Local government audit committee briefing

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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.

Building a better working world



Government and economic news

EY item club summer 2015 forecast

In its latest forecast, the EY Item Club highlights the continuing impact on the UK economy of world events, with those in Greece and China being of particular concern. Despite this, domestic demand remains buoyant and activity has increased since winter. They forecast GDP growth of 2.7% for this year and next, and inflation, as measured by CPI, well below target.

The latest data shows consumer expenditure remaining strong, and set to continue into next year, with the strong pound and weak commodity prices keeping inflation low. With manufacturing 'stuck in the slow lane', the economy is seen to be becoming increasingly unbalanced. The forecast goes on to predict that interest rates are unlikely to move above 3% until 2019.

Commenting on the Summer Budget, the Club sees the new surplus target as very challenging, meaning a significant increase in household taxes and a massive squeeze on welfare payments. It comments that, if the public sector is to move from heavy deficit into surplus, the private and overseas sectors must move in the opposite direction. As it sees households as being reluctant to move further into deficit, it will be up to companies to increase investment and exports to make the Budget strategy work. Alternatively, to swing the balance of payments and government accounts back into surplus, growth and imports will have to slow down.

National living wage

In the recent Budget the Chancellor announced that, from April 2016 workers aged over 25 will be entitled to a National Living Wage significantly higher than the current minimum wage of £6.50 which applies to those aged over 21. Those entitled to the 'living wage', will get £7.20 and that will rise to at least £9 an hour by 2020. This is expected to boost the income of approximately six million workers, covering all full and part-time workers, and those in public and private sectors. Whilst the government announced changes in corporation and employment taxes which it said would offset the additional costs to employers, the former will not apply in the public sector, and many comments have been made about the significant impact on employers from bodies such as the Local Government Association and the UK Homecare Association. The EY Item Club (in its Summer Forecast) commented that **"The Chancellor has effectively passed the prime responsibility for supporting low income working people over to employers and this poses a clear risk to hours and employment"**.



Government and economic news

All bodies will need to carefully consider the impact of the changes on their finances in the short and medium term. The impact is not liable to be limited to the additional employment costs of those employees currently on the minimum wage, but include:

- Employment costs relating to employees currently earning above minimum wage but below the National Living Wage
- Pressure on supplier contract prices arising from their increased costs (particularly in relatively low paid sectors such as care)

Whilst the increase is to be phased over a number of years, there will be a potential impact from 2015/16.

Creating a better care system

A new report by EY, commissioned by the Local Government Association, suggests the development of a new sustainable health and social care system, backed by establishment of a £1.3 billion a year transformation fund until 2019/20. It states that the fund should focus on keeping people independent and preventing complex and long-term conditions, and should be supported by:

- A pooled health and social care budget
- Devolved powers for health
- Reformed incentives

It outlines four key areas of focus as follows:

- **Put people in control** – including expanding integrated personal commissioning across health and care, increasing the number of personal health and care budgets by 250,000 in the next five years
- **Integrate and devolve commissioning powers** – including greater local control and freedom over pooled budgets to better respond to local needs and outcomes and allow local innovation
- **Fund services adequately and in an aligned way** – including aligning social care and health funding settlements over a five year period
- **Free the system from national constraints** – including replacing the tariff in the NHS with capitated accounting and payment mechanisms



Accounting, auditing and governance

The 2016/17 code of practice on local authority accounting in the United Kingdom: Invitation to Comment (ITC)

Each year CIPFA issue various Invitations to Comment (ITCs), setting out the proposed changes to the Code of Practice (the Code) for the following financial year and requests responses to the specific proposals. This year the ITC also requests comments on standards that are not expected to lead to changes within the Code until later years The ITC this year has a closing date for responses of 9 October 2015.

The main changes proposed in the ITC are set out below:

Highways network asset

This proposal introduces the requirements for the measurement of this asset at Depreciated Replacement Cost (DRC) from 2016/17 onwards. In the ITC, CIPFA/LASAAC proposes, for the first time, that the separately identified items in the Transport Infrastructure Assets Code are classed as one asset for financial reporting purposes. It is proposed that Highways Network Asset is a separate class of asset and will be shown separately in the balance sheet.

This change is fully retrospective and will require:

- A third balance sheet as at 1 April 2014
- Fully restated comparatives for 2015/16

The ITC also confirms that an annual condition survey will be required.

As outlined in the June 2015 Audit Committee Briefing, this change will have major implications for highway authorities and non-highway authorities who have material transport infrastructure assets. We have already run a number of successful workshops for accountants and engineers at highway authorities during the summer to discuss how this fundamental change will impact on the accounts closedown and audit. As a result we will be running additional separate events for highway and non-highway authorities going forward.

Review of accounting and reporting by pension funds

This review coincides with the publication of Financial Reports of Pension Schemes: A Statement of Recommended Practice (2015). The ITC:

- Proposes minor changes to the Fund Account and to the Net Assets Statement to improve presentation and mirror the updated SORP
- Adapts the reporting requirements of IFRS 13 to include fair value disclosure requirements for pension fund investments in the 2016/17 Code
- Recognises that under IAS 26, three options as to how to disclose the actuarial present value of promised retirement benefits are allowed and seeks views on the option to use
- Sets out a new recommended disclosure for transaction costs

Narrow scope amendments

These are amendments to International Financial Reporting Standards (IFRS), largely around clarification of individual standards.



Accounting, auditing and governance

The Local Audit and Accountability Act 2014 and the Accounts and Audit Regulations 2015 (English Authorities)

The ITC updates the specific references within the Code to reflect these legislative changes. In addition it:

- Considers that a full interpretation of section 3.1 of the Code will fully meet the requirements to produce a Narrative Report
- Highlights the additional guidance provided to enable the requirement that the Narrative Report **"must include comment by the authority on its financial performance and economy, efficiency and effectiveness in its use of resources over the financial year"**

Telling the story: consultation on improving the presentation of local authority financial statements

The financial statements are a vital part of the accountability framework of local authorities. CIPFA/LASAAC considers it vital that the user can relate the information contained within the financial statements to the funding the local authority receives and the promises made about how money will be spent.

Over the past couple of years CIPFA/LASAAC has been developing an approach to both streamline the financial statements and improve accessibility to users. The two publications Financial Statements; *A Good Practice Guide for Local Authorities* and the updated *How to Tell the Story*, have both sought to remove clutter from the financial statements and focus on material items.

The next stage was seen to be how to adapt the IFRS based accounts to improve the accessibility of information for the lay user with the benefits and improvements in reporting that IFRS has brought being retained.

The Invitation to Comment (ITC) sets out the recommended proposals for change, seeking views on whether they are considered to be the preferable option. The key strands of the proposal are that:

- To allow local authorities to report on the same basis they are organised by rather than in an analysis set out by Service Reporting Code of Practice (SeRCOP)
- To introduce a new Funding Analysis as part of the narrative report which provides a direct reconciliation between the way local authorities are funded and budget and the CIES in a way that is accessible to the lay-reader

It is important to note that the Service Reporting Code of Practice (SeRCOP) analysis used for Government returns will continue. Thus the revised approach will not, at this stage, lead to a single financial reporting regime.

The ITC also seeks views on the timing of the proposed changes and the practical effect of introducing this change in financial reporting on authorities. The closing date for responses is 9 October 2015.



Accounting, auditing and governance

EY digital innovation programme

In the digital age organisations are expected to be innovative and tech savvy to support the way they deliver services. As well as making services more accessible, embracing digital offers cost saving potential, and enables organisations to be forward thinking, faster and fitter.

EY has launched a Digital Innovation Programme, a new awards initiative designed to recognise and celebrate digital innovation in health and social care. Its aim is to help share best practice, and recognise and celebrate the patients, carers and citizens who, through their innovative use of digital platforms, have made a positive difference to society.

It is linked to the EY Startup Challenge which is an intensive six-week innovation programme focused on accelerating technological solutions for tomorrow's business problems. Participants will receive:

- Mentoring and coaching
- Access to the EY firm and client network
- Training and support workshops
- An understanding of how to access funding

Nominations close in November 2015 and the programme culminates in a national recognition ceremony in June 2016. More details can be found at http://www.ey.com/UK/en/Industries/Government---Public-Sector/EY-Digital-Innovation-Programme.

Cap on public sector exit payments: consultation

The government announced in May that it intended to end six figure exit payments for public sector workers.

Exit payments help to unlock substantial reductions in staff costs in the medium to longer term and help authorities to meet the challenge of reduced funding available. However, given the scale of the costs associated with exit payments it is vital that they offer value for money to the taxpayer.

The government already has in place, for 2016, legislation to prevent highly paid individuals who return to the public sector within 12 months of exit from retaining their full exit payment.

Following on from this the government believes that it is right to ensure that public sector workers do not receive disproportionately large exit payments in the first instance. In particular the government is concerned about the number of public sector workers who are receiving exit payments of six figures. In 2013-14 alone, nearly 2,000 public sector employees received exit payments costing more than £100,000.

The government has proposed to introduce a cap of £95,000 on the total value of exit payments and HM Treasury launched a consultation on the proposed cap which ended in August 2015.

The current proposal has indicated that compensation payments in respect of death or injury attributable to the employment, serious ill health and ill health retirement will not be in the scope of the cap.



Regulation news

PSAA annual regulatory compliance and quality report

Public Sector Audit Appointments (PSAA) have released their Quality Review Programme annual reports for the 2014/15 audit season. There are individual reports on the seven principal audit firms and an overall summary report that compares all firms. The two main categories auditors are monitored for are audit quality and regulatory compliance.

PSAA have used a Red, Amber, Green (RAG) system throughout their reports. EY were one of two firms that received Green for the combined regulatory compliance and audit quality performance rating with the remaining five audit firms receiving an Amber rating.

For the second year in a row EY have received the highest Audit Quality score improving from 2.49 in 2014 to 2.55 in 2015 compared to a 2015 average of 2.19. Similarly for the financial statement audit work EY topped the table with a score of 2.36 compared to an average of 2.07.

As well as obtaining Green ratings for the two above categories, EY received a Green rating for Whole of Government Accounts work, VFM Conclusion work, Housing Benefit work, Regulatory Compliance, and Client Satisfaction.

The PSAA report on EY states:

"The firm is meeting our standards for overall audit quality and our regulatory compliance requirements. The firm has maintained its performance against the regulatory compliance indicators since last year, with all but one of the 2014-15 regulatory compliance indicators scored as green. The firm's overall weighted audit quality score has increased from last year and the satisfaction survey results show that audited bodies are satisfied with the performance of EY as their auditor."

Based on this review, PSAA state:

"We are satisfied that the risks of audit failure remain low; that all firms are meeting PSAA's regulatory requirements; and that all firms are continuing to produce work to an acceptable standard."

Auditors' work on value for money arrangements

The Local Audit and Accountability Act 2014 provided the Comptroller and Auditor General with the power to issue guidance to auditors which may explain or supplement the provisions of the Code of Audit Practice. This was a role previously undertaken by the Audit Commission.



Regulation news

This guidance is issued in the form of Auditor Guidance Notes (AGNs) and the 2014 Act requires auditors to comply with this guidance.

The NAO is currently consulting on a draft AGN regarding auditors' work on value for money arrangements. The consultation closes 30 September 2015 in advance of the guidance being issued in November 2015. EY and other audit suppliers are currently coordinating their responses to the draft guidance which would apply to audits from 2015/16 onwards.

A short guide to the NAO's work on local authorities

The NAO is publishing a suite of short guides relating to each government department and some cross-government issues. Although the main purpose of these guides is to assist House of Commons Select Committees, the guide on local authorities provides a useful overview for elected members. It includes arrangements for funding, major recent developments, the pressures faced by local authorities, and developments that are on the horizon.

Care Act first-phase reforms: local experience of implementation

Under its powers in the Local Audit and Accountability Act 2014, the Comptroller and Auditor General has published a report concerning the Care Act.

The Care Act 2014 puts new legal responsibilities on local authorities in England and requires them to cooperate with local partners to meet them. The NAO have previously reported that only a fraction of care is publicly funded, with the majority of support and care being provided by unpaid family, friends and neighbours. Many adults pay for all or a proportion of their care. Despite this, adult social care continues to be one of the biggest areas of spending for many local authorities. For 2014/15, the NAO estimates that net spend on adult social care in 2014-15 for local authorities is £14.4 billion.

This further report follows the NAO's report on central government's approach to the Care Act First-phase reforms, and provides examples from local case study areas which show how different authorities are addressing risks arising from uncertainty in demand from carers and self-funders.



Key questions for the audit committee

What questions should the Audit Committee ask itself?

Has the authority considered the impact (both direct and indirect) on its finances of the National Living Wage?

Are there any patients, carers or citizens that we wish to nominate for the EY Digital Innovation Programme?

Are we aware of our responsibilities under the Care Act 2014, and have we considered what changes we may need to make in order to fulfil our responsibilities whilst maintaining affordability?



Find out more

EY item club summer 2015 forecast

For details of the EY Item Club's latest forecast, see http://www.ey.com/UK/en/Issues/Business-environment/Financial-markets-and-economy/ITEM---Forecast-headlines-and-projections

National living wage

Sources include:

BBC – http://www.bbc.co.uk/news/uk-politics-33437115

Local Government Association – http://www.local.gov.uk/web/guest/media-releases/-/journal_content/56/10180/7386419/NEWS

UK Homecare Association – http://www.ukhca.co.uk/downloads.aspx?ID=473

Creating a better care system

Find out more details and a copy of the report at http://www.local.gov.uk/web/guest/publications-list/-/journal_content/56/10180/7350693/PUBLICATION

2016/17 code of practice ITC

For details about the CIPFA Invitation to Comment on the 2016/17 Code of Practice, see http://www.cipfa.org/policy-and-guidance/consultations/201617-code-of-practice-on-local-authority-accounting-in-the-united-kingdom-invitation-to-comment

'Telling the Story' ITC

More information about CIPFA's consultation on 'Telling the Story' can be found at http://www.cipfa.org/policy-and-guidance/consultations/telling-the-story-improving-the-presentation-of-local-authority-financial-statements

EY digital innovation programme

Details of the programme and how to nominate can be found at http://www.ey.com/UK/en/Industries/Government---Public-Sector/EY-Digital-Innovation-Programme

Cap on public sector exit payments: consultation

The details of the Government's consultation on capping public sector exit payments can be found at https://www.gov.uk/government/consultations/consultation-on-a-public-sector-exit-payment-cap/consultation-on-a-public-sector-exit-payment-cap

PSAA annual regulatory compliance and quality report

The PSAA's Audit Quality webpage can be found at http://www.psaa.co.uk/audit-quality/, the annual Regulatory Compliance and Quality Review Programme report is at http://www.psaa.co.uk/wp-content/uploads/2015/07/Annual-Regulatory-Compliance-and-Quality-Review-Programme-2015-Final.pdf, and the report specific to EY is at http://www.psaa.co.uk/wp-content/uploads/2015/07/EY-2014-15-Annual-Regulatory-Compliance-and-Quality-Report-Final.pdf

Auditors' work on VfM arrangements

The consultation document is available at http://www.nao.org.uk/keep-in-touch/wp-content/uploads/sites/11/2015/08/Vfm-arrangements-auditor-guidance-consultation-document.pdf

A short guide to the NAO's work on local authorities

To access the interactive guide see http://www.nao.org.uk/wp-content/uploads/2015/08/A-Short-Guide-to-the-NAOs-work-on-local-authorities2.pdf

Care Act first-phase reform

The full report is available at http://www.nao.org.uk/report/care-act-first-phase-reforms-local-experience-of-implementation/

Notes

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