe an audit delivers and what is actually delivered.

The Communities Secretary stated "A robust local audit system is absolutely pivotal to work on oversight, not just because it reinforces confidence in financial reporting but also service delivery and, ultimately, our faith in local democracy."

Sir Tony Redmond, former President of CIPFA, will lead the review. Representatives from EY will be contributing to the review in October. We expect initial recommendations to the Communities Secretary in December 2019, with a final report published in March 2020.

The review of external audit and financial reporting follows the implementation of the Local Audit and Accountability Act 2014, which abolished the Audit Commission and put in place a new localised audit regime in order to improve transparency. This review will meet the Ministry of Housing, Communities and Local Government's commitment to undertake a post implementation review of the revised audit regime framework.



# Key Questions for the Audit Committee

## Spending Review and Tax Reform

What is the size of your authority's funding gap in the medium term? What processes does your authority have in place to address its funding gap?

As members how do you provide effective oversight and governance of these processes?

## Children's Services and Social Care Pressures

What is your authority's year to date performance of children's social care and adult social care services against budget? How is this performance being addressed and what are the implications for next year's budget?

If funding of the Better Car Fund grant (and related grants) is not renewed for 2020-21 what impact will this have on services for your authority?

## NAO consultation on the Code of Audit Practice

Will your authority contribute to Phase Two of the consultation conducted by the NAO?

## PSAA records rise in delayed audit opinions

Did your authority make the publication deadline?

## Find out more

### Spending Review and Tax Reform

<https://www.publicfinance.co.uk/news/2019/07/new-pm-given-stark-warning-over-future-local-councils>

<https://www.publicfinance.co.uk/news/2019/08/councils-call-spending-review-plug-their-funding-black-hole>

<https://www.publicfinance.co.uk/news/2019/06/council-tax-must-be-reformed>

### Children's Services and Social Care Pressures

<https://www.publicfinance.co.uk/news/2019/08/english-councils-overspend-nearly-ps800m-childrens-services>

<https://www.cipfa.org/about-cipfa/press-office/latest-press-releases/local-government-chief-finance-officers-losing-confidence-in-ability-to-deliver-services>

<https://www.publicfinance.co.uk/news/2019/08/umbrella-groups-make-spending-round-plea-social-care>

### Value of PWLB loans rises by 75%

<https://www.publicfinance.co.uk/news/2019/07/pwlb-loans-shoot-751>

### NAO consultation on the Code of Audit Practice

<https://www.nao.org.uk/code-audit-practice/code-of-audit-practice-consultation/>

<https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2019/03/Local-audit-in-England-Code-of-Audit-Practice-Consultation.pdf>

### PSAA records rise in delayed audit opinions

<https://www.publicfinance.co.uk/news/2019/08/psaa-records-dramatic-rise-delayed-audit-opinions>

<https://www.publicfinance.co.uk/news/2019/07/brookshire-reveals-independent-probe-local-government-audit>

### Independent Audit Quality Review

<https://www.gov.uk/government/news/audit-quality-of-councils-will-face-examination-in-new-independent-review>

#### About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation is available via [ey.com/privacy](https://ey.com/privacy). For more information about our organization, please visit [ey.com](https://ey.com).

#### Ernst & Young LLP

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

© 2019 Ernst & Young LLP. Published in the UK.

All Rights Reserved.

ED None

EY-000105308.indd (UK) 09/19. Artwork by Creative Services Group London.



In line with EY's commitment to minimise its impact on the environment, this document has been printed on paper with a high recycled content.

Information in this publication is intended to provide only a general outline of the subjects covered. It should neither be regarded as comprehensive nor sufficient for making decisions, nor should it be used in place of professional advice. Ernst & Young LLP accepts no responsibility for any loss arising from any action taken or not taken by anyone using this material.

[ey.com/uk](https://ey.com/uk)