National Audit Office

This supporting information has been prepared to assist the auditor in performing the risk assessment to inform their work on the conclusion on VFM arrangements under Auditor Guidance Note 3 (AGN 03). The supporting information is intended to provide additional sector specific context only. It is NOT part of the statutory guidance and auditors are only required to have regard to the explicit requirements set out in AGN 03. This document should be read in conjunction with *Supporting Information: General Arrangements*.

Auditor Guidance Note 3 (AGN 03) Supporting Information:

Local Authorities

April 2019

This document forms part of the suite of supporting information designed to assist auditors in performing their risk assessment.

The suite of supporting information comprises this document and the following:

General arrangements

Local health bodies

- NHS trusts and foundation trusts (FTs)
- Clinical commissioning groups (CCGs)

Local government bodies

- Police and Fire & Rescue bodies
- Combined authorities
- Other local bodies

These documents will be updated from time-to-time to reflect new, significant sector developments, or updates to the statutory guidance. They are designed to help the auditor undertake their risk assessment.

Supporting information does not include organisation-specific information. Accordingly, the issues included are **neither prescriptive nor exhaustive,** and do not substitute for the consideration of local context.

What's new?

Changes to the supporting information include:

- Financial position;
- Commercialism;
- Business rate retention;
- Local Enterprise Partnerships (LEPs);
- Delayed transfer of care;
- Integrated care systems;
- Capital flexibilities (minor changes); and
- Update to sector resources

Background

This section provides some general information about the sector.

The term "local authority" (LA) covers a wide range of local bodies with varying roles and responsibilities, depending on both their legal status and individual local arrangements each body might have made. Generally speaking, within each area in England services are provided by either a "single-tier" LA or through a "two-tier" LA structure where responsibilities are shared between a county council and a district council.

Single-tier LAs include unitary authorities, metropolitan boroughs and London boroughs. "Two-tier" areas comprise a county council and a number of district councils.

In some parts of the country, strategic or combined authorities have been established to carry out certain functions in an area. For example, the Greater London Authority is responsible for some London-wide strategic functions. In other parts of the country combined authorities have been, or are being, established to carry out specified functions on behalf of two or more local authorities.

There is separate supporting information on other local bodies, combined authorities, and police and fire & rescue bodies.

In some parts of the country smaller local bodies such as parish councils carry out some local government functions. These are out of scope for AGN 03 and therefore are not included in this supporting information. However, where parish councils have opted to produce accounts in accordance with the CIPFA Code of Practice on Local Authority Accounting and undergo a full audit, AGN 03 applies.

Financial position

LAs are funded by grants from central government and locally raised revenues; either through taxation (council tax and business rates) or from fees, charges, or other revenue generating activities. From 2010-11 to 2017-18, LAs have seen their funding from central government reduced by 49 per cent in real terms, in the same period a reduction in their spending power of 28.6%.

Alongside reductions in funding, LAs have had to deal with growth in demand for key services, as well as absorbing other cost pressures. Demand has increased for homelessness services and adult and children's social care. From 2010-11 to 2016-17, the number of households assessed as homeless and entitled to temporary accommodation under the statutory homeless duty increased by 33.9%; the number of looked-after children grew by 10.9%; and the estimated number of people in need of care aged 65 and over increased by 14.3%. Local authorities have also faced other cost pressures, such as higher national insurance contributions, the apprenticeship levy and the National Living Wage.

LAs have faced funding reductions for six years. For the first three years, authorities as a whole reduced spending on services at a rate in excess of their income reductions, allowing them to build up reserves. In the second three-year period, net reductions in service spending accounted for less than half of the required savings. Instead, in aggregate, LAs have increasingly offset funding reductions by reducing other spending – including reducing the cost of servicing debt – reducing their net contributions to reserves or drawing them down, and increasing alternative income such as commercial trading profits or external interest.

LAs have protected spending on service areas such as adult and children's social care where they have significant statutory responsibilities, but the amount they spend on areas that are more discretionary has fallen sharply. Adult and children's social care services have seen a reduction of 3.3% and an increase of 3.2% in real terms, respectively. In contrast, spending on planning and development fell by 52.8% in real terms, with spending on housing services and highways and transport falling by 45.6% and 37.1% respectively. Spending on cultural and related services fell by 34.9%.

LAs now spend less on services, and their spending is more concentrated on social care. Since 2010-11, spending on services has fallen by 19.2% in real terms. This is the net outcome of a 3.0% fall in spending on social care and 32.6% fall in spending on non-social-care services. Consequently, social care now accounts for 54.4% of service spend, compared with 45.3% in 2010-11.

The NAO's report on local authority financial sustainability has identified signs of real financial pressure. A combination of reduced funding and higher demand has meant that a growing number of single-tier and county authorities have not managed within their service budgets and have relied on reserves to balance their books. These trends are not financially sustainable over the medium term. Financial resilience varies between authorities, with some having substantially lower reserves levels than others. Levels of total reserves in social care authorities as a whole are higher now than in 2010-11. However, there is variation in individual authorities' ability to build up their reserves and differences in the rate at which they have begun to draw them down. Some 10.6% of single-tier and county councils would have the equivalent of less than three years' worth of total reserves (earmarked and unallocated combined) left if they continued to use their reserves at the rate they did in 2016-17.

Central government has also changed the way it funds LAs. Until 2013-14, all business rates income was paid to central government and redistributed to LAs via a needs-based formula. Under the Localism Act 2011, and the business rates retention scheme introduced in April 2013, LAs are now able to retain a share of locally raised business rates. The government has put on hold its plan to move to 100% of business rates retention by local government by the end of the Parliament. Business rate retention pilots are continuing, and the government has proposed that it will hold a wider review of fair funding for local authorities.

In this landscape, those LAs that are relatively more reliant on central government funding and are less able to increase locally raised revenues may need to make greater efficiency savings or draw on reserves in order to set a balanced budget. Where LAs are unable to raise revenues sufficient to meet their planned commitments, and do not have sufficient reserves to meet any shortfall, budgets will need to be reduced further which may carry a risk of service failure. LAs with insufficient funding may be at risk of being unable to discharge all of their statutory duties.

Autumn Budget 2018

The Autumn 2018 Budget announced a reduction in the forecast for public sector net borrowing from £37.1 billion as announced in the Spring Budget to £25.5 billion. The Office for Budget Responsibility (OBR) and HM Treasury calculations show that compared with the Spring Budget, borrowing is lower in every year of the forecast and falls as a share of GDP from 1.4% in 2019-20 to 0.8% of GDP in 2023-24.

The government's programme to return public finances to balance by the middle of the next decade and to get debt falling as a share of GDP is continuing and as a result, pressure on public spending remains. The 2019 Spring Statement on 13 March 2019 made no significant changes to the position set out in the Autumn Budget.

Local government finance settlement

The **final local government finance settlement: England, 2019 to 2020** was announced by the Secretary of State for Housing, Communities and Local Government on 29 January 2019. The settlement is the final year of the four-year offer and has been accepted by 97% of councils in return for publishing efficiency plans. The settlement confirms that core spending power is forecast to increase from £45.1 billion in 2018-19 to £46.4 billion in 2019-20 – a cash increase of 2.8%.

The final settlement also includes confirmation additional resources across 2018-19 and 2019-20 to support social care. The funding includes £240 million in both 2018-19 and 2019-20 to support adult social care services to reduce pressures on the NHS and an additional £410 million Social Care Support Grant for local authorities to support adult and children's social care services.

The legal framework

This section sets out the legislation that governs the audited body's sector, together with any statutory guidance issued thereunder. It is included to provide auditors with information about the roles and responsibilities of the audited body as set out in law.

The framework of authorities for LAs is complex and there is a large body of primary and secondary legislation that relates to LA functions. In June 2011 the government (in consultation with LAs) produced an inventory of legislation relevant to LAs.

The Localism Act 2011 sets out a legal framework for local authorities. Section 1 of that legislation confers on local authorities the "*power to do anything that individuals generally may do*". This legislation provided more freedom for local authorities to carry out their own function consistent with statutory obligations.

The Cities and Local Government Devolution Act 2016 has made various amendments to the Local Democracy, Economic Development and Construction Act 2009, including removing the geographical restrictions; enabling the transfer of functions from other bodies to support devolution deals; and it enabling combined authorities to create directly-elected mayors.

Bodies need to have proper arrangements in place for complying with relevant legislation and be aware of new legislation that may affect their functions or responsibilities. While it is a matter for auditor judgement, non-compliance with legislation identified by the auditor (or other inspectorates or review agencies) can have implications for the conclusion on arrangements to secure VFM, depending on the nature and severity of the issue.

The auditor's risk assessment

This section provides some general information about the auditor's risk assessment.

AGN 03 describes what "proper arrangements" comprise for the purposes of the work under the Code, and the sector developments and contextual information in the section below have been grouped according to sub-criteria set out in the AGN. The AGN states:

> *"Auditors are not required to consider all illustrative significant risks set out… [and] should consider the illustrative significant risks insofar as they are consistent with their understanding of the audited body."*

Similarly, the sector-level developments are only intended to be considered where the auditor deems them relevant. And as the AGN further states:

> *"Where other matters come to the auditor's attention which – in the auditor's judgement – are relevant to the discharge of their duties in respect of VFM arrangements under the Code, their impact on the risk assessment should be considered, irrespective of whether or not the issue is explicitly referenced within the scope of proper arrangements."*

Therefore, the auditor is ultimately responsible for preparing and documenting a risk assessment that mitigates the engagement risk.

Sector developments and contextual information

This section contains contextual information that may be relevant to the body's general arrangements, and sets out some of the current developments within the sector. The material may be helpful to auditors when undertaking their risk assessment.

The examples below are neither prescriptive nor exhaustive, and should not be used as a checklist. In addition to this sector specific supporting information, auditors should also refer to *Supporting Information: General Arrangements,* which contains further contextual information applicable to all sectors. The information in this section does not cover developments at individual audited bodies and auditors are also likely to need to draw on their own local knowledge.

Sustainability

The continuing financial pressures within local government have been widely publicised, including in the NAO's 2018 report '*Financial Sustainability of local authorities 2018*', which was brought to the attention of local auditors in March 2018.

The report finds that the sector has done well to manage substantial funding reductions since 2010-11, but financial pressure has increased markedly since our last study in 2014. Local authorities face a range of new demand and cost pressures while their statutory obligations have not been reduced. Non-social-care budgets have already reduced substantially, so the scope for delivering further savings is reducing.

In response, LAs are looking to generate alternative income streams to help them remain financially sustainable. Auditors will be aware that in recent years, the number of local government bodies receiving non-standard auditor reports has remained relatively static over the past three years.

The NAO's report '*Local auditor reporting in England 2018'* highlighted that, as at 17 December 2018, and with 20 still be issued for 2017-18, auditors had qualified 40 (8%) of their conclusions on LAs' arrangements to secure value for money; in 2015-16, 40 (8%) were also qualified. The proportion of qualifications for 2017-18 to 17 December 2018 was highest for single tier local authorities and county councils where auditors qualified 27 (18%) of their conclusions. The qualifications were mainly for weaknesses in governance arrangements, often also highlighted by inspectorates' ratings of services as inadequate.

Capital Flexibilities

Many LAs are facing significant pressures on revenue budgets, making the setting of a balanced annual budget a challenging process. Authorities may therefore look to use existing schemes to support their revenue budgets such as the use of the capital receipts flexibility.

There are strict rules in place which restrict authorities from spending capital receipts on revenue items. The Local Government Act 2003, sections 16(2)(b) and 20 allow, under certain circumstances, the use of capital receipts from the disposal of property, plant and equipment assets generated during years in which the capital flexibility is offered, to help fund the revenue costs of transformation projects and release future savings. This potentially allows authorities who are asset-rich but cash-poor to fund transformation schemes that would not otherwise be possible.

A Direction from the Secretary of State in December 2015, and the subsequent Direction in December 2017, allows authorities to use capital receipts generated in the years 2016 until 2021 to fund revenue expenditure if it is designed to generate ongoing revenue savings from service reform or any transformational project. Upfront costs on projects which will generate ongoing savings is considered as ‘qualifying expenditure’. The statutory guidance issued by the Ministry of Housing, Communities & Local Government (MHCLG) includes a list of projects that can be considered by authorities that fall under the definition of ‘qualifying expenditure’.

The guidance requires that details of the individual projects that will be funded or part-funded through the capital receipts flexibility are reported to the full council or the equivalent. This requirement is often satisfied through the annual budget-setting process, through the Medium-Term Financial Plan (MTFP) or equivalent or, for those authorities that sign up to a four-year settlement deal, as part of the required Efficiency Plan.

Issues which may be of particular relevance to informing the auditor’s VFM arrangements risk assessment at bodies making use of such flexibilities might include:

- The robustness of assumptions in the MTFP on the expected savings from the service reform or transformational projects. For example, if the originally planned savings or outcomes from use of the flexibilities in year one looks unrealisable, there may also be risks to the achievement of savings and outcomes planned for year two. In these circumstances, it may no longer be appropriate to continue using capital flexibilities to fund the expenditure, which could have implications for service delivery and sustainable resource deployment.

- Lack of transparency or accountability in respect of the plans setting out what will be delivered by the projects that are to be funded by these capital receipts.

- A lack of transparency could raise the risk that the authority may be planning to apply capital receipts to fill gaps in its general revenue budget (for example, to avoid spending cuts or to support activities that are otherwise financially unsustainable), rather than applying it specifically to transformational projects as required by the guidance. This could indicate weaknesses in arrangements for sustainable resource deployment.

- Failure to report adequately to members in terms of the planned use of the flexibilities and the risks associated with the projects funded by the flexibilities could indicate weaknesses in the authority's arrangements to support informed decision making.

Business Rates Retention Reform

Business rates retention was introduced in April 2013 and was designed to give authorities more control over the money they raise locally. The government has indicated that it is committed to further business rates retention and announced in 2017 that it would aim to introduce 75% business rates retention from 2020. In addition, the government plans to conduct a relative needs and resources review but this would be subject to a separate consultation.

In December 2018, the government opened a consultation on business rates retention reform which focuses on how business rates retention system works. The consultation covers two broad objectives:

- The balance of risk and reward in the business rates retention system with the expectation that local authorities would continue to receive the benefit of growth they achieve in their local areas.
- The work undertaken to develop options to mitigate volatility in income and address the impact of appeal losses and valuation change on local authorities.

The government has had two previous consultations on business rates retention and the design of the rates retention system. They include:

- **Self- sufficient local government: 100% Business rates Retention** (published July 2016); and
- **100% Business Rates Retention - Further consultation on the design of the reformed system** (published February 2017)

The reform of the business rates retention system is proposed to sit alongside wider changes to the local government finance system, which the government plans to introduce in 2020.
The current consultation document can be found at **Business rates retention reform** (published in December 2018).

The provisional local government settlement announced in December 2018 included provisions for local authorities to keep around £2.4 billion in business rates growth and the distribution of £180 million of the levy surplus to all local authorities on a basis of need. In addition, the government announced that it was aiming to increase the level of business rates retention from its current levels of 50% to 75% from 2020.

The final local government finance settlement announced in January 2019 confirms that £180 million will be returned to local authorities and distributed based on each local authority's 2013-14 Settlement Funding Assessment. The final settlement also confirmed that London and 15 local authorities will participate in the 75% business rate retention pilots. These local authorities include:

- Berkshire;
- Buckinghamshire;
- East Sussex;
- Hertfordshire;
- Lancashire;
- Leicester and Leicestershire;
- Norfolk;
- North and West Yorkshire;
- North of Tyne;
- Northamptonshire;
- Solent Authorities;
- Somerset;
- Staffordshire and Stoke-on-Trent;
- West Sussex; and
- Worcestershire

In addition to the above, ongoing pilots are continuing in 5 devolution areas.

The NAO published a report in March 2017 that examined MHCLG's planning arrangements for 100% local business rates retention and its links with other issues such as devolution. The report can be found on the NAO website – Planning for 100% local retention of business rates. The issues raised will be relevant if MHCLG reintroduce the Bill to be considered by Parliament.

This introduces a significant degree of uncertainty into local government medium-term financial planning. We do not expect authorities to be specifically considering the impact of 100% retention when producing Medium-Term Financial Plans (MTFP); authorities should be planning on the basis that the existing funding arrangements will continue in the medium term.

Commercialisation

LAs have sought ways of generating income in constrained financial circumstances. The scale of investment activity, primarily in commercial property, has increased in recent years. These activities are often discharged via a company, partnership, or other investment vehicle. However, the nature of commercial investments appears to be changing. For example, there are more joint ventures being entered into with asset-backing arrangements as opposed to the more traditional debt-backed schemes.

Where authorities enter into commercial schemes to generate revenues to reduce pressure on budgets, this can lead to authorities seeking the maximum returns possible. This may expose them to risks that they have not anticipated, including:

- poor financial forecasting;
- not having sufficient commercial expertise;
- not having the skills and experience to manage commercial property effectively; and
- not investing in existing proven commercial property whose revenue stream can be more accurately valued.

Authorities may also be investing to achieve a number of competing priorities, for example economic regeneration as well as an income stream. This could see voids or discount rents to support the regeneration aspect, but which may not be sufficient to cover the income stream requirement.

There is also a risk that authorities may not involve the auditor early enough in discussions when planning these schemes, or consider the accounting implications or risks from changes to the regulatory or accounting framework. Whilst authorities have a general power of competence, they should follow the Wednesbury principles of reasonableness and are required to comply where there is already an existing legal duty, e.g. compliance with the capital financing regulations and minimum revenue provision guidance.

Authorities should also be mindful of changes in the accounting and regulatory environment as part of any sensitivity analysis being conducted, for example, ensuring the implications of the adoption of IFRS 9 have been considered, particularly given that the statutory override is only for a period of five years. As under IFRS 9, gains or losses or investments may need to be taken directly through the income and expenditure statement. This would have a direct impact on the general fund and, in the current absence of any statutory override, impact on council tax payers.

Entering into commercial activity on this increased scale requires local authorities to have appropriate governance and corporate arrangements to plan and deliver these schemes. In some cases, new commercial schemes dwarf the current assets held by the authority making it potentially a significant risk area. This can be coupled with more complex forms of financing or delivery vehicles and may also be happening outside of the local authority geographical area, raising questions of local scrutiny and accountability.

Issues which may be of particular relevance to VFM arrangements considerations might include:

- assumptions in the MTFP around likely levels of income, which may be more volatile in a commercial environment, and require more sophisticated forecasting and sensitivity analysis;
- increased risks in terms of the value of the assets, which may be determined by factors over which the authority has no control, and which might make it difficult for the authority to dispose of the assets without incurring losses;

- impact on the authority's capital/revenue planning, as investments or reserves which could previously have been used to support revenue spending may become capital receipts upon disposal;
- potential for increased refurbishment/maintenance costs when compared to operational assets, as commercial properties will need to keep pace with market expectations in respect of, for example, facilities and décor; and
- opportunity cost of investing out of area with a view to generating income streams, while there are competing demands for additional spending within the authority's area. A decision to invest out-of-area may have a consequential impact on the adequacy of the authority's arrangements elsewhere.

Auditors may also want to consider consistency with other published information in terms of what the authority says about value for money in their narrative statement.

Changes to statutory codes and statutory guidance

In 2017-18 there have were changes to key statutory codes that bodies need to comply with. CIPFA have issued updated Prudential Code and Treasury Management Code. MHCLG have issued revised statutory guidance on setting the Minimum Revenue Provision and investment guidance.

Prudential code

In the preparation of the financial statements, authorities will need to ensure that their commercial activity is presented in a true and fair manner and complies with the accounting code and statutory framework, including the Capital Finance Regulations and the Minimum Revenue Provision (MRP) Regulations. Authorities will need to consider the impact on both the single entity financial statements and the need to prepare group accounts.

Authorities borrowing to finance these types of activities will need to ensure they have regard to **CIPFA's Prudential Code for Capital Finance in Local Authorities**. Where these activities are held as an investment, the authority must have regard to CIPFA's Treasury Management Code and MHCLG's Investment Code.

CIPFA has published both an updated Prudential Code and Treasury Management Code. The key change is the introduction of a formally reported capital strategy to provide full council (or equivalent) with a concise, accessible view of the authority's approach to borrowing, investment and treasury management, with a focus on risk management. This will ensure that commercial activity scores against prudential borrowing limits and that the entire group position is taken into consideration and reported in the prudential indicators. Section six of the Prudential Code reminds authorities that they "should also consider carefully whether they can demonstrate value for money in borrowing in advance of need and can ensure the security of such funds". CIPFA is concerned that authorities may be putting themselves at risk of breaching this requirement and therefore will be issuing further guidance in due course.

Statutory Investment Guidance

MHCLG has published updated Statutory Investment Guidance which applies from 1 April 2018. The guidance requires that authorities:

- prepare an investment strategy at least once a year that is approved by full council. This can be incorporated into the capital strategy required by the Prudential Code;
- disclose the contribution that investments make "towards the service delivery objectives and/or place making role of the local authority";
- include indicators that enable councillors and the public to assess the authority's investments and the decisions taken, including suggested indicators on gross debt as a percentage of net service expenditure and commercial income as a percentage of net service expenditure;
- must not "borrow in advance of need" to profit from the investment of the sums borrowed. This requirement now applies to non-financial investments (e.g. investment in commercial property that is solely commercial) rather than just financial investments. This broader interpretation is based on application of all parts of the prudential framework, including the two CIPFA codes. In the past, investments in commercial property would have counted solely as capital expenditure and so could have been funded from borrowing; now this will only apply where the council can justify that the investment is not wholly commercial; and
- if they do borrow in advance of need for profit must set out the reasons for their non-compliance in the strategy and their risk management arrangements.

Auditors should be aware of the impact of MHCLG's updated guidance, particularly on the reporting of authority commercial investment activity. Where an authority has borrowed in advance of need for profit, auditors should consider both the compliance requirements and the implications of wider public law. Auditors will need to consider the impact of this on their VFM arrangements conclusion, the opinion on the accounts and the use of their wider reporting powers.

Implications of fire safety reviews

Local authorities are undertaking fire safety reviews of their housing stock. To date 149 high rise council stock buildings in 45 council areas have failed fire safety tests. Where the council is responsible for the building, they will be expected to make it safe.

For 2018-19, auditors may need to consider whether bodies' MTFPs have addressed this risk, particularly if significant additional costs are not likely to be matched with additional funding. Authorities will want to consider wider issues such as the adequacy of their arrangements for contracting and building safety inspection.

All local authorities including FRAs received a four-year settlement up to 2019-20 in return for publishing their efficiency plans. MHCLG is currently undertaking a review of all local authority funding formulas including the fire formula. The Home Office will lead on fire and is engaging with the sector in relation to the formula and indicators, however, no implementation date has been confirmed.

Informed decision making

Where the authority is in the process of considering making a significant decision, it may be necessary to revisit supporting business cases to ensure that the authority's considerations take account of any significant impacts on medium- and longer-term financial planning that have been identified. Set out below are some areas that auditors may wish to consider.

Combined authorities

A number of combined authorities (CAs) have been established to date and include Greater Manchester, Sheffield City Region; Liverpool City Region; North East Combined Authority; West Yorkshire Combined Authority; Tees Valley Combined Authority; Cambridgeshire and Peterborough; West of England; and West Midlands Combined Authority.

The Localism Act 2011 permits the Mayor of London to create mayoral development corporations (MDC) in Greater London. The object of an MDC is to secure the regeneration of its area. There are two mayoral development corporations in London:

- London Legacy Development Corporation (LLDC), established in 2012, replacing the Olympic Park Legacy Company; and
- Old Oak and Park Royal Development Corporation, established in April 2015.

The government and local leaders announced proposals to establish a MDC for the Tees Valley (the South Tees Development Corporation), the first such corporation outside London. Powers from the 2011 Act to designate an MDC outside Greater London were created by a 2017 Order. The objective of the proposal was to drive forward growth and investment, create jobs, and support local communities in the area in light of the closure of the SSI steelworks site in Redcar and Cleveland.

CA's can take a long time to become formally established due to the number of parties and stakeholders involved in the various stages in agreeing proposals. Further information is included in the supporting information for CAs and similar bodies.

Long-term commitments

In recent years, the level of public scrutiny of significant borrowing or investment decisions has increased, not only in respect of current activity, but also historic decisions that continue to impact the authority's financial position or arrangements for delivering services in the current financial year. Some of these decisions relate to very long-term arrangements to which the authority is committed, such as borrowing for long periods (sometimes in excess of 30 years), or decisions to enter into schemes such as PFI.

Where an authority has not retained sufficient relevant documentation from the time the decision was made, it can be difficult to explain the rationale that lay behind the original decision, should it be questioned or challenged in respect of its impact in the current financial year. Where authorities have, or are in the process of entering into, significant long-term borrowing or investment arrangements, auditors may wish to consider the extent to which authorities have made provision to retain relevant documentation in support of such decisions for a period of time commensurate with the nature of that borrowing or investment.

Inspectorates

Care Quality Commission

Care Quality Commission (CQC), the independent regulator for health and social care in England, has launched a new programme of inspections across all of England's adult social care services, giving a rating according to whether they are safe, effective, caring, responsive and well led.

Ofsted

Ofsted (the Office for Standards in Education, Children's Services and Skills) is the regulator of services that care for children and young people. It inspects and produces reports on LAs with regard to their statutory duties in this area.

HM Inspectorate of Probation

HM Inspectorate of Probation inspects various institutions in the probation landscape, including youth offending services. Some of its reports are relevant to LAs with regard to their statutory duties in this area.

HM Inspectorate of Constabulary and Fire & Rescue Services

HM Inspectorate of Constabulary and Fire & Rescue Services (HMICFRS) independently assesses the effectiveness and efficiency of police forces and fire & rescue services in the public interest. Some of its reports are relevant to LAs with regard to their statutory duties in this area.

Sustainable resource deployment

Auditors may wish to consider the following topic areas in respect of sustainable resource deployment.

Pay and employment issues

The government has increased the statutory minimum pay level (National Living Wage) and employer's national insurance contributions (end of contracting-out on introduction of new State Pension) from April 2016. These changes are likely to affect the staffing costs of LAs and may have implications for medium term financial planning.

In November 2014, the Employment Appeals Tribunal (EAT) held that Article 7 of the Working Time Directive is to be interpreted such that payments for overtime are part of normal remuneration and to be included as such in the calculation of pay for holiday leave taken under regulation 13 of the Working Time Regulations 1998. This judgement has a bearing on organisations that offer significant overtime.

Rateable values

The Valuation Office Agency (VOA) has updated the rateable values of all business properties from 1 April 2017. This could lead to an increase in the number of appeals. This can lead to increased uncertainty about the level of business rate income at some local authorities, which could affect the medium term financial planning assumptions made by the local authority.

Brexit

The UK's planned departure from the European Union (EU) may impact on the medium-term and longer financial planning of bodies who receive significant EU funding. Further information on potential issues that could arise as the UK prepares to leave the EU can be found in *Supporting information: General arrangements*. A summary of the main types of EU funding that authorities may receive is contained in the LGA document titled '*Guide to EU funding for Councils*'.

Working with partners and other third parties

Accountability for services cannot be transferred to third parties, and the body's arrangements to monitor the performance and delivery of services and take action where standards fall need to be appropriate to the method of delivery.

Social housing

LAs that either directly own social housing, or have transferred their social housing to another provider, remain accountable for that housing. The Homes and Communities Agency, as the regulator of social housing, publishes regulatory judgements where provision has been found to be non-compliant. Regulatory judgements could be a helpful information source for auditors when undertaking their risk assessment.

Local Enterprise Partnerships

LAs work with private enterprise in their area to promote economic growth through Local Enterprise Partnerships (LEPs). There are now 38 LEPs in England and each one is responsible for managing one of the agreed Growth Deals. Each LEP has the flexibility to determine the details of its governance and accountability arrangements and there are a variety of models including those that have remained as partnerships, local authority Section 101 committees, community interest companies and companies limited by guarantee. Public funding for LEPs is directed via a local authority in the area of the LEP, which is appointed to undertake the accountable body role. The government also appoints Relationship Managers – regionally based civil servants who provide LEPs with day to day advice and support and are the main channel of engagement between the LEPs and central government.

LEPs are currently required to follow the LEP national assurance framework set by MHCLG which covers all government funding flowing through LEPs, to ensure they have robust value for money processes in place and sets out what government expects LEPs to cover in their local assurance frameworks. However, from 1 April 2019, LEPs will be required to follow the National Local Growth Assurance Framework (the Framework) which replaces the LEP national assurance framework. It sets out HM Government's guidance for places that are required to develop their own Local Assurance Framework. This applies to Mayoral Combined Authorities (MCAs) with a Single Pot and LEPs and seeks to provide a common framework of understanding of the assurance required for local growth funding. It recognises the close working in places and seeks to streamline processes whilst providing a framework to govern the appropriate use of public money.

All LEPs and MCAs are required to update their Local Assurance Framework(s) to reflect the requirements set out in the national framework. LEPs are required to have new Local Assurance Frameworks in place by 31 March 2019. In MCA areas and where the LEP and MCA are combining their Local Assurance Frameworks, unless otherwise specified or agreed by exception with MHCLG, these arrangements must be in place by the beginning of the 2019-20 financial year.

The Section 151 Officer (or Section 73 Officer for the GLA) of the accountable body must also sign-off the revised local assurance framework, and write to MHCLG's Accounting Officer by 28th February each year certifying that the local assurance framework has been agreed, is being implemented, and that it meets the standards set out in the current LEP National Assurance Framework and, going forward, the revised National Local Growth Assurance Framework. Local assurance frameworks must be published on each LEP's website, and reviewed annually.

MHCLG carried out a *'Review of Local Enterprise Partnership Governance and Transparency'*, the aim of the review was to look at the extent to which LEPs are fully implementing existing requirements of the national framework.

The arrangements in place between LAs and their strategic partners to manage and monitor local growth may be helpful in informing the auditor's risk assessment.

Better Care Fund

The Better Care Fund (BCF) came into being during 2015-16 and takes the form of a local, single pooled budget that aims to fund ways that the NHS and local government throughout England can work more closely together. It provides a mechanism for joint health and social care planning and commissioning, bringing together ring-fenced budgets from CCG allocations, the Disabled Facilities Grant (DFG) and funding paid directly to local government for adult social care services – the Improved Better Care Fund (IBCF).

The Spring Budget 2017 announced an additional £2 billion to support adult social care in England. This money is included in the IBCF grant to local authorities (LAs) and will be included in local BCF pooled funding and plans for the period 2017-18 to 2019-2020. An additional £240 million was announced in the Budget on 29th October 2018 for local authorities to spend on adult social care to help alleviate winter pressures on the NHS. This is also included in the IBCF grant.

The Department of Health, NHS England and MHCLG have published a document which sets out the detailed requirements for planning based on the *2017-2019 Integration and Better Care Fund (BCF) policy framework*. In developing BCF plans for 2017-19, local partners will be required to develop, and agree through the relevant Health and Wellbeing Board, and set out how they are going to achieve further integration by 2020. The framework encourages areas to align their approach to health and care integration with Sustainability and Transformation Plan geographies, where appropriate. The framework forms part of the NHS England Mandate for 2018-19.

The key changes to the policy framework since 2016-17 include:

- a requirement for plans to be developed for the two-year period 2017-2019, rather than a single year; and
- the number of national conditions which local areas will need to meet through the planning process in order to access the funding has been reduced from eight to four which now include: plans to be jointly agreed; NHS contribution to adult social care to be maintained in line with inflation; agreement to invest in NHS commissioned out-of-hospital

services, which may include 7 day services and adult social care; and managing transfers of care (a new condition to ensure people's care transfers smoothly between services and settings).

Beyond this, areas have flexibility in how the fund is spent over health, care and housing schemes or services, but need to agree how this spending will improve performance in the following four metrics:

- delayed transfers of care;
- non-elective admissions (general and acute);
- admissions to residential and care homes; and
- effectiveness of reablement.

All local partners will need to confirm mandatory – and any additional – funding contributions to all plans to which they are a partner. This will include confirming that individual elements of the funding have been used in accordance with their purpose as set out in the policy framework.

For LAs, the following special conditions must be met regarding the ICBF:

- The funding can only be used for the purposes of meeting adult social care needs; reducing pressures on the NHS, including supporting more people to be discharged from hospital when they are ready; and ensuring that the local social care provider market is supported.

- A recipient local authority must pool the grant funding into the local Better Care Fund, unless an area has written Ministerial exemption; work with the relevant Clinical Commissioning Group and providers to meet national condition four (Managing Transfers of Care) in the Integration and Better Care Fund Policy Framework and Planning Requirements 2017-19; and provide quarterly reports as required by the Secretary of State.

- MHCLG has also required local authorities to certify (via their Section 151 officer) that spending of the additional money provided at the 2017 Spring Budget will be additional to previous plans for adult social care spending.

Auditors may wish to consider the impact of BCF and IBCF plans and achievements in their VFM arrangements risk assessment.

Delayed transfer of Care (DTOC)

NHS Improvement has developed a tool to enable trusts, clinical commissioning groups and local authorities to understand where delayed transfers of care are in their area or system. The tool brings together data already submitted by NHS organisations and local authorities and indicates where their biggest delays are.

Auditors may find this data useful in understanding the most common reasons for delayed transfers of care and may wish to consider this as part of their VFM arrangements risk assessments.

Sustainability and Transformation Partnerships (STPs)

In December 2015, the NHS Shared Planning Guidance 2016-17 - 2020-21 outlined a new approach with the aim of further integrating health and care services. NHS bodies and local councils have formed partnerships in 44 areas covering all of England, with the aim of improving health and care. Each area has developed proposals, known as sustainability and transformation plans, built around the needs of the whole population in the area.

The footprints are locally defined, based on the nature of communities, existing working relationships and patient flows. They take account of the scale needed to deliver the services, transformation and public health programmes required, along with how they best fit with other footprints. The partnerships are not statutory bodies, and do not replace existing local bodies, or change local accountabilities.

Each sustainability and transformation partnership (STP) was required to produce and agree a sustainability and transformation plan. NHS England has published the plans for each area on its website.

In March 2017, NHS England published Next step on the five year forward view which reviews the progress made since the launch of the NHS five year forward view in October 2014. It also provides more detail on the priorities for the next two years. Chapter 6 provides further information on STPs.

In July 2017, NHS England released its first rankings of the 44 STPs across the country in its progress dashboard. This provides an initial baseline view of STPs' work and tracks the combined achievements of local services through 17 performance indicators across nine priority areas: emergency care; elective care; safety; general practice; mental health; cancer; prevention; finance and system leadership. Each area falls into three core themes of hospital performance, patient-focused change and transformation. This forms an overall assessment of each STP on a scale of 1 to 4: 'outstanding' (1); 'advanced' (2); 'making progress' (3); and 'needs most improvement' (4).

Five STPs have been rated as 'outstanding', and five rated as 'needs most improvement'. Another 20 are rated as 'advanced', with the remaining 14 'making progress'.

There are a number of aspects to STPs where weaknesses in arrangements may be relevant to the auditor's VFM arrangements risk assessment. These include:

- lack of clear and measurable outcomes;
- lack of capacity within organisations to implement the plans;
- lack of a clear accountability structure for delivery;

- potential conflicts between partnerships and the strategic plans of individual organisations; and
- insufficient funding to deliver transformational change.

Potential conflicts of interest arising from new models of care and changes in commissioning arrangements are included in *Annex K: Conflicts of Interest and New Models of Care* within NHS England's revised statutory guidance on conflicts of interest management.

Over time, some STPs will become integrated care systems, in which NHS providers and commissioners choose to take on collective responsibility for resources and population health, often in partnership with local authorities.

Integrated Care Systems

In March 2017, NHS England set out an ambition to create a system of integrated care which is now being pursued through the development of sustainability and transformation partnerships (STPs) – local 'place-based' partnerships of NHS and local authority organisations. The most advanced local partnerships have been asked to develop 'integrated care systems' (ICSs) which intend to take more control of funding and services across local areas.

Integrated care system leaders will gain greater freedoms to manage the operational and financial performance of services in their area. They will draw on the experience of the 50 'vanguard' sites, which have led the development of new care models across the country.

The following 14 areas are working towards integrated care systems:

1. South Yorkshire and Bassetlaw
2. Frimley Health and Care
3. Dorset
4. Bedfordshire, Luton and Milton Keynes
5. Nottinghamshire
6. Lancashire and South Cumbria
7. Berkshire West
8. Buckinghamshire
9. Greater Manchester (devolution deal)
10. Surrey Heartlands (devolution deal)
11. Gloucestershire
12. West Yorkshire and Harrogate
13. Suffolk and North East Essex
14. North Cumbria

The Kings Fund published its report *'A year of Integrated Care Systems- Reviewing the journey so far'* in September 2018 which sets out the landscape in which the ICS operate and the progress made so far.

Guarantees

LAs are entering into more numerous and varied joint arrangements, both as a result of the outsourcing of existing service delivery and their increasing commercial activity. In doing so, LAs may offer certain financial guarantees to newly established bodies, for example offering guarantees in respect of increased pension liabilities for staff transferred to a subsidiary under Transfer of Undertaking (Protection of Employment) (TUPE) arrangements.

In completing their VFM arrangements risk assessment, auditors may wish to consider the extent to which an authority issuing such guarantees has factored the impact of the guarantees crystallising into their financial planning, including any existing guarantees that may already be in place for existing arrangements.

Governance reporting

This section sets out the Annual Governance Statement reporting requirements for the audited body mapped against the description of proper arrangements. Auditors might find this useful when considering the "subject matter" as defined in AGN 03 in order to prepare their risk assessment.

Local bodies' own governance reporting provides helpful, although not necessarily comprehensive, information about the subject matter for auditors' work.

Existing requirements to support Annual Governance Statements are set out below. Note that some governance statement requirements could provide information relevant to more than one sub-criterion, and are included more than once. **Auditors should not consider these categorisations as prescriptive or exhaustive, or use the framework as a "checklist"**.

The extent to which the information contained in the governance statement will inform the auditor's risk assessment will depend on the auditor's knowledge of the audited body and the quality of the evidence supporting the body's governance statement.

	Local Government (CIPFA/SOLACE framework 2016)
Informed decision making	• Developing codes of conduct which define standards of behaviour for members and staff, and policies dealing with whistleblowing and conflicts of interest and that these codes and policies are communicated effectively. • Ensuring compliance with relevant laws and regulations, internal policies and procedures, and that expenditure is lawful. • Documenting a commitment to openness and acting in the public interest. • Establishing clear channels of communication with all sections of the community and other stakeholders, ensuring accountability and encouraging open consultation.

	• Developing and communicating a vision which specifies intended outcomes for citizens and service users and is used as a basis for planning. • Reviewing the effectiveness of the decision-making framework, including delegation arrangements, decision-making in partnerships, information provided to decision makers and robustness of data quality. • Measuring the performance of services and related projects and ensuring that they are delivered in accordance with defined outcomes and that they represent the best use of resources and value for money. • Defining and documenting the roles and responsibilities of members and management, with clear protocols for effective communication in respect of the authority and partnership arrangements. • Ensuring effective arrangements are in place for the discharge of the monitoring officer function. • Ensuring effective arrangements are in place for the discharge of the head of paid service function. • Reviewing the effectiveness of the framework for identifying and managing risks and for performance and demonstrating clear accountability. • Ensuring effective counter fraud and anti-corruption arrangements are developed and maintained in accordance with the Code of Practice on Managing the Risk of Fraud and Corruption (CIPFA, 2014). • Ensuring an effective scrutiny function is in place. • Ensuring that assurance arrangements conform with the governance requirements of the CIPFA Statement on the Role of the Head of Internal Audit (2010) and, where they do not, explain why and how they deliver the same impact. • Undertaking the core functions of an audit committee, as identified in Audit Committees: Practical Guidance for Local Authorities and Police (CIPFA, 2013). • Ensuring that the authority provides timely support, information and responses to external auditors and properly considers audit findings and recommendations.
Sustainable resource deployment	• Measuring the performance of services and related projects and ensuring that they are delivered in accordance with defined outcomes and that they represent the best use of resources and value for money. • Providing induction and identifying the development needs of members and senior officers in relation to their strategic roles, supported by appropriate training. • Undertaking the core functions of an audit committee, as identified in Audit Committees: Practical Guidance for Local Authorities and Police (CIPFA, 2013).
Working with partners and	• Developing and communicating a vision which specifies intended outcomes for citizens and service users and is used as a basis for planning.

other third parties	• Translating the vision into courses of action for the authority, its partnerships and collaborations. • Incorporating good governance arrangements in respect of partnerships and other joint working and ensuring that they are reflected across the authority's overall governance. • Defining and documenting the roles and responsibilities of members and management, with clear protocols for effective communication in respect of the authority and partnership arrangements. • Reviewing the effectiveness of the decision-making framework, including delegation arrangements, decision-making in partnerships, information provided to decision makers and robustness of data quality. • Establishing clear channels of communication with all sections of the community and other stakeholders, ensuring accountability and encouraging open consultation.

Sector resources

This section sets out some of the key stakeholders and their publications that auditors might find useful when preparing their risk assessment. Where a framework or guidance suggests "best practice" this will not necessarily map onto proper arrangements for VFM, where adequate practice may suffice. Auditors might wish to add value and make the audited body aware of "best practice" guidance they identify.

National Audit Office: The NAO scrutinises public spending for Parliament. It publishes various outputs relevant to the audited body's sector; in this case on local services. Reports that might be of particular interest to auditors of LAs include:

- Local authority governance (published January 2019)
- Local auditor reporting in England 2018 (published January 2019)
- Financial Sustainability of Local Authorities (published March 2018)
- A Short Guide to Local Authorities (published September 2017)
- Overview: Local Government (published November 2016)
- Departmental Overview 2015-16: Department for Communities and Local Government (published November 2016)
- Planning for 100% local retention of business rates (published March 2017)
- NAO work on transition grant and rural services delivery grant (published February 2017)
- Financial sustainability of local authorities: capital expenditure and resourcing (published June 2016)
- Progress in setting up combined authorities (published July 2017)
- English devolution deals (published April 2016)
- Devolving responsibilities to cities in England: Wave 1 City Deals (published July 2015)
- Local Public Service Reform (published September 2016)
- Local Enterprise Partnerships (published March 2016)

- Health and social care integration (published February 2017)
- Housing in England: overview (published January 2017)
  Local welfare provision (published January 2016)
- Cyber security and information risk guidance for Audit Committees (published September 2017)
- Investigation: WannaCry cyber-attack and the NHS (published October 2017)
- Local support for people with a learning disability (published March 2017)

Local Government Association (LGA) publications: The LGA regularly produces guidance and case studies that cover local government. For example, it maintains LG Inform, which is designed to provide up-to-date published data about a local area and the performance of LAs. Auditors may find these resources helpful to either identify risk factors or to use as a comparator to the arrangements in place at the audited body.

The LGA also provides details on current and upcoming devolution deals.

LG Inform Value for money profiles: The Local Government Association maintains profiles that bring together data about the costs, performance and activity of local authorities and fire and rescue authorities. Auditors may find these profiles helpful to identify risk factors from trends in input, output, and outcome data relevant to the audited body.

Other resources

Local auditors may also wish to consider the results from CIPFA's Resilience Index tool. The Beta Version of the Resilience Index tool was released to finance directors of English councils in December 2018. CIPFA's intention is for the tool to enable authorities to view their position (relative to other bodies) on a range of measures linked to financial risk. The current tool is a test version, with a final version being released later in 2019. Further details on the tool can be found at **CIPFA briefing – measured resilience in English authorities**.