THE SOCIETY OF DISTRICT
COUNCIL TREASURERS

STREAMLINING ACCOUNTS AND THE AUDIT PROCESS

A discussion paper containing 7 ‘asks’ to improve district council reporting and help streamline the accounts and audit process.

SEPTEMBER 2024

INTRODUCTION

1. Local Authority Accounting and Audit is at a crossroads. The accounts themselves are becoming increasingly long and impenetrable, whilst the local audit system is in freefall with legislation required to address the backlog of outstanding audits and effectively confirm that some years accounts for a large number of local authorities will never be audited.

2. Against this background there has been much discussion by all the key players in the system about how the future of local accounts and audit can be secured. This is by no means guaranteed with the latest procurement round only just securing the capacity required from the market and concerns that if nothing changes this cannot be guaranteed for the next procurement round. It is vital that Government, the National Audit Office, Financial Reporting Council and CIPFA/LASAAC continue to come together and find real lasting solutions.

3. The Society of District Council Treasurers has been engaging with this debate with responses to consultations, a survey of members and a successful debate at the CIPFA Conference. District Councils are especially hard hit by the backlog and this paper builds upon those discussions and sets out a series of suggestions for simplification of the accounts and improving the audit process. Its starts from the premise that the move to International Financial Reporting Standards based accounts is not up for debate, although we would question whether the additional burden IFRS based accounts place on smaller authorities is proportionate.

4. It would be wrong to ignore the value for money being achieved from the production and audit of accounts. Whilst accountability and external scrutiny is essential and should not be undermined our survey showed that the average uplift on the original PSAA scale fee was 96% equivalent to around 1% of authorities' net revenue expenditure. It is against this background that our suggestions are made focussing on those areas with significant cost, either external or internal, but that have little or no impact on decision making and accountability.

MATERIALITY

5. The average materiality level for authorities responding to our survey was 3.2% of net revenue expenditure. It is accepted that for those items of expenditure that directly impact on the general fund should be subject to detailed scrutiny. This reflects the use of council and non-domestic rates in the provision of services and is key to accountability to the taxpayer.

6. The issue, and a key contributor to the reason district councils are disproportionately impacted by audit delays, is that this materiality figure is then

applied to the balance sheet of local authorities. For district councils this results in a balance sheet materiality level of 0.7% of total assets. Given that valuation of property, plant and equipment can only ever be an estimate this brings a level of audit scrutiny to these figures that implies a false, and unachievable, accuracy.

7. There is some argument that auditors do have the ability to apply to differential materiality levels already, however lack of clarity of the regulators view of differential materiality, leads to a risk adverse approach being taken by auditors and a single materiality level applied.

Ask Number 1 That separate materiality levels are applied to the balance sheets of local authorities commensurate with total assets values. That this is supported by clarity within the system that this approach will not be challenged by regulators.

RELIANCE ON EXPERTS

8. Value for public money cannot be achieved by the result which is arguments between local authorities' external valuers and the valuation teams of auditors as to the basis of and professional assumptions underlying valuations. Whilst we acknowledge that there is value to understanding the value of assets tied up in service provision within the public sector, decisions about their use and investment are made on the basis of service delivery. In a similar way the information supplied by actuaries for Pension Fund entries are subject to detailed scrutiny by experts.

Ask Number 2 Where suitably qualified expert external valuations are obtained by local authorities, these can be relied on by auditors subject to normal review of the information supplied by local authorities to that valuer.

ADDITIONAL INFORMATION

9. The Government and CIPFA use the statement of accounts to provide additional information, such as that around pay, and to demonstrate compliance with other codes, such as the Annual Governance Statement. This approach harks back to a time when the accounts were physically published and before the rise in open access to information through councils' websites and legislation such as Freedom of Information.

10. We recognise that more can be done now accounts are published online rather than physically printed through the use of embedded links to information published elsewhere. However we feel that it would be helpful if CIPFA could

provide guidance on how this can be improved and there is clarity from regulators about the scope of audit of these linked items. In addition Government should review the legislative requirements for publication of information in accounts to ensure that these requirements are not duplicated, such in the publication of Pay Policies or in government returns, and that publication as part of the accounts remains the best way to achieve transparency.

11. As part of this work CIPFA/LASAAC may wish to review links between the accounts and other professional requirements such as the Annual Governance Statement or the links between financial instrument disclosures and Treasury Management annual reports to minimise disclosures and improve understanding by users of the accounts.

Ask Number 3 CIPFA and regulators provide guidance on how to reduce the length of accounts through reliance on information published elsewhere and the Government review the statutory disclosures within accounts.

PENSIONS

12. We recognise that at a national level, pensions accounting provides a useful measure of the liabilities and assets held within public sector pension funds. For individual local authorities however, it is the triennial actuarial valuation that determines the call on resources and impacts upon financial sustainability.

13. There is also a practical implication for district councils accounts preparation and audit in that this information is dependant upon upper tier authorities providing information and the audit of the pension fund as part of upper tier accounts. Any delay at the upper tier level has a knock on impact on district councils' accounts preparation compounding delay in the publication and audit of accounts. Audit costs are also increased as audit work overlaps with individual auditors reviewing pension disclosures for each of the individual authorities within a pension fund.

14. By separating pension fund accounts from individual local authority accounts, sensible information could be provided about the health of pension funds and their assets and liabilities. This would also be provided at a level aligned to decision making around investments and pensions strategies and allow individual local authorities to account as defined contribution schemes which would reflect the actual cost of pensions to them. Given that there are already defined benefit schemes that are deemed to be defined contribution schemes with the public sector there can be little argument against adopting such an

approach. Local authorities could be required to publish links to the Pension Fund accounts and actuarial valuation to improve accountability.

Ask Number 4 Government legislates to separate out the Pension Fund accounts and require local authorities to account on a defined contribution basis.

COLLECTION FUND

15. It is recognised that similar arguments could be applied to the Collection Fund and that this could be separated from the accounts of individual authorities. This again would remove delays in two tier areas and duplication of audit effort. Under legislation local authorities are required to apply taxation income based on the formal budget decision and initial estimates of income with in-year variations dealt with within the collection fund.

16. Consideration should be given to separating out collection fund accounting and the interaction of legislation and income recognition standards reviewed to determine if revenue recognition should align more closely to the statutory position. Publication of a separate collection fund account, alongside existing government returns, would give taxpayers the accountability required.

Ask Number 5 Government legislates to separate out the Collection Fund from individual authority accounts and require individual authorities account for tax income on a legislative basis.

NON-INVESTMENT ASSETS

17. CIPFA/LASAAC has consulted on mandating full valuation every 5 years with indexing of values in other years. Whilst this approach is supported, for the audit burden to be reduced it should be mandated along with the use of prescribed indices to minimise scope for audit challenge. There is a danger that such an approach, without prescribed indices, would move audit work from valuations to choice of indices. Any movement without allowing reliance to be placed on external expert valuers would be limited in impact.

18. Another key area of work on non-investment assets is review of impairment. Greater clarity should be given as to what constitutes impairment of non-investment assets under such a regime, with impairment only being required where it prevents the authority using assets for their intended service purpose.

Ask Number 6

Mandate full valuation every 5 years with prescribed indexes to be used to determine values in between. Impairment to be restricted to circumstances when the asset cannot be used for its intended service purpose.

EXPENDITURE AND FUNDING ANALYSIS

19. The Expenditure and Funding Analysis attempts to set out the adjustments between the IFRS statements and funding basis of local authorities, however, it has become overcomplicated and aurally fails in its intention so should be reviewed.

20. If changes are made to the pension and collection fund accounting in line with proposals then the adjustments within the Expenditure and Funding Analysis would be limited to the holiday accrual adjustments and those related to capital accounting. The holiday accrual adjustment could be removed as non-material if school staff were excluded, not a district issue, leaving the only adjustments relating to capital funding.

Ask Number 7

A review of the EFA is undertaken and consideration given to replacing the EFA with a much simplified Capital Funding Statement.

OTHER CONSIDERATIONS

21. A more fundamental approach alongside the asks in relation to the current system would be to separate out the IFRS accounts and a simple expenditure and funding statement aimed at the local taxpayer. CIPFA/LASAAC may wish to give consideration to standard format local authority IFRS based accounts along the lines of that produced by the NHS. This would allow easier and automatic consolidation at a national level and sit alongside the existing RA and RO forms. Local authorities could then focus on publication of information for taxpayers in line with the statement proposed by Tony Redmond as part of his review.