

AT/PSC

Future of Local Audit Team  
Department for Communities and Local Government

By email: [foia@communities.gsi.gov.uk](mailto:foia@communities.gsi.gov.uk)

24 July 2014

Dear Sir/ Madam,

### **Future of local audit consultation - ICAS response**

1. The Public Sector Committee of The Institute of Chartered Accountants of Scotland (ICAS) welcomes the opportunity to comment on this consultation. Our Public Sector Committee is a broad based committee of ICAS members with representation from across the public services and across the UK.
2. ICAS's Charter requires its committees to act primarily in the public interest, and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires us to represent our members' views and to protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.
3. Our comments focus on the Accounts and Audit Regulations.

### **Narrative Statement**

4. ICAS welcomes the proposal to introduce a Narrative Statement. We strongly believe that the introduction of a management commentary is necessary to support understanding and transparency of local authority accounts and enhance accountability. It is also a key tool to help drive a holistic approach to simplification of the accounts i.e. bolstering the explanatory front half of the accounts and simplifying the technical second half of accounts<sup>1</sup>.
5. We believe that greater consistency and comparability supports simplification, transparency and widens understanding of public sector reporting. To reduce unnecessary specialism for English local authorities and ensure key strategic issues are targeted, we suggest some changes are required for the draft regulations to align more closely with good practice across the UK and to maintain consistency across local authorities in devolved jurisdictions.
6. Firstly, we would remove the descriptive wording in the draft Regulations 7(1) setting out what the Narrative Statement should contain. This is inconsistent with the latest good practice recently introduced by the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2014 – "Strategic Report". The new Strategic Report focuses commentary on the strategy, business model and risks. Given the increasing use of group structures by some local authorities to deliver services, it is important that there is some explanation of the business model used and why it has been selected for example, does it offer efficiencies or deliver services more effectively, what are the risks/ financial exposure to parent local authorities and how does the parent maintain control and ensure their overall responsibility and quality standards are met?
7. We also suggest that it would be informative to include an explanation of deferred expenditure, such as PPP commitments, buildings and road repairs backlogs which can span many years. This could give the reader a clearer idea of the extent to which flexibility of future spend may already be constrained.

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<sup>1</sup> Further discussed here: [Future of local audit consultation on secondary legislation - ICAS response](#)

8. The Strategic Report is applied by central government as set out in the FREM and is the direction set by the Scottish Government for Scottish local authorities<sup>2</sup>. We support the approach taken by the Scottish Government which sets out a clear expectation in guidance (Finance Circular 7/2014) of what good practice is by aligning this with the central government FREM and to steer those responsible for setting the Code<sup>3</sup>. This is also well positioned to incorporate future good practice developments through the Companies Act. We believe the DCLG should also set a clear direction and expectation to ensure a consistent vision of good practice is followed and to set the bar.
9. To enhance consistency and understanding we would prefer a more universal term for the Narrative Statement. Our preference is "Management Commentary" which is used by central government, Scottish local authorities<sup>4</sup> and the IASB. This also suggests a more strategic focus.

### **Improving transparency**

10. Local authority accounts are specialist and complex which does not make it easy for a wider audience to understand. A major step forwards is the inclusion of a narrative statement/ management commentary. Another development which is needed to improve transparency would be to remove any specific jargon or unnecessary specialist terminology. We believe that it would be beneficial for the DCLG to take the lead in this matter. We suggest the DCLG communicates this expectation to local authorities and those setting the Code, to accelerate work to improve transparency of local authority accounts. This should start with a reduction of specialist terminology by encouraging more universally known terms and greater consistency. One example is that the role of a Finance Director may be known as Director of Corporate Services and Resources, the section 151 officer or responsible financial officer. The latter two terms are not known beyond local authorities. An example of how this is being driven is provided in sections 2-5 in the [Scottish Government Finance Circular no.7/2014](#).
11. We would also prefer the term 'statement of accounts' to be replaced with the more universal term 'financial statements' or 'annual accounts' as part of this exercise to review the Regulations and for this to be consistent across the UK.
12. Local authorities are increasingly using arm's-length organisations to deliver services which are reducing the entity level size and services but correspondingly increasing the number of entities in the group. This shift in approach means that it may be more difficult for citizens to get the same level of information as group bodies may follow different accounting frameworks and are subject to less scrutiny and regulation. We encourage Government efforts to improve accessibility and transparency of information.
13. We also suggest that given the growing significance of local authority groups, it is timely to undertake further work to assess whether current arrangements for group accounts disclosures are sufficient to meet the principles of public interest, transparency and accountability. Examples could be whether existing disclosures provide a clear picture of the extent of group activities and the level of risks this may expose a council to, such as any underlying financial guarantees/commitments. Why services are delivered through a group structure and the benefit to the taxpayer could form part of the business model (paragraph 6). It would also be helpful to identify areas where consistency and simplification could be improved. Any gaps could be incorporated within future revisions of the Accounts & Audit Regulations. The aim is to recognise the continued local authority responsibility for the stewardship of public funds and delivery of services regardless of the business model used.

### *Accountabilities*

14. We believe that the accountabilities of local authorities still need reviewed to align overarching responsibility and top-level accountability. We would prefer the Regulations to take a consistent approach. The council appears responsible for everything underpinning the

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<sup>2</sup> [Scottish Government Finance Circular no.7/2014](#)

[Local Authority Accounts \(Scotland\) Regulations 2014](#)

<sup>3</sup> Code of Practice on Local Authority Accounting in the UK

<sup>4</sup> [Local Authority Accounts \(Scotland\) Regulations 2014](#)

accounts but not the true & fair view. We would prefer the responsible financial officer to sign off the statements as the delegated authority and representative of the local authority (the relevant body) following approval by the relevant body. This would provide the opportunity for wider challenge at the highest level of authority in the organisation before sign-off and is an important control.

15. We trust that our comments are helpful and would be happy to discuss any aspect of our response with you.

Yours faithfully,

ALICE TELFER  
Assistant Director, Business Policy and Public Sector  
ICAS