

Local government audit committee briefing

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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, the Local Government sector, and the audits that we undertake.

The briefings are produced by our public sector audit specialists within EY's national Government and Public Sector (GPS) team, using our public sector knowledge, and EY's wider expertise across UK and international business.

The briefings bring 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.

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

EY Item Club

The latest EY Item Club forecast (Autumn 2016) focuses on the United Kingdom's decision to leave the European Union and highlights that it believes the relatively small impact on the economy to date may be deceptive. The Sterling's performance could be an indication that troubles lie ahead.

At the moment, growth in the economy is being driven entirely by the consumer, supported by rising employment and real wages, as well as ultra-low interest rates. However, sterling's devaluation will push inflation up to 2.6% temporarily next year. With average earnings still subdued, which will slow the consumer. In the meantime, many firms have put investment and recruitment on hold whilst they assess the likely impact of the Article 50 negotiations on their business and consider their long-term options.

Policy uncertainty is feeding through into lower levels of business confidence which we expect to translate into lower investment in 2017. This together with a squeeze on margins from input cost inflation and a tightening labour market in some areas is leading to investment projects that are seen as marginal either being cancelled or delayed, with some of this capital being diverted to other geographies.

Now is the time to update strategies and associated business plans to reflect the slowing macro-environment and emerging policy outlook. Slowing growth and rising inflation together with a depreciating currency which could negatively impact the economy.

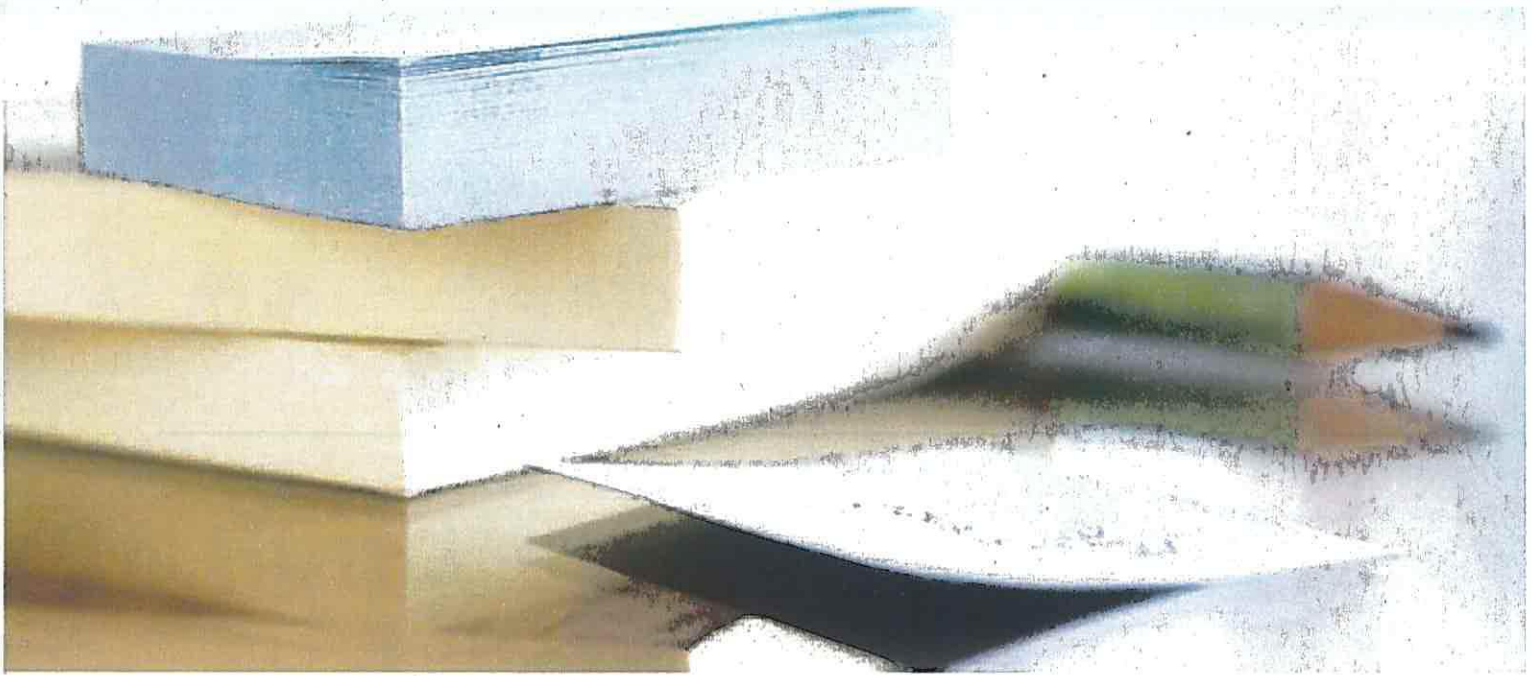
Sustainability and transformation plans

The NHS Planning Guidance issued in December 2015 included the requirement for Sustainability and Transformation Plans (STPs). NHS organisations were asked to work together to come up with a 5-year plan for their area for all areas of NHS spending.

A named individual has been identified to lead each STP. In most cases this is from CCGs, NHS Trusts and Foundations but there are a smaller number from local government bodies.

These STPs have now been delivered and are designed to articulate how individual organisations will play their part in delivering their locally agreed STP objectives, including sustainable financial balance across the health economy.

From April 2017, access to NHS transformation funding will be linked to effective delivery of the STP. STPs represent a shift in focus from the role of competition within the health system to one of collaboration – referred to as 'place-based planning'. NHS organisations are telling us that the changing needs of their populations are best met through integrated models of care, with the delivery of care being best met by different areas of the NHS working in a co-ordinated way. The King's Fund has argued that a place based approach to planning and delivering health and social care services is the right approach – and that this should also include collaborating with other services and sectors outside the NHS – with the aim of improving the health and wellbeing of local populations.



Development and delivery of STPs is a complex task, with large footprints, involving many different organisations, in an already stretched environment in terms of finances and capacity. There are further challenges with the need to address weaknesses in NHS incentives to work together and to avoid organisations focussing on individual goals rather than the effective implementation of STP objectives – for example, NHS Trusts are closely monitored on their own performance targets.

The STPs have been delivered in a relatively short timeframe and propose major changes to services. With the growing financial challenges in the system, the STPs are required to show how they will bring the NHS back into financial balance. Given the short timeframes, the submitted plans will need further development and engagement before they can be effectively implemented.

Four of the STPs have been published early and these demonstrate the significance of the changes being considered under these plans, including reducing the number of acute hospitals and the consolidation of services. Such changes are likely to lead to public and political opposition.

The challenge for STP partners will be to move from the planning phase to implementation in order to realise the objectives agreed.

Treasury confirms public sector pay offs to be capped at £95,000

The Treasury have confirmed that public sector exit packages will be capped at £95,000. The announcement follows a consultation period which heard replies from over 350 interested parties. The changes will apply to the majority of the five million public sector workers. Reflecting on the announcement the Treasury noted that the reduction in exit packages across the public sector would result in significant savings but would still offer a comparable and competitive settlement process similar to that in the private sector.

The proposals include the following:

- ▶ A cap on the salary level at which exit packages can be calculated. It is likely that this will fall in line with the current NHS cap of £80,000
- ▶ The tariff for calculating exit packages will be based on three weeks' pay per year of service with a maximum of 15 months being the cap
- ▶ A clawback proposal would also come into effect which would mean that anyone returning to a public service post soon after leaving with an exit package would be required to repay their redundancy payment



Pension investment schemes

There is a proposal to replace the Local Government Pension Scheme 2009 with new draft regulations as set out below:

The two main areas of reform are:

- ▶ A package of reforms that propose to remove some of the existing prescribed means of securing a diversified investment strategy and instead place the onus on authorities to determine the balance of their investments and take account of risk
- ▶ The introduction of safeguards to ensure that the more flexible legislation proposed is used appropriately and that the guidance on pooling assets is adhered to. This includes a suggested power to allow the Secretary of State to intervene in the investment function of an administering authority when necessary

Revaluation of business rates

The next revaluation of all properties for business rates will take effect from 1 April 2017. From next April, businesses will benefit from the biggest ever cut in business rates in England-worth £6.7bn over the next five years. £3.4bn worth of transitional relief will be available to provide support for the changes. By 2020 councils will be able to keep 100% of all local taxes to fund local services. Invoices will be issued by councils, and the valuations carried out by the VOA, as is currently done, to avoid conflict of interest.

The small business rate multiplier is expected to fall from April 2017 by 1.7p to 46.7p, the standard rate multiplier is also expected to fall by 1.7p to 48.0p.

Schools no longer required to convert to academies

The government will no longer pursue a bill making it compulsory for all schools to convert to academies after protest from Councils, the bill will now only encourage converting.

The original plans required all schools to have converted, or have plans in place to do so by 2022. The announcement coincides with draft plans to introduce more grammar schools in England, reversing the 1998 ban on new grammar schools. And proposals suggesting more schools will be allowed to select pupils based on academic ability which is under consultation until mid-December.

In addition a bill on technical and further education has been published with the aim of boosting the countries productivity by addressing skills shortages by providing high quality technical education. This stems from the independent panel chaired by Lord Sainsbury, which undertook a review of the post-16 skills system and advised Government on measures to improve technical education in England, this led to the Post-16 Skills Plan published in July 2016, which set out the plan to replace thousands of courses with 15 routes into technical employment.



Public sector borrowing

Public sector borrowing for August has decreased by £0.9bn to £10.5bn compared with the same month last year. This is due largely to a decrease in central government net borrowing of £0.4bn as well as a fall in local government borrowing of £0.2bn.

Public sector net debt at the end of August was £1,621.5bn which is equivalent to 83.6% of UK GDP. This is an increase of £52bn compared with August 2015.

The latest figures come 2 months after the vote to leave the European Union in June.

The Emergency Services Network

In 2011 the Government set up the Emergency Services Mobile Communications Programme to look at options to replace the current provider, Airwave Solutions Limited, for communications between personnel in the field and control rooms. The current contract is set to expire in 2019 and the objective was to replace the current service with one that:

- ▶ Makes high speed data easily available to the emergency services
- ▶ Provides more flexibility and takes advantage of new technologies as they emerge
- ▶ Costs less

The chosen option to replace the Airwave service and meet the three objectives is the Emergency Services Network (ESN). The provision of this service has been contracted out to three main providers Kellogg Brown and Root, Motorola Solution and EE Ltd.

The plan is emergency services will start moving to this new network in September 2017 and the process will be complete by December 2019.

It is estimated to cost £1.2bn from April 2015 to March 2020. After this date the ESN is expected to save money compared to Airwave, the current provider.

Barclays changes LOBO loans to fixed rate loans

Following a period of public scrutiny Barclays has changed its Lender Option Borrower Option (LOBO) Loans to Councils and Local Authorities to a fixed rate basis. The LOBO's had initially been offered at lower rates than the other main source of public sector funding the Public Works Loan Board (PWLb) however Barclays always retained the right to adjust the interest rate. This had come under scrutiny and it was argued didn't offer value for money for taxpayers. A series of objections by local electors have been made to the 2015-16 accounts of 24 local authorities that have taken out LOBO loans. The objections predominantly argued that the decision to take out LOBO loans was irrational and unreasonable, and thereby unlawful. Appointed auditors are currently considering these objections under the legal framework for objections contained in the Local Audit and Accountability Act 2014.

Under the changes Barclays has stated that over 100 local authorities and housing associations will benefit from the change. It will also give such bodies much more certainty over their finances in the future as it will remove an element of uncertainty attached with the nature of the loans by locking the loans in at a fixed rate for the duration of the loans. Barclays said that clients impacted had been notified of the change in June 2016.



Accounting, auditing and governance

PSAA as appointing person

In July 2016, the Secretary of State for Communities and Local Government specified PSAA as an appointing person under regulation three of the Local Audit (Appointing Person) Regulations 2015. This means that PSAA can make auditor appointments for audits of the accounts from 2018/19 of principal authorities that choose to opt into its arrangements.

Appointments for 2018/19 must be made by 31 December 2017. Details of the scheme as well as a timetable will be available soon.

Governing culture: practical considerations for the board and its committees

Corporate culture has been a hot topic for many years now and we are finding Boards and Audit Committees are starting to question more and more how they can ensure proper oversight. The EY Corporate Governance team have prepared a report that summarises the findings of the recent EY and FT board survey on culture and their own work at individual organisations.

We would define culture as the collective values and beliefs that exist in an organisation, or parts of an organisation, that inform and influence behaviours, actions and decision making. Culture can then be split into four organisational pillars:

- ▶ Political architecture: where does power lie and how is it used?
- ▶ Performance architecture: how do economic and performance objectives drive behaviour?
- ▶ Social architecture: what values govern relationships and what behaviours do these drive?
- ▶ Operational architecture: how do organisational frameworks, systems and processes affect behaviour?

Audit committees have a unique role to play in the governance of culture, which can directly affect internal control processes, risk management and the integrity of the financial statements. The Corporate Governance team included the following key messages for the audit committee:

- ▶ The audit committee should understand how culture can impact the effectiveness of risk mitigation strategies and support decision making throughout the company in line with the risk appetite determined by the board
- ▶ The committee should consider the cultural context for performance and results and the integrity of the financial statements
- ▶ Data analytics can help the committee create a picture of culture throughout the company, including across international locations. This data should form part of the overall analysis that is used to drive further assurance and oversight efforts
- ▶ The committee should be aware of cultural factors that can influence the relationship with the external auditor. It should use internal audit as a resource for monitoring and championing the desired culture throughout the organisation

If you have any questions on culture or corporate governance then please speak to your external audit team who will be able to provide information on the various pieces of work we have done, and could do, for your organisation.



Regulation news

Gender Pay Gap

Subject to the approval by Parliament the regulations for mandatory reporting on the gender pay gap will come into force during October 2016. However, employers will have around 18 months from commencement to publish the required information for the first time.

Employers with 250 or more employees will fall within the scope of the regulations.

Pay

The regulations will require employers to publish their overall mean and median gender pay gaps as they are complementary indicators. As well as giving employers a better understanding of any pay gaps identified, this will facilitate comparisons with national and international figures.

Bonus

Employers within scope will need to publish the difference between the mean bonus payments paid to men and women (regulation 6). The mean takes into account the full distribution of bonuses paid by an employer. Only those employees who receive 10 bonuses should be included in the calculation. Employers will also be required to publish the proportion of male and female employees that received a bonus.

Salary Quartiles

Employers will be required to report on the number of men and women in each quartile of their pay distribution (regulation 7). Quartiles split into four equal groups, where each group contains a quarter of the data. Employers will calculate their own salary quartiles based on their overall pay range. The objective is to identify the numbers of women and men in each quarter by the overall pay distribution. This is straightforward to produce and will help employers consider where women are concentrated in terms of their remuneration, and if there are any blockages to their progression.

Impact

This is not yet a disclosure requirement but is something that could emerge in the future.



Key questions for the audit committee

What questions should the Audit Committee be asking itself?

What actions are being taken to consider the impact of the UK's decision to leave the European Union?

Do we have appropriate governance arrangements in place to facilitate the delivery of the STP?

Are we ready for the changes to exit package calculations?

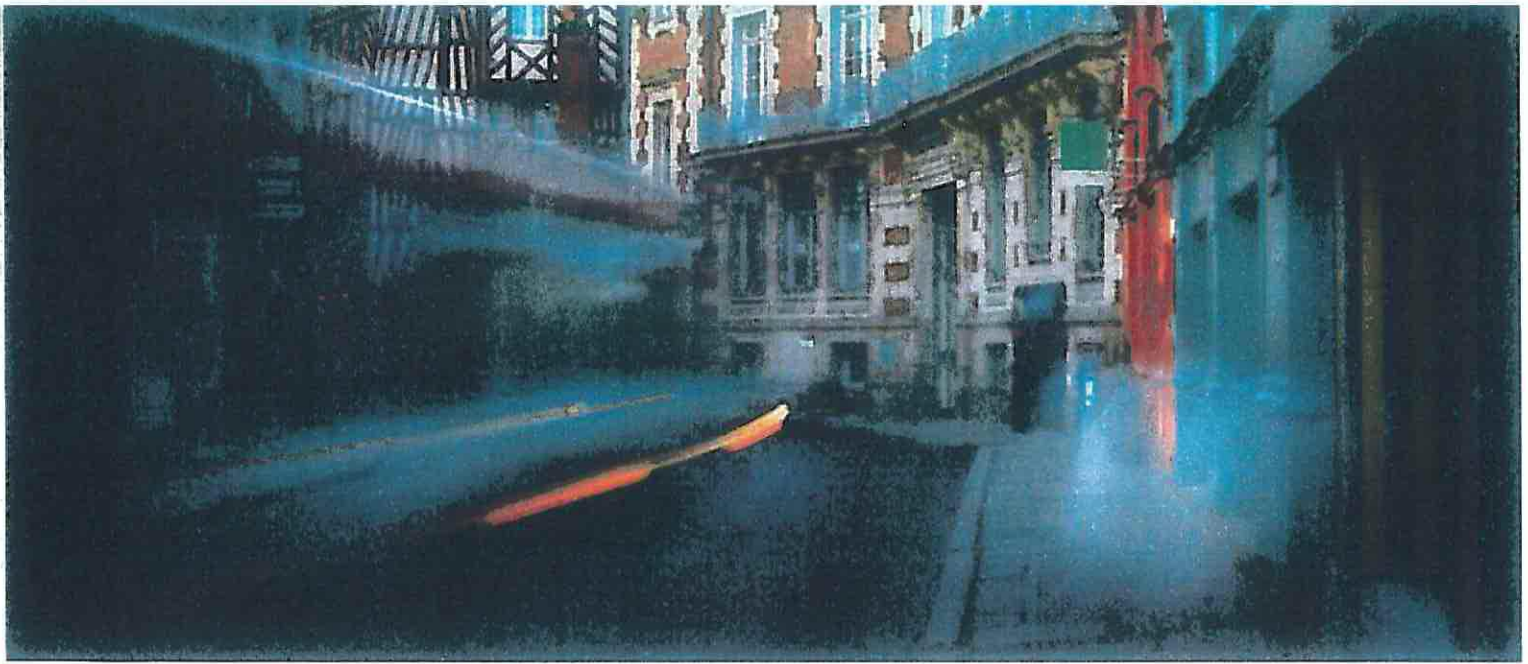
If you are an administering authority has the impact of the proposed changes to the new pension investment scheme been considered and how the local authority will go about determining the value of their own investment?

Did your local authority have a Barclays LOBO and if so have the impact of the changes made by Barclays been considered by your organisation?

Has the local authority got a plan in place to appoint an external auditor before 31 December 2017?

How thoroughly has the committee discussed the impact of culture on risk, risk management and the internal control environment?

Are there systems in place to be able to calculate the gender pay gap, ensuring your organisation is prepared if this does become a requirement?



Find out more

EY Item Club

<http://www.ey.com/uk/en/issues/business-environment/financial-markets-and-economy/item-forecast-headlines-and-projections>

Sustainability and transformation plans

<https://www.england.nhs.uk/wp-content/uploads/2016/02/stp-footprints-march-2016.pdf>

<https://www.kingsfund.org.uk/projects/sustainability-and-transformation-plans>

Exit packages

<http://www.publicfinance.co.uk/news/2016/09/treasury-confirms-public-sector-pay-offs-be-capped-ps95k>

Pension investment schemes

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/479642/Consultation_on_investment_reform.pdf

Revaluation of business rates

<https://www.gov.uk/government/news/government-promises-fairer-bills-for-business-across-the-country>

Schools conversion to academies dropped

<http://www.bbc.co.uk/news/education-37191282>

and

<https://www.gov.uk/government/collections/technical-and-further-education-bill>

Public sector borrowing

<http://www.publicfinance.co.uk/news/2016/09/public-sector-borrowing-falls-august>

The Emergency Services Network

<https://www.nao.org.uk/wp-content/uploads/2016/09/Upgrading-emergency-service-communications-the-Emergency-services-Network.pdf>

Barclays changes LOBO loans to fixed rate loans

<http://www.publicfinance.co.uk/news/2016/09/barclays-ditches-lobo-loans>

PSAA as appointing person

<http://www.psa.co.uk/2016/08/news-release-psaa-specified-as-appointing-person/>

Governing culture: practical considerations for the board and its committees

<http://www.ey.com/uk/en/issues/governance-and-reporting/corporate-governance/ey-governing-culture-practical-considerations-for-the-board-and-its-committees>

Gender Pay Gap

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/504398/GPG_consultation_08.pdf

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