

Question 1: Do you agree with the proposed functions which the system leader for local audit needs to enable a joined-up response to challenges and emerging priorities across local audit? Please let us know any comments you have on the proposal.

Timely and good quality local audit is crucial for sustaining public confidence in local democracy, as the proposals note. Currently, local audit is failing residents, which is in no small part due to the conduct of auditors in their responses to the public's concerns, which effectively hinder the ability of the public to scrutinise the spending and decision-making of their local authority. (see our recent research:

<https://researchforaction.uk/democracy-denied-audit-and-accountability-failure-in-local-government>)

Fragmented and poor oversight is enabling this audit and accountability failure. Thus we agree that a more joined-up approach is needed. However, we have concerns of further neglect of the particular circumstances of the sector when local audit is being placed under the same regulator as corporate audit. ARGA overseeing the quality of local audit will not solve the problem of how best to benchmark and assess quality within that sector. For example, as Emeritus Professor Baron Prem Sikka noted in a roundtable we organised on local audit reform, the IFRS audit standards now used in local audit were designed for auditing commercial entities which have a different purpose.

(<https://researchforaction.uk/event-audit-accountability-failure-in-local-government-where-next-for-reform-7-june>)

We also believe that the ARGA needs functions that are not listed within the current proposals. It needs to take responsibility for carrying out independent inquiries or investigations into issues of concern across multiple local authorities. The LOBO loan scandal

(<https://researchforaction.uk/debt-and-democracy-in-newham-a-citizen-audit-of-lobo-debt>) has highlighted the absence of this, and it is not present in the current proposals either.

The regulator also should have responsibility for investigating and resolving: complaints and appeals about auditors and local authorities; possible conflicts of interest in public sector audit; cross-cutting issues affecting multiple councils; instances where local authorities deny access to

documents; and conducting random, spot reviews of local government audit quality and robustness.

It should look at fraud and corruption and take rigorous action on them.

In the long term, it needs to have the capacity to investigate whether the current, fully privatised audit system is adequate for local government and its needs.

Question 2: Do you have any comments on the proposed functions that ARGA should have alongside its new system leader responsibilities?

When responsibilities are transferred to the new regulation, attention needs to be paid that there are no gaps. For example, all current NAO functions are vital for ensuring that there is at least some oversight of the national picture.

In addition, ARGA should be responsible for monitoring and enforcing the public rights in the LAAA in order for them to be fit for their purpose:

- A transparent public appeal process for handling objections and questions to the auditor should be introduced, including a remit to look at the quality of the responses
- Clear criteria for issuing a public interest report should be introduced. This should at the very least include: objections concerning an issue of national scale or raised in several authorities; subject of objection brought to the attention of regulators; actual or potential financial impact of the issues raised impacting the auditors' ability to sign off on the councils accounts.
- Auditors should provide more detailed reports of their objection handling to ARGA, including time taken and fee charged. This data should be made publicly available.

The ability of local electors to inspect and question the finances of their council is seen as a sign of a healthy local audit regime

(https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/691006/Local_audit_reforms_-_RAND_research_report.pdf).

Currently, the public rights are not upheld, as our research has shown.

(<https://researchforaction.uk/democracy-denied-audit-and-accountability-failure-in-local-government>)

Question 3: Do you agree that the system leader should conduct a full post implementation review to assess whether changes to the Code of Audit Practice have led to more effective external audit consideration of financial resilience and value for money matters two years after its introduction, with an immediate technical review to be conducted by the NAO? Please let us know any comments you have on the proposal.

A fundamental reassessment of public audit should take place with civil society and public interest being central to that process. The immediate technical review by NAO and full post implementation review of the Code are welcome starting points; however, there also needs to be a deeper assessment of the values underpinning public audit. In addition to value for money considerations, there is a need to reassess what the public expects from public audit. Financial resilience is connected to a wider landscape of local government reforms, some of which undermine the sector's long-term sustainability and financial resilience.

Question 4: Do you agree with the proposals to ensure that ARGA has sufficient expertise and focus on local audit? Please let us know any comments you have on the proposals.

The proposals to recognise local audit as its own separate entity within ARGA have the potential to improve the current situation regarding local audit. However, we are not currently sure where the expertise on local audit will come from considering the widely recognised lack of expertise within audit firms and the investment into skills that was lost with the closure of the Audit Commission. The regulator needs a stronger local audit focus for ensuring that a public sector ethos, alongside the skills and appreciation for public audit, is reintroduced.

The precarious financial position of so many local authorities has been described by the Public Accounts Committee as exposing the government “as the funder of last resort” to “significant

risk". (<https://publications.parliament.uk/pa/cm5801/cmselect/cmpubacc/655/65502.htm>) Yet we have seen no substantial increase in timely Public Interest Reports and there has been no sector-wide urgency across audit firms or their regulators to address this growing risk. In order for this to change, strong leadership that puts public interest at heart is needed.

**Question 5: Do you agree with the proposed role and scope of the Liaison Committee?
Please let us know any comments you have on the proposal.**

A Liaison Committee has great potential to coordinate across a fragmented sector. It needs to be ensured that there is sufficient communication between the committee and the oversight functions of the regulator so that ARGA is able to swiftly pick up on issues that might arise, for example financial concerns that have similarities across the sector, and deal with them rigorously.

In addition to bodies listed in the proposals, the committee should include representation from the public - for example, civil society - to ensure public audit works in the public interest. It should also include elected council members - for example, Audit Committee chairs - to ensure that the views from on the ground of the sector are included.

Question 6: Do you agree that the responsibilities set out above will enable ARGA to act as an effective system leader for local audit? Are there any other functions you think the system leader for local audit should have?

ARGA needs to be able to rigorously implement the guidelines that are in place, such as issuing fines for poor audit quality or late completion of audits that can not be passed onto local authorities.

A system leader also needs to ensure it has an overview of whether the current audit regime is functioning. It needs to be able to prompt investigations into auditor conduct when authorities fail - Northamptonshire County Council's Section 114 notice in February 2018 prompted no investigation into the council's auditor KPMG, contrasting sharply with the investigations and reviews of Carillion, its auditor (same KPMG), which swiftly followed the collapse of the outsourcing company only weeks earlier. It needs to have separate functions to monitor fraud and corruption.

ARGA also needs to ensure that the public's concerns are taken seriously in order for audit to be conducted in the public interest. Currently, the public are being actively silenced by auditors when they try to raise concerns through legitimate avenues.

(<https://researchforaction.uk/democracy-denied-audit-and-accountability-failure-in-local-government>)

Question 7: What is your view on the proposed statutory objective for ARGA to act as system leader for local audit? Please include any comments on the proposed wording.

The objective needs to put the public interest at the heart of public audit, which is why we propose the wording:

“System leader for local audit objective: to ensure the local audit system operates effectively and in the public interest.”

However, although public interest is often referenced in local audit discussions, it is currently undefined. There needs to be a clear criteria for what it means for local audit to take into account the public interest and thus be accountable to the public.

Audit is crucial for the functioning of the local government sector and ensuring the financial health of local authorities, which has implications for both public services and democracy. The increasingly frequent Section 114 notices show this is not a trivial matter. Thus the objective of local audit needs to go further than effectiveness, which is a narrow aim for an audit system and does not take into account the need for consulting the public on matters that have direct implications on how their services are financed or their council tax spent.

Question 8: Do you agree with the proposal that ARGA will have a responsibility to give regard to the value for money considerations set out in the Local Audit and Accountability Act 2014? Please include any comments on the proposed wording.

ARGA is best placed to have responsibility for the value for money considerations set out in the LAAA 2014. However, local authorities have wider responsibilities to residents than just value for money, and a wholesale review of the values underpinning public audit is needed.

Question 9: Do you agree that the proposals outlined above will provide an appropriate governance mechanism to ensure that the new system leader has appropriate regard to the government's overarching policy aims without compromising its operational and regulatory independence? Please let us know any comments you have on the proposal.

We have concerns that ARGA is too close to the government to be able to raise concerns about government policy that is harmful to the local government sector if their remit is set by the Secretary of State for Business, Energy and Industrial Strategy as outlined in the current proposals.

Question 10: Do you agree that ARGA's annual reporting should include detail both on the state of the local audit market, and ARGA's related activities, but also summarising the results of audits? Please include any views on other things you think this should include.

ARGA's annual reporting should include detail on the state of the local audit market, ARGA's related activities, and summarising the results of audits, as well as what has been previously covered by PSAA reporting.

It should also include:

- Non-statutory recommendations by auditors
- Number of resident objections raised under the S.5 of the LAAA 2014 across local authorities and their subject matters
- Time taken to respond to objections across the sector. Our research analysing 83 resident objections in three years since the LAAA 2014 came into being found that auditors averaged two years to provide responses to residents. Recently introduced Code of Audit Practice sets a time limit of six months for auditors' responses. This

should be effectively monitored and enforced, with financial sanctions for late responses which cannot be passed onto local authorities

Question 11: Do you agree with the proposal outlined above relating to board responsibility for local audit? Please let us know any comments you have on the proposal.

Board appointments should be made by Parliament, not the government, to ensure that the board remains independent and able to provide appropriate challenge and scrutiny.

There is a need for local audit to be a bigger part of the ARGA's mandate, which ought to be represented in the structure of the board. It needs to have several members with different foci that concern local audit, including representation that ensures accountability to the wider public.

Question 12: Do you agree that ARGA's local audit functions and responsibilities should be funded directly by MHCLG rather than a statutory levy?

We agree that the government is best placed to take on the cost of the regulation of local audit without either undermining the willingness of the firms to conduct audits or the financial viability of the local government sector.

Question 13: Do you agree that ARGA should also take on system leader responsibilities for health audit? Please let us know any comments you have on the proposal.

N/A

Question 14: If you agree that ARGA should assume system leader responsibilities for health audit, do you think any further measures are required to ensure that there is alignment across the broader system?

N/A

Question 15: Do you agree with the government's proposals for maintaining the existing appointing person and opt-in arrangements for principal bodies but with strengthened governance across the system, including with the new system leader? Please let us know any comments you have on the proposal.

N/A

Question 16: Do you agree with the proposal for strengthened audit committee guidance? Please let us know any comments you have on the proposal.

The strengthened audit committee guidance is a welcome start. However, it needs to be binding and it needs monitoring.

We agree with bringing in independent members and increased training. We also believe that processes need to be in place where the public can bring issues into the attention of the audit committee, for example through regular public hearings where residents can raise matters that concern the council's finances or the auditor's conduct, and the audit committee has to take these on board.

Audit committees also need to have clear remit to monitor authorities' compliance with inspection requests under S.5 of the LAAA 2014 and auditors' performance responding to resident objections under the same legislation. According to our research of 155 resident interactions under the legislation, the public rights are currently not upheld by authorities or auditors.

(<https://researchforaction.uk/democracy-denied-audit-and-accountability-failure-in-local-government>)

Question 17: Do you have any views on whether reliance on auditors to comment and recommend improvement in audit committee arrangements is sufficient, or do you think the Department should take further steps towards making the committee a statutory requirement?

Audit committees should be made a statutory requirement. In addition, there should be steps to ensure that audit committee members are able to provide an independent scrutiny function. They should hence not be the same council members who make the decisions in the first place, i.e. Cabinet members for Finance or similar should be excluded from the audit committee.

Question 18: Do you agree with the proposals that auditors should be required to present an annual report to Full Council, and that the Audit Committee should also report its responses to the Auditor's report? Please let us know any comments you have on the proposal.

We agree with the proposals that auditors should be required to present an annual report to Full Council, and that the Audit Committee should also report its responses to the auditor's report. However, we note that this does not sufficiently respond to the concerns regarding "a question as to whether Audit Committees are sufficiently transparent to local taxpayers and service users" as outlined in the proposal. There needs to be a more direct way for the public to engage, for example through regular public hearings where residents can raise matters that concern the council's finances or the auditor's conduct.

As part of their reporting, auditors should present to the audit committee a full disclosure of non-audit (consultancy) work they do for the council as well as any companies that are implicated in pending resident objections to avoid conflicts of interest. In addition to auditing local government, many audit firms act in consultancy roles - even consulting on issues they have then been asked to investigate as auditors

(<https://researchforaction.uk/democracy-denied-audit-and-accountability-failure-in-local-government>). The parliamentary inquiry into Carillion's collapse, which exposed KPMG's lack of due diligence and professional scepticism on the auditing of PFI contracts (<https://publications.parliament.uk/pa/cm201719/cmselect/cmworpen/769/769.pdf>),¹ called for the forced separation of audit and consulting arms to remove possible conflict of interest scenarios.

¹ Business, Energy and Industrial Strategy and Work and Pensions Committees, May 2018, HC769 'Carillion'

Question 19: Do you have any comments on the proposals for amending Key Audit Partner guidance or addressing concerns raised about skills and training?

We share the concerns regarding qualified auditors who understand public audit. According to our research, auditors show a deep lack of understanding of particularities of local finance, including basic concepts such as the cost and risk of fixed vs variable rate borrowing. At present, their conduct frustrates public accountability, as residents' legitimate concerns are not heard and their objections sidelined, despite causing regulatory interventions elsewhere.

(<https://researchforaction.uk/democracy-denied-audit-and-accountability-failure-in-local-government>)

Concerns were also raised in the initial call for views for the Redmond Review: *“many authorities are delivering these services through increasingly complex business models. This means that those providing audit and wider assurance services need to have access to a range of specialist skills and experience beyond audit and accounting. They also need to have sufficient understanding of the wider regulatory framework.”*

(<https://www.gov.uk/government/news/call-for-views-for-independent-review-into-local-authority-audit>)

Training is of crucial importance as the shortcomings in sufficiently qualified auditors should not be remedied by altering the requirements for KAPs.

Auditors should have a sufficient understanding of the wider local authority governance and regulatory frameworks as well as the financial realities facing the sector. They also need to have an understanding that local audit is unlike corporate audit in the sense that auditors too are responsible to the taxpayer for their work.

However, it is only part of the solution: there remains a deeper question of why local audit is not attractive. We believe this is not just a skills and training issue, but also about the mandate of public audit: the profession needs a stronger vision of its purpose. The difference between what the public views on what auditors should do and what they actually do are often dismissed by the audit sector as the ‘expectations gap’. However, this is a highly problematic framing.

Professor Adam Leaver et al reframe this as an ‘accountability gap’: “the shortfall between what the wider public might legitimately expect auditors to do and what the audit process currently delivers”. This framing enables a conversation on “if audit is failing its wider public purpose,

what interventions are needed to restore its social utility function?”

(https://www.sheffield.ac.uk/polopoly_fs/1.884025!/file/Auditing-with-Accountability.pdf)

Question 20: Are there other changes that might be needed to the Local Audit (Auditor Qualifications and Major Local Audit) Regulations 2014 alongside changes to the FRC’s guidance on Key Audit Partners?

N/A

Question 21: Are there other changes that we should consider that could help with improving the future pipeline of local auditor supply?

The expertise that was lost with the closure of the Audit Commission did not all go into the private audit firms. Some of it was lost from the sector. (<https://researchforaction.uk/event-audit-accountability-failure-in-local-government-where-next-for-reform-7-june>) There needs to be investment into training to replace this specific expertise on public audit.

However, public sector expertise also needs to be valued. The deterioration in audit quality since the privatisation of local audit function shows the need for a fundamental assessment of whether the private companies are able to deliver high-quality local audits. Civil society and public interest need to be central to that process.

Question 22: Do you have any comments on the proposal to require smaller bodies to publish their budget statements and variance explanations alongside the Annual Governance and Accountability Return to aid transparency for local service users?

N/A

Question 23: is the current threshold of £6.5 million still right? If you think a different threshold would be more appropriate, please provide evidence to support this.

N/A

Question 24: Do you have any comments on the proposal for a requirement for smaller bodies to transfer to the Category 1 authority audit regime only once the threshold has been breached for 3 years in succession?

N/A