November 2013

Local Government Audit Committee briefing

Contents at a glance

Introduction

This sector briefing is one of the ways that we hope to continue to 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, the Local government sector and the audits that we undertake. The public sector audit specialists who transferred from the Audit Commission form part of EY's national Government and Public Sector (GPS) team. Their extensive public sector knowledge is now supported by the rich resource of wider expertise across EY's UK and international business. This briefing reflects this, bringing together not only technical issues relevant to the local government sector but wider matters of potential interest to you and your organisation.

Links to where you can find out more on any of the articles featured can be found at the end of the briefing, as well as some examples of areas where EY can provide support to Local Authority bodies. We hope that you find the briefing informative and should this raise any issues that you would like to discuss further please do contact your local audit team.

EY

Building a better working world

Sector and economic news

Proposals for the use of capital receipts from asset sales to invest in reforming services

On 25 July 2013 the Government launched a consultation on 'Proposals for the use of capital receipts from asset sales to invest in reforming services'. The consultation aimed to gather views from the Local Government sector on proposals to allow part or even the whole of a capital receipt from new asset sales to be used for one-off revenue purposes.

The broad aims of the proposed policy are to:

- Encourage good asset management planning and incentivise the appropriate sale of local authority assets so that they are put into productive use and support growth.
- To enable additional resources, from local authority asset sales, to give a capital receipt flexibility for the one-off cost of reforming, integrating or restructuring services.

Views were sought to gauge the level of support for the proposed policy, as well as comments on how it would work in practice and the mechanisms for delivery.

A competitive bidding process is the preferred mechanism for approving such use of capital receipts. It is proposed that any application under a bid based process should set out a cost/benefit analysis to demonstrate value for money.

The criteria to evaluate competing applications from local authorities could include:

- Amount of expenditure and proposed use of that revenue
- The reduction of ongoing/long-term costs
- How you plan to transform your services
- Working across the wider public sector
- Asset to be sold
- Possible forward use of an asset

The consultation also considered how any approved proposals would be implemented, highlighting two possible methods:

- A Direction from the Secretary of State, allowing specified revenue expenditure to be treated as capital expenditure
- Through the existing provisions in The Local Authorities (Capital Finance and Accounting) Regulations 2003 (SI: 2003/3146).

The preferred option set out in the consultation documented is through a letter of Direction from the Secretary of State, as this would more closely fit with the competitive bid process.

Sector and economic news

The consultation closed on 24 September, and it is expected that there will be a response to the consultation in Autumn setting out the finalised proposals. The indicative timeline set out in the consultation document is set out below.

Event	Timing
Bid process commences	Winter 2013
Bid process decisions	Spring 2014
Direction letter issued	Spring 2014
Disposal of Asset	August 2013-March 2016
Revenue Expenditure	April 2015-March 2016

Economic outlook

The ITEM Club, one of the UK's foremost independent economic forecasting groups, sponsored by EY, published its Autumn Forecast in October 2013. It recognises that the UK economy is improving with GDP now projected to grow by 1.4% this year and 2.4% next year after a 0.1% rise in 2012. It notes that this is supported by the encouraging outlook for exports and business investment. It warns, however, that unforeseen events could disrupt this positive outlook, not least new external shocks such as the US budget deadlock. It believes that the view that the UK government's initiatives to support the housing market will result in a housing bubble is strongly overplayed. It states that the current rises in prices and transactions are from a historically very low base, and remain way below pre-crisis levels. With the housing recovery knocking on into wider consumer spending, and virtually all surveys of business confidence trending upwards, the economic outlook for the UK is continuing to brighten – despite the inevitable risks.

Accounting, auditing and governance

Audit Commission briefing on the Local Audit and Accountability Bill

On 4 September 2013 the Audit Commission released a briefing paper on the Local Audit and Accountability Bill, which is currently passing through Parliament.

The briefing provides an up-to-date view of where the Commission believes that amendments and refinements could further improve and strengthen the Bill.

Eight areas are identified in the briefing, where the Commission believes improvements to the bill could be made:

1. Including an option for optional collective procurement arrangements.
2. Strengthening the arrangements for the appointment of auditors, by having external members on audit committees rather than separate audit panels.
3. Expanding the data collected as part of the National Fraud Initiative.
4. Allowing more time to develop a proportionate audit regime for small bodies, by allowing current arrangements to be extended to 2020.
5. Ensuring that there continues to be central returns and publications to support accountability to Parliament and the public.
6. Including reporting on arrangements to secure value for money.
7. Updating the legislative framework governing local public audit.
8. Considering the transitional issues to the new regime, given that contracts under the current framework end in 2016/17 (with potential extensions to 2020), but the Commission, who manage the contracts, is due to be fully abolished in 2015.

Minimum Revenue Provision (MRP)

The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414) became effective from March 2008. These regulations replaced the formula-based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new requirement was for an authority to:

'Determine for the current financial year an amount of minimum revenue provision which it considers to be prudent'.

No definition of 'prudent' was given, although DCLG issued statutory guidance in 2008, which authorities had to take account of, setting out their interpretation. This was updated in 2012 to take account of HRA self-financing and the implications of IFRS regarding PFI schemes. For authorities with a positive Capital Financing Requirement (CFR) the guidance set four out options, but indicated that any alternatives that met the basic criteria included within the statutory guidance was acceptable. The four options are briefly described below:

1. Regulatory Method (for expenditure incurred before 1st April 2008, and supported expenditure incurred after that date):
   - MRP is charged at 4% of the Authority's capital financing requirement (or underlying need to borrow for a capital purpose) which has been reduced by Adjustment A (calculated in 2004 under previous regulations).
2. CFR Method (for expenditure incurred before 1 April 2008, and supported expenditure incurred after that date):
   - MRP is simply charged at 4% of the Authority's capital financing requirement at the end of the preceding financial year (with no technical adjustment).

Accounting, auditing and governance

3. Asset Life Method (for unsupported capital expenditure incurred on or after 1st April 2008):
   - An MRP provision is made over the estimated life of the asset for which the borrowing (or other long-term financing) has been undertaken. This will be based either on the 'equal instalment method' or the 'annuity method'.
4. Depreciation Method (for unsupported capital expenditure incurred on or after 1st April 2008):
   - An MRP provision is calculated in accordance with the standard rules for calculating depreciation provision.

The use of a broad framework rather than the formulaic approach has resulted in incorrect interpretation and calculation of MRP at a number of authorities in the past. Our audit work during the last year identified examples where authorities were not following their own accounting MRP policy or were, in a number of cases, overstating the amount of MRP that they set aside. Detailed work at selected sites identified that these non-compliance and calculation errors had accumulated overstatements of MRP of more than £10mn which could be reversed. Similar in-depth reviews can be incorporated within the 2013/14 audit programmes.

Regulation news

Pensions Regulator to have oversight of public sector pensions

The 2013 Public Service Pensions Act which received royal assent in April afforded the Pensions Regulator an enhanced role – broadening its remit to include oversight of public sector pensions from April 2015. It will set standards of governance and administration for public sector schemes in response to the Independent Public Service Pensions Commission's 2011 recommendations make improvements to both of these areas.

The schemes include approximately 22,000 employers and 12.6mn members (2012 figures taken from the Pensions Regulator website), and span Local Government, NHS, Police, Fire, Teachers, Civil Service, Armed Forces and Judicial pension schemes.

The Pensions Regulator has published a report, together with the supporting research, which documents current practice in these eight categories of public sector pension schemes.

The Pensions Regulator has promised to 'take action if necessary' to ensure public sector pension schemes are run to high standards following government reforms that will see it assuming oversight of the public sector.

Following the passage of the 2013 Public Service Pensions Act the regulator will set standards of governance and administration for public sector schemes from April 2015 including Police and Fire.

On September 6, the Pensions Regulator produced a report summarising current practice in eight categories of civil service pension schemes.

The survey of current schemes found room for improvement but also highlighted areas of good practice.

Local Government Pension Scheme findings:

- The survey noted that governance and administration had been on the agenda for these schemes for several years, and that this was evident in the survey findings, which demonstrated greater awareness of these matters.
- Ninety eight percent had a governance board in place. The majority of schemes also had a risk register in place, with risks and internal controls being reviewed at least annually; a conflict of interests policy and a register of members' interests.
- Eighty one percent of LGPS arrangements are administered in-house and the majority have service standards which are documented and reported against.
- LGPS schemes when compared the others in the survey had the most active member communication.

The Regulator is now working on producing code of practice as well as the regulatory strategy, and has plans to monitor and report on the progress of public sector schemes each year.

Local Government Pension Scheme Structural Reform

In addition to the review of investment regulations noted in the previous sector update, a wide ranging consultation was announced by Brandon Lewis MP (Minister for Local Government) in a speech at the National Association of Pension Funds local authority conference in May 2013. The consultation was launched by DLCG and the LGA in June 2013 and aimed to identify reforms that will both improve investment performance and reduce fund management costs, in advance of the implementation of the new scheme in April 2014.

The consultation closed at the end of September, and the analysis of submissions is expected to inform a further consultation on options for change, which is to be released in early 2014.

At the same time, further detail has been provided about the proposed governance arrangements for the new LGPS in the DCLG discussion paper 'Local Government Pension Scheme (England and Wales) New Governance arrangements, also issued in June 2013.

The paper set out the proposed response to five specific sections of the Public Service Pensions Act 2013 which impact on the governance arrangements of the new scheme:

1. Responsible authority
2. Scheme manager
3. Pension board
4. Pension board information
5. Scheme Advisory board

The intention is for new regulations to be in place before April 2014, which will require new scheme advisory boards and local pension boards to become operational later in the year. In the intervening period between the commencement of the new LGPS scheme and the governing bodies becoming operational, existing governance arrangements under Section 101 of the Local Government Act 1972 will continue to apply.

This consultation closed at the end of August.

Find out more

To find out more on the articles above, please follow the links below:

Proposals for the use of capital receipts from asset sales to invest in reforming services

Full details can be found at:
https://www.gov.uk/government/consultations/proposals-for-the-use-of-capital-receipts-from-asset-sales-to-invest-in-reforming-services.

Economic outlook

For the full analysis go to:
http://www.ey.com/UK/en/Issues/Business-environment/Financial-markets-and-economy/ITEM---Forecast-headlines-and-projections

Audit Commission briefing on the Local Audit and Accountability Bill

The full briefing can be found at:
http://www.audit-commission.gov.uk/2013/09/public-briefing-on-the-local-audit-and-accountability-bill/

Minimum Revenue Provision

For more information, please see the DCLG guidance at:
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/11297/2089512.pdf
For more details on calculating MRP, please refer to Chapter 6 of the Practitioners' Guide to Capital Finance in Local Government (CIPFA 2008).

For details on incorporating a more in-depth review of MRP into your 2013/14 audit programmes, contact your audit team.

Pensions Regulator to have oversight of public sector pensions

For more information see the Pensions Regulator website at:
http://www.thepensionsregulator.gov.uk/index.aspx
and the civil service pension schemes report at:
http://www.thepensionsregulator.gov.uk/docs/public-service-research-summary.pdf

Local Government Pension Scheme Structural Reform:

For further detail on the consultation, and to view all available consultations and consultation outcomes within the Local Pension series please visit:
https://www.gov.uk/government/organisations/department-for-communities-and-local-government/series/local-government-pensions

EY | Assurance | Tax | Transactions | Advisory

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. For more information about our organization, please visit 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.

ED None

1377228.indd (UK) 10/13. Artwork by Creative Services Group Design.

ey.com/uk

This page is intentionally left blank