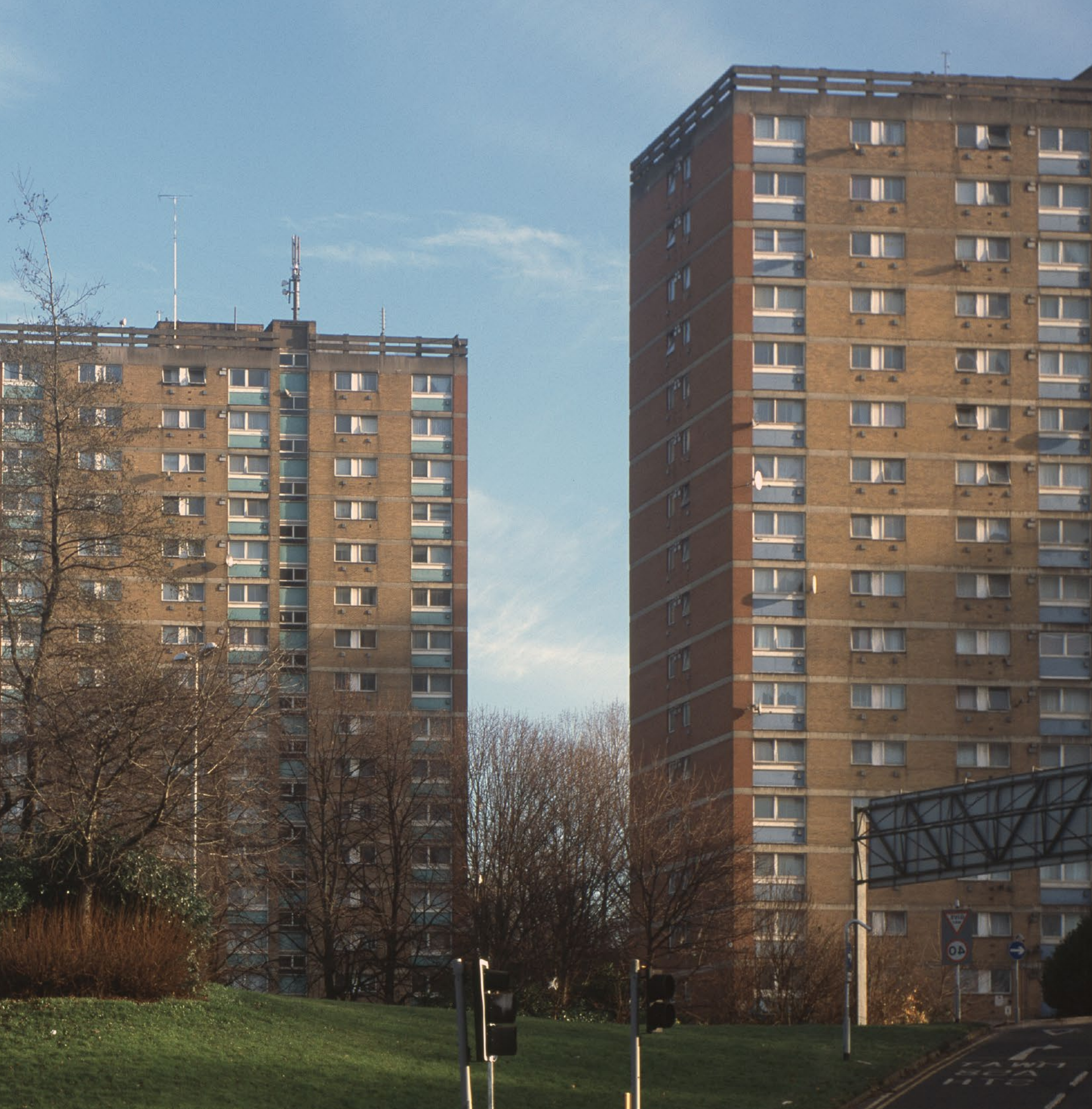

DEMOCRACY DENIED:
Audit and accountability failure in local government

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EXECUTIVE SUMMARY

This report presents evidence of citizen experiences of using the Local Audit and Accountability Act and Local Authority Accounts (Scotland) Regulations to scrutinise local government finances. It demonstrates serious accountability gaps, reveals the significant role played by private auditors in disempowering residents, and shows a concerning lack of accountability on the part of local authorities. The absence of robust external oversight, in the context of a deepening crisis in local government finance with deeply intertwined public and private sectors, undermines local democracy.

Residents have the right to scrutinise their councils' spending under the 2014 Local Audit and Accountability Act (LAA Act) and Local Authority Accounts (Scotland) Regulations (LAA[S]R). The legislation gives residents the right to inspect their council's accounts and any related documents, ask questions about these to the council's external auditor, and object to spending they believe is not in the public interest. In a 2017 addition to the legislation, the right to inspect council accounts was also extended to journalists, including citizen journalists and bloggers.

These rights should give residents the right to access information that would not otherwise have been available and to challenge local government spending they believe is not in the public interest or could be unlawful. When objecting, a resident can request for the auditor to issue a public interest report, which the council will have to discuss and publish, or to refer the issue to the high court to define its lawfulness.

The findings presented in this report demonstrate the public rights of the Act in their current form are not fit for purpose. We document 155 resident interactions with external auditors and local authorities. We have found that residents' requests to inspect the accounts are often obstructed by councils, which shows a striking lack of awareness of the legislation and – as it seems to those attempting to exercise their rights – often deliberate attempts to conceal information. This has a chilling effect on local democracy.

When residents object to council spending they would like the external auditor to scrutinise, they face further barriers. Auditors did not take any of the actions requested by the objectors, yet they charged councils significantly extra – often tens of thousands of pounds[1] – for sub-standard investigations.

Local government is increasingly financialised and privatised. Councils have become commercial actors whose main purpose, to provide services for residents, is getting lost in market logic as councils scramble to top up lost government grant revenue. This is clear in the way toxic private finance initiative (PFI) debts continue to be serviced for failing projects or where high interest payments on complex financial instruments are honoured, despite devastating cuts to frontline services.

The recent parliamentary Redmond Review into local government audit argued that greater public scrutiny and intervention by auditors should be expected "given the increasingly high profile of commercial and other new arrangements entered into by some local authorities".[2] Most of the uses of the LAA Act described in this report were in relation to PFI projects or bank loans called LOBOs (lender option, borrower option) sold to hundreds of councils. Both instruments are costing taxpayers millions of pounds extra in payments, and the objectors we spoke to ultimately wanted loan contracts to be declared as illegal and voided, and the control over PFI projects returned to the local authority.

Central government funding to local authorities has already been cut by half since 2010 – the reduction in funding in real terms between 2010/11 and 2017/18 was 49.1%, and the Covid-19 crisis has only intensified the plight of councils. Government support during the pandemic has averted a wave of council bankruptcies, but it has not resolved the underlying crisis and is not enough to keep councils afloat in the long term.

The LAA Act has also privatised local government audit itself. In 2015, the process to abolish the Audit Commission in England was complete and external audit of councils was handed to private companies, including some of the 'Big Four' accountancy firms, in particular KPMG and EY, along smaller players such as BDO, Mazars and Grant Thornton. The same companies dominate the world of corporate audit and consultancy, where several recent high-profile corporate bankruptcies and corruption scandals have put a spotlight on audit failure and conflicts of interest.[3]

Within the context of the rising risk of local authority bankruptcy, the increasingly blurred line between the public and the private sector raises questions about what audit failure means in the public sector and its impact on local services and value for taxpayers' money. When

1 Data on costs from responses to FOI requests submitted December 2020 to all English authorities where LOBO or PFI objections were lodged

2 Parliamentary review into the arrangements in place to support the transparency and quality of local authority financial reporting and external audit in England, September, 2019

3 Financial Times, 12 May 2020, 'KPMG faces £250m negligence lawsuit over Carillion'

residents' attempts to scrutinise spending are stonewalled, delayed and ultimately suppressed by audit firms, they are effectively prevented from holding elected representatives to account. These private companies have no definition for public interest, which enables them to sideline the public.

What is more, the experiences described in this report show that local government audit contributes to the deficit in oversight and failure to consider the public interest, not least because of the growing role of conflicted private audit firms which have frequently acted in both audit and consultancy roles for local authorities as well as for the banks and companies which councils have entered into contracts with.

The LAA Act enables corporations to act as unaccountable gatekeepers for residents' concerns. Objectors encountered a variety of obstructions when asking auditors to produce a public interest report or make a high court referral. These included the use of a clause in the legislation which prevents objectors publicly sharing the auditor's provisional decisions as well as a costly appeal process should they want to challenge the auditors decisions. There is no time limit for auditors to respond to objections, no oversight body, and no process to identify or manage conflicts of interest.

It was also evident from responses to objections that auditors did not meaningfully engage with or even fully understand the issues raised, as they failed to address key arguments and made incorrect claims about the financial arrangements of councils. Auditors frequently failed to respond to arguments made in the objections, responded to arguments that had not been made and dismissed expert evidence provided in the objections. Many decisions were based on evidence that was either lacking or extremely limited and often was not shared with the residents.

Despite the auditors' dismissal of the objections, behind closed doors many of the issues raised by objectors were acted upon by auditors in conjunction with local authorities and central government departments. Public accounting watchdog National Audit Office (NAO) urged local government auditors to pay attention to LOBO loans even if no objection was made at their council. This shows that the issues residents tried to highlight through the LAA Act were considered worthy of external intervention even when residents' role in the accountability process was otherwise dismissed.

The public interest needs to be clearly defined and upheld by councils and their auditors. Instead of leaving it to private, for-profit companies to define the public interest and how it is best served, local government residents who attempt to use their rights to hold their council to account must be supported, and the issues they raise should be afforded due importance.

This report identifies the failings of the current local audit and accountability system and sets out what should be done to improve it.

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1. INTRODUCTION & CONTEXT

Financialisation of local government

For the past three decades, local government finance has seen rapid changes. Increased use of outsourcing and complex financial instruments have complicated both decision-making and oversight of the use of public funds. Councils have become commercial actors in a financialised economy where they are encouraged to borrow from capital markets, hedge against risk, enter into public-private partnerships and make speculative commercial property investments. When things go wrong, this risk-taking jeopardises the delivery of basic services: interest payments are prioritised over service spending. Debts on inflexible long-term PFI deals must be serviced even when it becomes clear that public authorities are overpaying for poor quality or even non-existent services.[1]

Financial pressures have brought local government to breaking point. A decade of austerity and unprecedented cuts to funding have instigated a rolling programme of cuts to public services. Local authorities are legally obligated to balance their books and cannot run a deficit like central government or private companies, which leaves little room for shielding the public from funding cuts. At the same time grant funding has been slashed, demand for social services, a statutory obligation, has increased. The results are a human tragedy, visible in rising poverty, destitution and an acute housing crisis. These are amplified by deregulation, which has increased opportunities for profiteering by private companies and privatisation – including the creation of arms-length bodies – causing a systematic erosion in accountability. The most stark example of the risks arising from this context was the Grenfell Tower fire in 2017 and the loss of 72 lives which followed a deeply controversial refurbishment and the legitimate concerns of residents being routinely denied and dismissed.

The Covid-19 crisis has only intensified the pressures on local authorities. Although government support has averted a wave of council bankruptcies, it has not resolved the underlying crisis and does not make local government finances sustainable in the long term. In 2020, one council issued a Section 114 notice to warn it was not able to balance its books; at least seven asked for government bailouts to avoid insolvency; and at the end of the year 25 councils reported to the National Audit Office (NAO) survey that they were at acute or high risk of financial failure.[2]

1 Telegraph, 26 Jan 2011, 'PFI: £70m bill for schools that had to close'

2 NAO, 3 March 2021, 'Local government finance in the pandemic'

In this context of increasing need and slashed resources, a system of accountability and financial audit which prioritises public over commercial interests is needed more than ever. Decisions about how to allocate resources need to be accompanied by increased public involvement, scrutiny and debate. This is impossible without transparency on the part of local authorities and their external auditors, alongside processes and institutions to hold them to account when they fail.

Audit failure

There is growing recognition of the need for audit reform in the private sector. Audit failure has played a contributing role in several high-profile collapses of companies in the 2000s. From the recent bankruptcies of UK companies including Carillion and Thomas Cook, to Northern Rock as harbinger of the 2008 financial crisis and the 2001 collapse of energy company and commodity trader Enron, audit firms have come under sustained and intense criticism for their complicity in corporate excess and failure.

Patisserie Valerie's collapse into administration in January 2019 was one of the events that prompted scrutiny into the audit sector. The evidence presented by Grant Thornton's CEO to a Select Committee inquiry highlighted the deeply problematic role auditors played. He said about auditing the cake and café chain: "We're not looking for fraud, we're not looking at the future, we're not giving a statement that the accounts are correct…We are saying [the accounts are] reasonable, we are looking in the past and we are not set up to look for fraud."[3]

Such audit failures have prompted increasing parliamentary scrutiny and calls for audit reform. Major reviews including Kingman (2018) and Brydon (2019) focused on the inherent conflicts of interest and market dominance of the so-called Big Four audit companies (EY, KPMG, Deloitte, PwC). These issues are equally relevant for public sector audit, especially in England where, since 2015, local government audit has been outsourced to private audit firms.

The risks of failed audit to the public sector were realised when in 2018 Northamptonshire County Council became the first local authority in three decades to issue a Section 114 notice, warning it was not able to balance its books. Yet Northamptonshire's bankruptcy prompted no investigation into the council's auditor (KPMG) or any of the bodies

3 The Guardian, 30 Jan 2019, 'Ex-Patisserie Valerie auditor says 'not his role to uncover fraud''

involved in regulation and oversight of local government audit. This contrasts sharply with the investigations and reviews of Carillion, its auditor (KPMG) and regulators (the Financial Reporting Council), which swiftly followed the collapse of the outsourcing company only weeks earlier. In Northamptonshire, the council went on to suspend the 2019 local elections, with Conservative Minister for Local Government James Brokenshire arguing that proceeding with the elections "would involve significant costs that would be hard to justify".[4] There could not be a clearer illustration of the connection between financial risk-taking and democratic deficit.

This report contributes a unique perspective at a decisive moment for local government – one that evidences the risks of excluding the public and public interest from accountability processes and the need for audit reform. It gives voice to residents' concerns that have been marginalised at a time when councils are at breaking point and scrutiny is ever more necessary.

Changes to local government audit

Local government finance across the UK is subject to external audit and scrutiny through different arrangements in each nation. In Scotland, audits are undertaken by Audit Scotland's Audit Services Group or (in just over a third of cases) by private firms, and all audit appointments are made by the Accounts Commission. In Wales, audit is undertaken by the Welsh Audit Office and in Northern Ireland by the Northern Ireland Audit Office. In contrast to the situation in England, these institutions have remained public bodies. The findings of this report relate to use of the LAA Act in England and (LAA[S]R) Scotland only.

In England, there has been a huge transformation in local government audit since the onset of the austerity agenda. The public body responsible for audit, the Audit Commission, was shut down in 2015, having had its functions gradually reduced over the previous five years. The Audit Commission had been responsible for appointing auditors, setting audit fees and monitoring the standard of local government audit, regulating performance and providing indemnity to auditors (giving them more confidence to challenge local councils and risk potential legal challenge). It also had freedom and responsibility to spot and carry out investigations into issues of concern affecting multiple authorities.[5] Its abolition was carried out under the pretext of cost savings and an assumption that the public sector is inefficient and wasteful.

Organisations across different sectors advocated for the closure of the Audit Commission. Contributors to a Select Committee inquiry in 2011 including local authorities, regulatory bodies like the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Financial Reporting Council (FRC) and most significantly, several of the audit firms that now dominate local government audit in England: Deloitte, Mazars, BDO and Grant Thornton.[6]

The 2014 Local Audit and Accountability Act, which replaced the 1998 Audit Commission Act, has allowed private companies to act as councils' auditors and councils can now appoint their own auditors. The Audit Commission was by no means perfect, having been politically conceived as a means of constraining redistributive spending by Labour councils, and we do not argue for its wholesale reinstatement. However, there are some significant differences in the post-Audit Commission era, some of which are highly problematic, which we seek to highlight. One such difference with implications which are touched upon in this report has been the fragmentation of oversight functions in public audit. The abolition of the Audit Commission has seen its numerous oversight and regulatory functions fragmented across a range of bodies. Appointing auditors, setting audit fees and monitoring standards are now dealt with by Public Sector Audit Appointments (PSAA), the NAO and FRC along with Recognised Supervisory Bodies. The Commission's previous counter-fraud function is now covered by CIPFA and the Cabinet Office has taken over responsibility for national fraud initiatives.

No organisation has taken on the remit or responsibility for carrying out independent inquiries or investigations into issues of concern across multiple local authorities.

In 2019 a Parliamentary review (the Redmond Review) was undertaken into 'arrangements in place to support the transparency and quality of local authority financial reporting and external audit in England'. The review touched on the gaps in oversight produced by the fragmentation of responsibilities following the closure of the Audit Commission and has recommended the creation of a "new regulatory body responsible for procurement, contract management, regulation and oversight of local audit".[7] This has since been rejected by the government.[8]

The call for views as part of the Redmond Review rightly highlighted with concern the low use of public interest reports (or in fact any other actions available to the auditors), noting:

> *"Particularly at a time when local authorities are under acute financial pressure, and some local authorities are*

4 Statement to Parliament by James Brokenshire (Secretary of State for MHCLG), 29 Nov 2018, HCWS1124

5 Institute for Government, March 2014, 'Dying to Improve'

6 K. Tonkiss and C.Skelcher, 2015, 'Abolishing the Audit Commission'

7 Sir Tony Redmond, September 2020, 'Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting'

8 Local Government Chronicle, 17 Dec 2020, 'Jenrick rejects Redmond's call for single national audit body'

engaging in risky speculative ventures, high-quality and robust scrutiny of local authorities' finances and financial management in the public interest is a critical part of local democracy. The Review is very concerned that the quality of this scrutiny is being pared back at the worst possible time."

The scope of the review was encouraging and included questions on whether auditors were "...properly responding to questions or objections by local taxpayers?" and "... does the inspection and objection regime allow local residents to hold their council to account in an effective manner?" However, the final report of the review, published in September 2020, failed to address any of these issues; made no mention of either public inspection or objection rights[9] and did not seriously engage with citizens experiences of rights to challenge and object.

We are not the first to raise concerns regarding significant changes in local government and their impacts on accountability. Transparency International warned in their 2013 report "Corruption in UK Local Government: The Mounting Risks" that government reforms including the Localism Act[10] and Local Audit and Accountability Act were creating "an enabling environment for corruption."[11]

Several regulatory bodies have recently sounded the alarm about the state of local government audit. Fewer than half of audits in local government had been completed on time for the financial year 2019/20. The NAO warned in March 2021[12] that delays in audit opinions and recommendations "can mean that actions to improve financial efficiency and resilience are also delayed, and risks those actions being less effective" and noted that the Covid-19 pandemic has "exacerbated long-standing problems in the audit landscape."

The PSAA, who are responsible for audit standards, also said there were "serious and pervasive problems" facing local audit and Rob Whiteman, chief executive of CIPFA said the delays found by the NAO were "further evidence of the incredibly fragile and challenging state of the local audit market" which "requires a system-wide solution for both auditors and audited bodies."[13]

Austerity and lack of scrutiny

Councils' internal audit and counter fraud departments have also been significantly weakened by government

Government reforms including the Localism Act and Local Audit and Accountability Act were creating "an enabling environment for corruption."

cuts, with changes in governance increasing the likelihood of significant issues remaining undetected.[14] Unlike cuts to frontline service budgets, cuts to financial scrutiny and governance processes often go unnoticed, unless or until mismanagement of public funds and corporate profiteering emerges.

The lack of effective internal and external audit oversight in local government is compounded by a wider democratic deficit. The UK is one of the most centralised countries in the world and has the highest population size per local authority in Europe. Turnout in local elections is low and the electoral system makes it hard for small parties to break through. In many councils there is no effective opposition, further weakening accountability.[15] Power has been increasingly concentrated through changes over the past two decades to governance structures that have handed decision-making powers to a cabinet with a leader or a directly elected mayor, marginalising backbench councillors.

In addition, local journalism has undergone unprecedented cuts over the past two decades with a significant reduction in regional news titles. Despite the recent emergence of various initiatives to fill the democratic deficit, including independent community presses and local democracy reporters,[16] this amounts to a worrying reduction in the civic scrutiny of local government.

It is often being left to local citizens to not only do the scrutinising and investigations but also to publish the findings and raise the alarm.[17] A powerful yet contradictory narrative accompanying austerity was that of the 'Big Society': an argument that downsizing the state was both necessary and desirable and would encourage citizens taking a more active role in providing services usually seen as the state's responsibility.

9 Objection rights were mentioned in relation to 'smaller authorities' which include Parish Councils and which are not the subject of this report.

10 Localism Act 2011 furthered the centralisation of power from local government to central government

11 Transparency International, October 2013, 'Corruption in UK Local Government: The Mounting Risks'

12 NAO, 16 March 2021, 'Timeliness of local auditor reporting on local government in England, 2020'

13 Local Government Chronicle, 16 March 2021, 'Half of local audits late as NAO calls for reform'

14 Local Authority Investigation Officers Group found a 15% reduction in the number of fraud managers.

15 Electoral Reform Society, 2 October 2015, 'Revealed: the cost of one-party councils'

16 In 2017, the BBC launched a Local Democracy Reporters programme as part of a partnership with local news organisations.

17 Lambeth People's Audit, 2017 onwards

Current audit arrangements are making citizen scrutiny increasingly difficult, with the recent changes in the legislation effectively enabling private companies to act as gatekeepers to public interest concerns.

When he announced the closure of the Audit Commission in 2010, the Communities Secretary Eric Pickles said he expected "an army of armchair auditors, who will be able to see at a glance exactly where millions of pounds... went" and through this level of scrutiny "hold Ministers to account for how taxpayers' money is being spent".[18]

But as our report will evidence, current audit arrangements are making this form of citizen scrutiny increasingly difficult, with the recent changes in the legislation effectively enabling private companies to act as gatekeepers to public interest concerns.

The work behind this report

Research for Action's previous report focused on the impact of cuts in services and the democratic deficit in Newham and argued that complex bank loans called LOBO loans taken out by councils were illegitimate.[19] This citizen audit of local authority debt has built on initial work by Move Your Money and Debt Resistance UK (DRUK). As part of the audit DRUK and RfA have supported over 50 residents across England and Scotland to exercise their rights under the LAA Act and LAA[S] regulations over three financial years. This report evidences those experiences.

This report was written in collaboration with Megan Waugh and includes work that stems from her ongoing PhD research project 'Public Accountability and the Outsourcing of Public Services', in the School of Geography, University of Leeds. Some of this work has already been published in the journal Parliamentary Affairs: Waugh, M and Hodkinson, S. (2020) 'Examining the Effectiveness of Current Information Laws and Implementation Practices for Accountability of Outsourced Public Services'; other data used here, also part of this PhD, will be published in a peer-reviewed journal in due course.

In addition to the issue-specific audits of PFI and LOBO loans, this report contains experiences of Lambeth People's Audit, a place-based group of residents who have been scrutinising the expenditure of their local authority since 2016.

We have also drawn on responses to a questionnaire from outside our networks. This included experiences of those involved with Bureau Local, a network of local journalists coordinated by the Bureau of Investigative Journalism, who made extensive use of the inspection rights under the LAA Act in 2019.[20]

In total, this report focuses on 155 separate citizen engagements with the LAA Act. These include 72 inspection requests and 83 objections submitted over three financial years and across 46 different local authorities in England and Scotland. Despite the different focus of each citizen audit and different motivations of individual objectors, this report brings these experiences together in an effort to collectively understand and test the accountability mechanism.

The findings of this report draw on the experiences of the authors as well as in-depth interviews with LOBO and PFI objectors and members of Lambeth People's Audit. We conducted a data analysis of the LOBO and PFI objections as well as a comparison of the auditors' final responses, where objectors shared these with us. In addition, we made Freedom of Information requests to councils and central government bodies to gain a more comprehensive picture of how many councils received and responded to objections and inspections.

Structure

The report is structured as follows: this first chapter has provided an overview of the history and context of local government audit, setting out our understanding of the current crisis of audit and accountability in local government. In chapters 2 and 3 we set out our experiences and findings in relation to objection and inspection rights respectively. The concluding chapter 4 draws together the implications of discouraging citizen scrutiny, and the final chapter 5 makes recommendations for changes to legislation and its implementation as well as changes to regulation in order to better serve residents and the public interest.

Before moving onto the details of the legislation and our findings, the following pages set out the background to PFI and LOBO loans and their implications to the public purse and public safety. The resident objections and inspections covered in this report came about as a result of concerns about these issues and the lack of public accountability concerning them.

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18 MHCLG, 12 Aug 2010, 'Eric Pickles 'shows us the money''

19 Research for Action, October 2018, 'Debt & Democracy in Newham: A citizen audit of LOBO loans'

20 Bureau of Investigative Journalism, 11 Sep 2019 'Councils Ignoring Public Right to Audit Accounts'

LOBO LOANS

Lender Option Borrower Option (LOBO) loans are long-term bank loans that were sold to at least 240 local authorities across the country between mid-1980s and 2010. Usually starting with a low initial 'teaser rate', the loans give the lender (bank) the option to change the interest rate on pre-agreed dates. The borrower (council) can then choose to accept the new rate or pay the loan back in full. This is the only way the council can exit the loan without paying a large exit penalty. Effectively, it means that authorities are locked into the contracts for their duration, up to 70 years. The loans also contain complex financial arrangements known as embedded derivatives, which makes them inherently risky – a lose-lose bet for councils. Ex-trader Rob Carver, who gave evidence in a Parliamentary inquiry into the loans in 2015, said he "would not do these deals if you put a gun to my head".[21]

This same parliamentary inquiry came about after an investigation by Debt Resistance UK featured in a Channel 4 Dispatches documentary in July 2015, (How Councils Blow Your Millions) however the inquiry was dropped without any regulatory action being taken. Research for Action has been building on the campaign by Debt Resistance UK, which included supporting residents to object to their councils' LOBO loans, since 2017.

Research for Action's previous report focused on the biggest LOBO borrower in the UK, the Olympics host borough Newham in East London. We analysed the council's loans and conducted research into the devastating impact of funding cuts at the authority, arguing Newham's LOBO debt was illegitimate. Newham has since renegotiated the LOBO loans it had with NatWest (Royal Bank of Scotland) and according to the council, this saves £3.5 million a year in interest, totalling £143 million over the lifetime of the loans.[22]

Newham's annual saving of £3.5 million illustrates the importance of tackling the scandal of illegitimate debt. One of the UK's most deprived areas where over half of children grow up in poverty[23], Newham has been devastated by funding cuts. Our interviewees in 2018 described "a state of collapse" where "everything is just bursting at the seams".

"[I] would not do these deals if you put a gun to my head."

We spoke to parents raising children in substandard accommodation intended as temporary, public sector workers who had lost their jobs, disabled people whose care needs were not met. We heard of an epidemic in violence after an 80% cut in youth service budgets had left young people in the streets. Since our research, the council has U-turned on their priorities by challenging toxic LOBO loans and channelling money into improving residents' lives. In 2020, Newham announced it was investing an extra £4.5 million a year in youth services.[24]

21 Communities and Local Government Committee, 20 Jul 2015, 'Oral evidence: Local Councils and Lender Option, Borrower Option loans' HC 353

22 Newham Council, 3 May 2019, 'Newham Council to save £143m after terminating Lender Option Borrower Option (LOBO) loans with bank'

23 Trust for London, 2020, London's Poverty Profile

24 Newham Council, 12 Feb 2020, 'Newham bucks the trend and invests millions in youth services'

PRIVATE FINANCE INITIATIVE

Private Finance Initiative (PFI) schemes have been described as 'outsourcing on steroids'.[25] They have taken the public private partnership model of outsourcing to new extremes and make the private sector responsible for the construction and management of large swatches of public infrastructure. There are more than 700 PFI schemes currently in operation across the UK with a combined capital value of £59bn. The schemes cover thousands of public buildings, more than half of which are hospitals and schools, and payments over the life of the contracts worth at least £309bn. PFI contracts involve handing over the whole process of financing, building, managing and maintaining public buildings and related services to a private company or special purpose vehicle (SPV) which represents the interests of developers, investors and banks. Rather than the government directly borrowing money to pay for construction, this is also contracted out to the SPV which raises the finance through commercial borrowing. The SPV then receives monthly payments from the public sector, which currently cost the public sector £10bn a year.

One of the central public interest justifications for the rapidly expanding PFI programme was that the contractors were incentivised through a mechanism in the contract which links payments to performance. However, rather than the public authority monitoring and penalising the contractor where they have not been compliant with the contract, the SPV is effectively paid to self-monitor and sign off its own compliance. This system of self-certification has been linked to a growing evidence base of performance and structural failings in PFI projects. Research on social housing regeneration in Lambeth[26] exposed evidence of poor and even dangerous delivery standards which differed starkly from official reports on performance by PFI contractors and. Several PFI hospitals, which were the subject of a BBC investigation,[27] were found to have significant fire safety defects in buildings. These had been hidden for years and were only exposed when NHS Trusts tried to claw back millions of pounds in performance related deductions from the PFI company.

Rather than the public authority monitoring and penalising the contractor where they have not been compliant with the contract, the SPV is effectively paid to self-monitor and sign off its own compliance.

In 2016, the risks to the public were further exposed when nine tonnes of masonry from an external wall of a PFI-built primary school in Edinburgh collapsed, triggering investigations which went on to reveal more than 80 PFI schools in Scotland having similar structural problems, as well as widespread fire safety defects. The subsequent independent inquiry[28] found that the collapse was due to poor construction, inadequate supervision, poor record keeping by both the council and the PFI company and insufficient quality assurance from both parties as well as the construction industry. It also highlighted specific weaknesses within the self-monitoring system which has characterised PFI projects. In addition to safety concerns, the Edinburgh schools PFI cost £104m more than it would have cost using public finance.[29]

In 2017, People vs PFI, a grassroots group of patients, students, public sector workers and residents, worked with University of Leeds PhD researcher Megan Waugh and undertook a safety audit of PFI buildings.[30] The audit raised questions about public safety and challenged payments to the private sector, building on previous research work by Waugh that investigated the contract performance and monitoring of PFI housing projects across the UK and exposed the hidden costs of inflexible PFI contracts in Scottish schools.[31]

25 Hodkinson, S., 2019, 'Safe as Houses: Private greed, political negligence and housing policy after Grenfell'

26 Hodkinson, S. Essen, C. 2015. 'Grounding accumulation by dispossession in everyday life: The unjust geographies of urban regeneration under the Private Finance Initiative'

27 BBC Radio 4, 10 July 2016, 'File on Four: The Price of PFI'

28 Prof John Cole, 9 Feb 2017, 'Report of the Independent Inquiry into the Construction of Edinburgh Schools'

29 Edinburgh News, 17 April 2016, 'Flawed schools cost capital £100m too much, says PFI expert'

30 People's Safety Audit of PFI, 7 Jul 2017 'How Do We Know Our Public Buildings are Safe?'

31 TES Scotland, 26 May 2017, 'Private Finance Legacy Frustrates Efforts to Reform Scottish Curriculum'

2. FINDINGS: OBJECTIONS TO COUNCIL ACCOUNTS

2.1 Introduction

This chapter looks at residents' experiences of interactions with auditors. Most of the findings covered here relate to objections, however we also cover questions to the auditor briefly. In both cases, findings relate to the auditors' interpretation and implementation of the current legislation The following chapter looks at experiences of inspecting the accounts, where the focus is on the local authority and their role in responding to the public and interpreting a different aspect of the same legislation.

Auditors are obliged to respond to questions if they relate to the accounts of the year in question. The legislation gives residents the right to submit an objection to an item in a council's accounts:

> *27 (1) This section applies if...a local government elector for an area to which the accounts relate makes an objection to the local auditor which meets the requirements in subsection (2) and which—*
>
> *(a)concerns a matter in respect of which the auditor could make a public interest report,*
> *or*
> *(b) concerns a matter in respect of which the auditor could apply for a declaration under section 28.*

The requirements in subsection (2) are that the objection is made in writing and a copy of the objection is sent to the authority in question. The declaration mentioned in 1(b) is a court declaration that an item in the accounts is unlawful. This would usually be the high court, but county courts also have the powers to act under the legislation. If a court makes the declaration, it "may also order rectification of the statement of accounts or accounting records."

If the auditor issues a public interest report, they must send it to the local authority. They must also send the report to the Secretary of State.

The legislation states:

> *4 (2) As soon as is practicable after receiving the report, the relevant authority must publish the report and a notice that—*
>
> *(a) identifies the subject matter of the report, and*
> *(b) unless the authority is a health service body, states that any member of the public may inspect the report and make a copy of it or any part of it between the times and at the place or places specified in the notice.*

The auditor can also take both of the above actions without being prompted by an objection and they can also issue written recommendations to the local authority.

The Audit Commission Act 1998 that preceded the LAA Act enabled objections to be made on the basis of unlawfulness (S.17) but also for recovering an amount not accounted for (S.18). The legislation enabled the auditor to order the person liable for authorising unlawful expenditure to repay it to the authority and, if the sum exceeded £2,000, "order him to be disqualified for being a member of a local authority for a specified period". There are no such provisions in the LAA Act.

Despite their powers under the current legislation, auditors did not issue any public interest reports nor any court declarations in any one of the 83 cases covered in this report. Where auditors did respond, the majority (56%) took more than a year to do so. It was common to issue a provisional view before producing a final decision (titled the Decision and Statement of Reasons). The provisional view provides an overview of the investigation undertaken by the auditor, which in some cases might involve additional evidence, as well as a first formulation of their decision on the issue raised. The resident was then given 21 days to respond to this new information, and if needed provide additional evidence, before the auditor issues a final decision. At the time of the objections being submitted, there was no guidance on the maximum timescales for issuing either a provisional view or a decision.

The findings in this section are based on 83 objections submitted over three financial years and across 46 local authorities in both Scotland and England. All of the decisions we refer to and quote from relate to objections lodged in England and therefore dealt with by private audit firms and all references to the legislation are to the LAA Act. Members of Lambeth People's Audit also regularly exercised their right to question the auditor about any item in the accounts and did so separately from the objection process. Questions directed at the auditors about PFI contracts and LOBO loans were submitted along with the objections.

Based on these experiences, we detail the overwhelming lack of response to residents' questions and objections and the troubling poor quality of responses that were received. We also show how auditors obstruct residents' use of the rights. The conduct of auditors and authorities, allowed by the legislation, is effectively hindering the ability of the

public to scrutinise the spending and decision-making of their local authority. This constitutes a significant failure for accountability legislation that in principle should further democracy but which, in its current form, does the opposite.

2.2 Public Scrutiny and Private Concern

The recent Redmond Review into Public Audit noted that the fact public interest reports are not being issued by auditors "… is surprising given the increasingly high profile of commercial and other new arrangements entered into by some local authorities." [1]

The PFI and LOBO loans residents objected to were precisely the type of commercial arrangements Redmond was referring to. It is therefore concerning that auditors refused to accept any public interest argument for investigating the issues raised and neither issued a public interest report nor subjected the arrangements to scrutiny by referring them to the high court. In fact, the very concept of public interest remains undefined in the legislation.

Auditors refused to engage with the objections through the legal avenues created by the LAA Act and failed to publish either public interest reports or the findings of investigations, denying the public the right to scrutinise both the council's decision and the auditors work. Instead as one objector put it, auditors gave the opposite message that they should "move on, nothing to see here". This stonewalling, coupled with restrictions on sharing information and a lack of an external appeal process, meant residents were left to act alone.

However, a series of FOI requests[2] have revealed that the obvious inaction was not because the auditors did not consider the issues raised to be in the public interest or worthy of investigation: behind the scenes, auditors were calling on councils and central government to take extreme measures to mitigate and resolve these cases, despite arguing in correspondence with objectors they were unworthy of a public interest report.

In contrast to what little outside assistance residents were permitted, auditors were regularly consulting each other in private forums and receiving technical support from the NAO and CIPFA behind closed doors. While the auditors were refusing to engage with or even acknowledge the objectors' concerns, they were taking action elsewhere by delaying signing off councils' accounts[3] and lobbying for

The conduct of auditors and authorities, allowed by the legislation, is effectively hindering the ability of the public to scrutinise the spending and decision-making of their local authority.

direct intervention from central government to prevent a run of council insolvencies. Similarly, councils were initiating legal cases against PFI companies and banks that had sold them LOBOs, while refusing to acknowledge the issues raised by citizen objectors with the auditors or to pass on required information in a timely fashion. It seems that auditors, councils and regulatory bodies alike would rather deliberations over the issues raised by objectors took place outside the democratic processes of the councils, where the flow of information can be more readily controlled.

Auditors did not act on resident concerns

There is no appeal process when the auditor refuses to issue a public interest report. When an auditor refuses to apply to the high court for declaration of unlawfulness, the objector can appeal. However, they must do so within a very short timeframe (21 days) and must bear the costs of the court case, which could run to tens of thousands of pounds.

When refusing to act on the objections, the justification given by the auditor to residents in most cases was that the matter raised was not an issue of significant concern. However, in several cases the auditor admitted there were questions on the lawfulness of the items which had been challenged in the objection. In these cases the auditor made the Catch 22 argument that only a court could decide if the item of the objection was unlawful, whilst simultaneously refusing to refer the matter to court for a decision.

One auditor stated:

> *"If an item of account appears to us to be contrary to law, it is at our discretion as to whether we apply to the Courts for a declaration under Section 28 of the 2014 Act to that effect. It should be noted that this discretion only arises insofar as we are clear that there is an item of account which is contrary to law – where there is doubt this discretion does not arise. It is not the role of the auditor to seek the clarification of the Court where there is legal doubt"*
> (Grant Thornton)

Moreover, auditors hid behind a limited interpretation of the law, claiming that courts should not interfere with a council's decisions. Grant Thornton even claimed that one of the relevant factors taken into account when deciding whether to

1 Sir Tony Redmond, September 2020, 'Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting'

2 FOIs submitted by Shepway Vox Team, September 2018

3 Public Sector executive, 24 Aug 2018, 'Lancashire County Council accounts to be signed off after contentious LOBO-loan holdup'

apply to the court was whether the local authority, the subject of scrutiny, agreed with the auditor's view on the lawfulness of the items in question. This highlights how auditors can effectively act as gatekeepers to further legal and public scrutiny, leaving a vacuum where there is no one left to scrutinise decisions.

When an auditor decides to not publish a public interest report or apply for a court declaration, their entire investigation remains concealed from the public. In some cases it is not even shared with the council, as pointed out in the Parliamentary review on audit in England.

Auditors compare notes behind the scenes

Residents were warned that sharing the provisional views and other documents obtained by the auditor with anyone other than their legal representative was against the law. In the case of LOBO loans and PFI, objectors had been supported by campaign groups and financial experts they relied on, rather than individual legal representatives, so as a result, they felt they had no one to turn to for advice or support in responding to the auditor.

An FOI request to the NAO found that between 2016 and 2018, LOBO loans and other issues raised in objections were continuously discussed in private via emails and in specially convened practice groups by auditors, regulators CIPFA and Ministry of Housing, Communities and Local Government (MHCLG) officials. A panel (called the 'Local Authority Accounting Panel') discussed how to respond to objections and the significant budget implications of specific loans.

Emails disclosed demonstrated how auditors were fully aware that derivatives in LOBO loans, which they claimed in response letters did not exist, could in fact bankrupt up to a dozen councils. Privately, they acknowledged the role objectors had played in drawing attention to the problem, as one NAO email pointed out:

> *"Public accountability – could be seen as enhanced...the objection process has unearthed a significant issue...it also highlighted a collective blind spot in how the Code was read/interpreted."* [4]

Ironically, while being fully aware that all related objections were being routinely dismissed, the NAO urged all auditors to "to consider whether it would be appropriate to exercise any of their additional public reporting powers, such as issuing a recommendation...or a Public Interest Report." [5] Furthermore, they repeatedly advised that while objections had only been received in some local authorities, the issues raised should be considered "at other authorities where LOBOs are material" because there is a "risk of issues relevant to auditor's responsibilities not being considered adequately, if consideration is only given to bodies where objections have been raised."

So while objectors were being actively and effectively silenced, their arguments were being regularly referenced, something they only uncovered by resorting to FOI requests.

Intervention prompted by objections

The objections not only prompted a series of behind-closed-doors discussions, they also raised an issue that ultimately necessitated central government intervention to prevent councils declaring bankruptcy as a direct result of LOBO loans.

One of the central issues raised by LOBO loans objectors was that the full cost and financial risk associated with the loans was not being appropriately accounted for by the councils. Authorities had not been required to consider the full costs related to LOBO loans upfront and instead they could spread the costs over the 60-70 year lifetime of the loans. The same was true with PFI contracts. This failure to properly consider the long-term risks of LOBO loans and of PFI contracts was exacerbated when new international financial reporting standards[6] were introduced which forced councils to record the cost of derivatives in a much more transparent way and set aside cash reserves against the hidden liabilities.

Grant Thornton, who repeatedly dismissed objectors who questioned the failure of councils to consider the long-term risks of LOBO loans, were simultaneously refusing to sign off the councils' accounts until they received further guidance on how some of the most toxic LOBO loans should be correctly accounted for. Emails disclosed via FOI showed that LOBO objections were an important factor in prompting action to avert what was described in one meeting by a civil servant as a "nightmare scenario of material options, that would wipe out a council's reserves." [7]

The same batch of FOI documents show that information was being gathered to inform a major government intervention on this issue in the form of "a potential statutory override". A statutory override is a central government decision to waive or override regulation, in this instance to mitigate the impacts of following new reporting standards and related accounting practices.

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4 Summary of LOBO discussion in LAAP meeting 17th July 2018: disclosed in response to Shepway Vox Team FOI, 2018

5 Local Government Technical Issues Log, 19th Jan 2017: disclosed in response to Shepway Vox Team FOI, 2018

6 IFRS 9 which relates to the accounting treatment of financial instruments (including LOBO loans and PFI) came into effect in 2018.

7 Summary of LOBO discussion in LAAP meeting 17th July 2018: disclosed in response to Shepway Vox Team FOI, 2018

The LAA Act allows auditors to sideline residents who are trying to use rights that could, under different circumstances, have the potential to enhance public scrutiny and participation.

In the case of LOBO loans, the statutory override was introduced by MHCLG towards the end of 2018, and allowed councils to ignore the new financial reporting standards for the following five years. Within two years of the override, all of the most risky LOBO loans (inverse floaters) were cancelled by the lending bank – publicly owned Royal Bank of Scotland – at significant cost to councils and taxpayers.

Councils resort to court over issues raised in objections

In the meantime, eight councils had initiated legal actions against a bank, Barclays, that had sold them the loans.[8] This included a joint action by seven authorities, including four where objections were raised by residents. Newham Council took action alone.[9] At the time of writing, these cases were not resolved. These cases relate to charges that the interest rates of LOBO loans sold to councils by Barclays were rigged, an issue raised repeatedly by objectors but routinely dismissed by auditors.

In relation to PFI, in the London Borough of Camden, where objectors raised safety concerns over Grenfell-style cladding on the PFI Chalcots Housing estate, it took more than three years to receive a response to an objection lodged in 2017 (and no action was taken), and no response was provided to FOI[10] or LAA Act requests (also submitted in 2017) for related information. Yet Camden Borough Council has now taken the same housing PFI back in-house[11] and has subsequently initiated high court action against the very PFI companies whose contracts and governance arrangements were the focus of both inspection requests and objections.[12]

Auditors' potential conflict of interest

PFI objectors raised questions about the ability of auditors to act impartially when being asked to investigate issues relating to contracts where they were involved as consultants. This happens with consultancy work for the council, the private sector or both. In some cases companies acted as consultants for both the council and private sector at the same time.[13]

These questions were routinely ignored or dismissed – except in the case of Hackney Borough Council, where 20 months after the objection was submitted, the auditor KPMG admitted that they had been "...one of the advisors [to Hackney Council] at the time the Hackney LTI PFI was entered into in 2000." As a result, Mazars were eventually appointed to consider the objection.

Despite a parliamentary inquiry into Carillion's collapse, which exposed KPMG's lack of due diligence and professional scepticism on the auditing of PFI contracts,[14] and a failure of Hackney Council to provide any evidence or assurances on their own due diligence in entering into a PFI contract, Mazars followed exactly the same line of argument already presented by KPMG in defence of PFI. The same parliamentary inquiry called for the forced separation of audit and consulting arms to remove the precise conflict of interest scenario that objectors were drawing attention to with KPMG at Hackney Council.

As journalist Richard Brooks observes in his book, 'Bean Counters': "Although Big Four consultants' advice is always labelled 'independent', it invariably suits a range of corporate clients, with a direct interest in it. Unsurprisingly, most of the consultants' prescriptions, such as marketisation of public services – entail yet more demand for their services in years to come."[15]

The Big Four are in reality primarily consultancy firms – in the UK, only a fifth of their income comes from auditing and related services.

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8 BBC, 1 Feb 2019, 'Seven councils sue Barclays over £500m loans'

9 Newham also initially took legal action against RBS, but the case was dropped when the loans were renegotiated

10 Waugh, M. and Hodkinson, S., 2020, 'Examining the Effectiveness of Current Information Laws and Implementation Practices for Accountability of Outsourced Public Services'

11 Inside Housing, 11 May 2018, 'Council to take back control of Chalcots Estate following PFI collapse'

12 Camden New Journal, 28 Nov 2019, 'Exclusive: Camden Launches High Court Action Against PFI Companies'

13 Hodkinson, S., 2019, 'Safe as Houses: Private greed, political negligence and housing policy after Grenfell'

14 Business, Energy and Industrial Strategy and Work and Pensions Committees, 16 May 2018, 'Carillion' HC769

15 Brooks, R., 2018, 'Bean Counters -The Triumph of the Accountants and How They Broke Capitalism'

2.3 Citizen Objectors Disempowered

Objectors were throughout the process reminded of the uneven power relationship between a local resident and the external auditor. This stood out from our experiences as well as interviews with other objectors, and it paints a worrying picture where the LAA Act allows auditors to sideline residents who are trying to use rights that could, under different circumstances, have the potential to enhance public scrutiny and participation.

Auditors used the tools available in the legislation to restrict objectors from sharing information. They also made it difficult for residents to engage with the objection process through various obstructive behaviours, ranging from pressure put on objectors to refusing to accept an objection as valid or even respond to it. Even where auditors provided a decision on the objections, this took inordinate periods of time.

Threatening behaviour towards objectors

As objections were sent to the council's external auditor, most objectors did not communicate with the council at all. However, in some cases backbench councillors filed objections. When this became known, it resulted in threatening behaviour from cabinet members. Research for Action's 2018 report "Debt & Democracy in Newham: A Citizen Audit of LOBO Debt" describes a Newham Council Audit Board meeting in which the Audit Board Chair attempted to name and shame the objector, who the Chair knew to be a councillor. The following quotes are from that meeting's transcript:[16]

> *"In terms of the objections to the accounts, I understand that one of those objections has come from a councillor in the local authority, yes?"* (Cllr Hudson, Chair of Audit Board)

> *"Can you name the objectors and how much will this additional work cost us…?"* (Cllr Paul, Audit Board member)

> *"Chair, I would suggest that if it's a councillor we should be able to name them. I'm not sure about the legal advice but if it's a councillor you should be able to name them. I appreciate DPA [Data Protection Act] considerations for a non-council member but if we know it's a council member we should be able to name them."* (Cllr Baikie, Audit Board member)

Councillors objecting to LOBO loans in other local authorities described similar attitudes and incidents. In one case we are aware of, a councillor opted to withdraw their objection after alleging they were verbally threatened by a senior finance officer.

16 Audit Board Meeting, Newham Borough Council, March 2016 as documented by Debt Resistance UK

Validity of objection questioned

The legislation clearly states that the auditor must consider an objection from a local elector if it relates to a matter that could be subjected to a public interest report or court ruling and has been sent in writing to the authority as well as the auditor. This can also be done electronically.

> *27 (4) The local auditor may decide not to consider the objection if, in particular, the auditor thinks that—*
>
> *(a) the objection is frivolous or vexatious,*
>
> *(b) the cost of the auditor considering the objection would be disproportionate to the sums to which the objection relates, or*
>
> *(c) the objection repeats an objection already considered—*

However, we found that auditors were keen to try to invalidate objections. In Lambeth, the auditor (KPMG) originally rejected an objection from People's Audit on the basis that the costs had not been incurred in the financial year in question. Residents had to point out that they were mistaken, before the auditors agreed to consider it.

> *"I tried to raise a concern and the auditor – who is a partner at KPMG, so quite senior – said it fell outside the relevant financial year, even though the invoice that it related to was clearly dated 5 March. I said no, it is within the year. Two weeks later he got back and then we had some back and forth and he dismissed the objection I had put in. I had been careful to use the word objection, formal objection. He said he has seen documents that lead him to believe that no offence has been caused."*

Use of exclusionary, technical and complex language

Many objectors said the language used by the auditors felt unnecessarily jargon-laden and exclusionary, making them feel ill-equipped to deal with the process:

> *"Without the financially literate support [from Research for Action], even I as a professor at a university with some experience – not an expert in finance, but some experience with the financial industry – would not have been able to do this."*

> *"[The auditor's response] certainly was not the most lucid transparent document, you think they are trying to make it somewhat obscure. The campaign for clear English could have had a field day with it."*

> *"I mean, we're in London, where we have some local authorities where 30% of people weren't born with English as their first language"*

> ***"It is slightly ridiculous that in government legislation that is supposed to enable transparency it was illegal to share it."***

In the documents we saw, it was common to find large sections of irrelevant legalese presented over and over again. The technical language in the auditors' communications gave the impression that they were not provided to help the resident understand better the issue raised, but rather to make it more inaccessible, and to underscore the objectors' lack of financial expertise.

> *"Every time they corresponded, it was almost patronising, they say you do not know what you're talking about, here are the corresponding documents, read them and everything is okay."*

> *"All the while I was made to feel: you do not know what you are talking about, how could you possibly know all this complicated financial stuff."*

The tone also made some objectors so insecure that they started to worry there may be legal repercussions. One objector discussing a provisional view said:

> *"The way they were stating that I had produced no evidence to support my allegations – even though I had – made it feel as if I had done something wrong and that I was about to be accused of defamation."*

Sharing documents prevented by Schedule 11

The LAA Act introduces restrictions on information-sharing and disclosure that are significantly more extensive than the previous legislation, the 1998 Audit Commission Act. These restrictions on 'disclosure of information' apply across all parts of the Act but our findings show that they are being specifically and repeatedly used by auditors to prevent objectors from sharing correspondence. This applied mostly to provisional views and occasionally even the final decisions. The LAA Act states:

> *5(1)A person who discloses information in breach of this Schedule is guilty of an offence and liable on summary conviction to a fine not exceeding level 5 on the standard scale.*

Residents who received provisional views were warned not to share them with anyone but their legal representative under the threat of a level 5 fine – that is an unlimited fine under the current legislation. Many objectors found these restrictions intimidating and were left with the impression that information obtained at any stage of the objection process was not to be shared at all. This was even the case where Schedule 11 restrictions were lifted in the majority of final decisions.

The objectors considered this threatening and undermined the stated purpose of the public rights of the Act:

> *"It is slightly ridiculous that in government legislation that is supposed to enable transparency it was illegal to share it."*

Even where Schedule 11 was not explicitly cited, auditors made objectors feel that sharing their communications could be risky. In Salford, Grant Thornton emailed a final decision to a PFI objector which could not be printed out and had "confidential" written across every page. When the objector questioned the status of the decision, pointing out that it related to a request for a public interest report on a matter which affected thousands of residents, he was told:

> *"Whether a Statement is a public document, or a private letter to an individual, is not a matter that has been tested in a court of law. We would suggest that anyone considering publication considers obtaining their own legal advice."*

The objector told us: "I definitely saw this as a veiled threat."

The use of Schedule 11 in provisional views effectively prohibited objectors from seeking input from their community, placing them at a significant disadvantage and considerable pressure. When objectors received a provisional view from the auditors, they were given only 21 days to respond and provide further evidence. The objectors we were in touch with all had jobs, families or other caring commitments which gave them very little free time to consider the information presented, and to respond at length.

One objector said:

> *"It felt so off putting to be given so little time to respond. I had waited for so long to hear anything and then out of the blue, this huge document arrived and I had to immediately reorganise my work and childcare to try and deal with it. I really resented the amount of time these paid professionals had spent dealing with this and then I, as someone without any accountancy or legal expertise was supposed to pick this up and give a considered response. It felt like a joke, as if it was designed to ensure that I didn't come back to them."*

One PFI objector, after waiting two years for a response, pointed out to the auditor that given the impending bank holidays, they were effectively being given 13 working days to respond to a lengthy legal document and requested an extension of two months to consider the evidence presented properly. With no reasoning, the auditor granted an extension of just 21 days.

Time taken to respond

In many cases, auditors took several years to reach a conclusion on an objection. Of the 83 objections we have followed, there have now been 55 decisions issued. In 21 of these cases auditors took more than two years to reach and produce a decision letter. The longest of these took almost four years (Wirral LOBO objection, 44 months and Haringey PFI and Cornwall LOBO objections both taking 40 months).

Objectors found the time auditors took to respond a big flaw in the process and often had to send follow-up emails to the auditor even to get an acknowledgement for their objection.

> *"They were obviously trying to kick it into the long grass… exactly like they have done with the PFI [objection]. If I had not chased it up they would not have dealt with it. Simple as that. In a way I'm glad I have not chased up the PFI [objection I made] as you can see the system is not working."*

> *"Well, obviously, I think it's outrageous. If you're launching a legal objection – and I have to say my letter was very, very detailed, with some substantial complaints about the lawfulness of the loans – and then you have to wait…for two and a half years."*

> *"All this just shows the law is not working as it was supposedly designed to do."*

Some delays went on so long that by the time auditors considered the objection, some objectors had already moved out of the local authority in question, and were never contacted by the auditor again. As the process is so closed and secretive, we have not discovered what happened to these objections. It appears that an individual resident's change of address can result in an objection being dropped altogether, even where it raises issues that are acknowledged to be in the public interest with wider implications for the entire council.

In 2020, the NAO issued a new Code of Audit Practice, which sets out what auditors are required to do to fulfil their statutory responsibilities under the Act. The Code, which will apply for the financial year 2020-21, recommends a six-month limit for responding to objections. However, given the high rate of non-responses and failure to even acknowledge the objection, and the fact that there is no regulatory body to enforce the rules, it is hard to believe this will be respected or have the required impact.

2.4 Auditors' Inadequate Responses Limit Oversight

Auditors did not take any formal action as a result of the objections covered in this report and in many cases did not even respond. Worse still, where they did respond, those responses were overwhelmingly poor in quality of both arguments and the work done to back them up. Across the country, residents were left feeling that their concerns had not been taken seriously.

Auditors frequently addressed arguments that had not even been raised, while refusing to address the actual concerns. When they did rebut arguments in the objections, they did so by dismissing evidence provided by objectors, even when it was in the public realm or provided by industry experts. And where they did engage, it was often cursory and revealed either a deliberate misunderstanding or lack of proper understanding not just of the issues being discussed, but also the local government financial sector and its regulatory framework. As a result, auditors' decisions seemed totally arbitrary. They failed to provide evidence for their decisions or to share evidence they referred to, and consistently made favourable assumptions about questionable council behaviour they should have been scrutinising, demonstrating a concerning lack of professional scepticism. This failure creates a worrying oversight vacuum, where local authorities' increasingly commercialised and financialised dealings are left unchecked and unchallenged.

Questions not answered

Some residents asked the auditor a series of questions before submitting their objections, as the legislation allows them to do:

> *26 (2)At the request of a local government elector for any area to which the accounts relate, the local auditor must give the elector, or any representative of the elector, an opportunity to question the auditor about the accounting records.*

These questions related to weakness in existing governance arrangements for monitoring PFI contracts and ensuring their ongoing safety and value for money. They also sought assurances about processes that were in place to check these, both within the council and as part of the audit. Responses to these questions were often minimal but more frequently non-existent with auditors simply ignoring very specific questions that could have formed the basis of a public interest report.

In the case of LOBO loans, a Newham resident had spotted the interest rates of a loan were pegged to the London Interbank Offered Rate (LIBOR), a common benchmark for interest rates that bankers had colluded to manipulate in the early 2000s. Knowing there were issues with LIBOR being rigged, she exercised her right to question the auditor about the accounting records, only to find herself ignored:

> *"PwC looked at the contract, they looked at me, and they were silent. Then they said 'hmm, yes, you've got a good point there' and then I never heard from them again."*

It appeared that auditors had either not properly read the objection letters, or had deliberately avoided engaging with the arguments made.

LOBO objectors also included a set of written questions about the specific circumstances of councils LOBO agreements. Very few of these questions were answered satisfactorily, if at all. In at least one case, auditors interpreted the right to ask questions about the accounts in a narrow way that did not include supporting documents:

> *"although you have the right to ask me questions, I can only consider questions about the accounts I am auditing"*

In Lambeth, People's Audit also tried to use the right to ask questions to little avail: replies were of varying quality if they were received at all – in one case the auditor even stated they would not answer questions from a resident.

Failure to engage with objections' arguments

From their responses to objections, it appeared that auditors had either not properly read the objection letters, or had deliberately avoided engaging with the arguments made.

When objections are made on the basis that a resident believes an item of spending or income in the accounts could be unlawful, there are three possible criteria for defining this. That it was spent or received without powers to do so; that the council took from or added to the wrong fund or account; or that the council spent on something that they had the power to spend on, but the decision to spend the money was wholly unreasonable or irrational – as in, no reasonable person would have made the decision.[17]

In the case of PFI schemes, all objections were made on the grounds that the original decision to enter into contracts was unreasonable or irrational. Yet auditors frequently spent a large part of their response focusing not on the unreasonableness of the contracts but instead on whether the council acted within their power, going to great lengths to check if central and local government policies and regulations had been respected. They concluded with almost identical language across all responses:

> *"Our provisional view is that the Council had the legal powers to enter into the PFI contracts that are the subject of this objection" (KPMG)*

Objectors to LOBO loans argued that in some cases, councils did not have the power to enter these contracts, and even if they had, the decision could still be viewed as irrational. Residents questioned the lawfulness of the loans on the basis of a 1989 ruling[18] prohibiting councils from taking out derivatives, which LOBO loans contain. The auditors went to great lengths to argue that it was within the powers of the council to take out long-term loans, completely ignoring the central question of the derivatives – both their legality and the unreasonableness of entering such risky contracts.

Evidence provided ignored or dismissed

When auditors did engage with the arguments made, they frequently failed to consider supporting evidence provided by the objector or stated that no evidence had been provided.

Before submitting objections, People vs PFI sent FOI requests to all UK authorities with PFI schemes involving public buildings. They asked a series of questions about monitoring arrangements during and after construction, paying particular attention to structural and fire-stopping defects. As part of the audit process, auditors are required to "provide an opinion on the adequacy of systems in place to support the economy, effectiveness and efficiency in [the council's] use of resources"[19], hence objectors focused on governance arrangements of PFI schemes.

Details of the local authorities' response to these FOIs (or lack of it) were provided in the objections as evidence of insufficient assurance that existing systems were adequate and represented efficient and effective use of resources. Yet the auditors' response was a uniform "you haven't provided any evidence".

In one instance, KPMG ignored all arguments and evidence to the contrary and simply re-stated that as a PFI scheme "is based on a self-monitoring reporting model. Performance reports are submitted by the operator on a monthly basis together with a deductions report…" therefore "given the arrangements described above our view is that the council had adequate governance arrangements in place".

One of the issues LOBO objectors raised was the relationship between companies that were involved in recommending and brokering councils' LOBO loans.

Local authorities routinely hire treasury management advisers (TMAs) for independent financial advice, and many of the councils taking out LOBO loans were receiving

17 NAO, July 2020, 'Local authority accounts: A guide to your rights'

18 In 1989, a court ruling invalidated interest rates swaps sold to Hammersmith and Fulham Council by banks, because they said it was outside the council's legal powers to enter into such contracts. New York Times, 6 Nov 1989, 'british Court Invalidates Some Financial Swaps'

19 Sir Tony Redmond, September 2020, 'Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting'

advice from TMA companies. It is also standard practice to employ brokerage companies to broker a deal, which councils did when taking out LOBO loans. However in the case of LOBOs, the TMA companies were in many cases subsidiaries of the broker firms that negotiated the loans for the councils, and the brokers paid the TMAs large fees every time the council opted to use them.

This practice, which resulted in brokers being paid by both sides of a deal was specified in a 2011 Competition Commission report looking into one of the company's takeover by a rival TMA. After being discovered by Debt Resistance UK, these broker-advisor relationships received substantial media coverage. Still, despite objections including details of individual councils' TMAs, auditors decided both the conflict of interest, and the specific terms of the TMA's advisory contract with the council were not worth looking into, as was requested by the objectors, and a number of influential MPs.[20]

PFI objectors also referred to a range of reports and investigations in the public domain, including the independent inquiry into the Edinburgh PFI schools scandal[21] which specifically highlighted weaknesses in the self-monitoring nature of public private partnerships; evidence about significant fire safety failings in schools and hospitals[22] including a 2016 BBC File on Four investigation[23] exposing significant fire safety issues in major hospitals. Auditors simply did not engage or respond in any way to any of these when issuing decision notices.

In the case of LOBO loans, objectors referred to evidence provided by two financial experts: a derivatives expert, Abhishek Sachdev, who has advised the FCA on a derivatives mis-selling case, and Rob Carver, a former Barclays banker who was involved in the pricing of these loans. Both experts provided evidence to a parliamentary inquiry[24] on LOBO loans and were interviewed by Channel 4 as part of a documentary on the loans,[25] and in both cases highlighted how highly problematic these loans were. Grant Thorton's response to the evidence was:

> *"…these are the views of one expert and do not provide prima facie evidence that the costs and risks associated with the Council's LOBO portfolio were not understood by Council officers or that the LOBO portfolio is prejudicial to the interest of tax-payers."*

The auditors themselves failed to provide any opposing evidence from other financial experts.

Inadequate investigations

As a result of auditors' poor engagement with the arguments and evidence in the objections, their decisions were of low quality. They looked at evidence very partially and came to conclusions that objectors often found baffling. Auditors' decisions were most often not backed up by reference to any evidence or supporting documentation, and when they did refer to supporting evidence this was only rarely shared with the objector. Furthermore, withholding all documentation upon which the auditor's decision was based made it much harder for objectors to even consider a legal challenge to the auditor's inaction.

One unusual example of an auditor sharing contemporaneous documents with an objector was in response to a 2016/17 PFI objection. In the words of the auditor KPMG, this was to "demonstrate that the financial and operational aspects of the PFI contracts were analysed and considered by officers and Members". In fact, it demonstrated the opposite. To make a decision on a PFI project, councillors had been given almost no time to consider and analyse any of the evidence in relation to entering into this agreement. From the minutes of the Policy and Implementation Urgency Panel, 27 March 2002:

> *"Concern was expressed that the reports for consideration at this meeting had only been available that afternoon. In the circumstances the Chair agreed to delay the start of the meeting for ten minutes to allow Members of the Panel time to read the reports."*

Reference to this and the absence of any other detailed financial analysis were followed by the usual auditor's conclusion that *"the approach taken was likely to have been lawful"*. (KPMG)

Assumptions about LOBO loans' lawfulness were also made on grounds that baffled objectors. Some LOBOs from foreign banks were taken out before a 2004 change in legislation allowed local authorities to take out loans from foreign banks without prior permission from the HM Treasury. However, neither councils nor the Treasury have been able to provide evidence of Treasury approval. In one case, EY even stated that as the law had subsequently changed, decision making prior to 2003/04 that might have been unlawful was not worthy of investigating:

> *"In our view, a Treasury consent may well have existed at least in relation to foreign lenders within the EU (given the passage of time, it is not surprising if the Council does not have a record of any consent)"*

20 The Independent, 23 March 2016, 'UK local authorities could have been ripped off by controversial 'lobo' loans, MPs say'

21 Prof John Cole, 9 Feb 2017, 'Report of the Independent Inquiry into the Construction of Edinburgh Schools'

22 The PFI schemes concerned were Knowsley Schools PFI, Coventry Hospital and Cumberland Infirmary. See Whitfield, 2017, 'PFI/PPP Buyouts, Bailouts, Terminations and Major Problem Contracts in UK'

23 BBC Radio 4, 10 July 2016, 'File on Four: The Price of PFI'

24 Housing, Communities and Local Government Committee, 2015, 'Local Council bank loans inquiry'

25 Channel 4, 6 July 2015 'How Councils Blow Your Millions'

Even more strikingly, the same auditor went on to state:

> *"Whilst this did raise questions of legality, we have concluded that whether or not unlawful for this reason (and we consider that a Treasury consent may well have been in place), given that the law changed within a year of the Council entering into the relevant LOBOs, this would not be a sufficient basis for seeking a declaration before the courts or issuing a public interest report."* (EY)

Furthermore, the auditor did not contact HM Treasury for clarification. In response to a FOI request by Research for Action, the Treasury confirmed they do not have records of such approvals ever taking place.

The most recent LOBO loans and PFI contracts were signed more than five years before these objections were submitted. Most auditors used this fact to blame the absence of contemporaneous documentation on the passage of time and the councils' data retention policies. However most local authorities' rules applying to the retention of documents are based on relevant legislation[26] which requires key contract documentation to be retained for a given number of years after the end of the project or contract. In the case of Leeds City Council, which has both LOBO loans and PFI projects, the policy is to retain agreements and tender documentation of PFI contracts for 12 years from the end of the project and LOBO contracts for six years after the contract has ended. In the case of a 25-year PFI contract it would have to be retained for 37 years. However, KPMG, wrote:

> *"As both PFI contracts were put in place over 16 years ago, it is perhaps to be expected that there would be little contemporaneous documentation available setting out the council's decision-making processes and what was taken into account prior to entering into the contract...."*

Auditors used similar arguments when dealing with objections to 70-year-long LOBO loan contracts.

Despite objections arguing that councils had not been capable of evaluating risks, auditors presented nothing to demonstrate they had asked for or received any documentation from councils as proof they had considered and understood the risks involved. Auditors confidently asserted that an absence of evidence was proof that all relevant factors were considered, despite, by their own admission, having no access to documents relating to those decisions.

"It is a reasonable assumption that the detailed analysis was undertaken" (Grant Thornton)

26 The Limitation Act (1980) Public Contracts Regulations (2006), Openness of Local Government Bodies Regulations (2014) as well as good industry practice i.e. National Archives Retention Guidance no. 5 Contractual Records.

"I would have expected them to gain an understanding on how the decisions were made and actually to reflect on whether it was rational decision making in the interests of the public."

LOBO objectors expressed surprise at the lack of effort made to investigate more thoroughly:

> *"For the time it took, and the cost, I would have expected them to speak to people and gain an understanding on how the decisions were made and actually to reflect on that decision making process, and whether it was informed by conflicts of interest and was rational decision making in the interests of the public."*

Where councils held numerous LOBO loans, the auditors in some cases decided it was sufficient to analyse only a small batch of them and base their conclusions on these. Only when objectors prompted the auditors, by highlighting that there were different types of LOBO loans, each with its own approval process and levels of risk, did they analyse all of the loans.

In some cases, the origin of the evidence provided by auditors appeared contrived and dubious. One auditor, who dealt with several LOBO loan objections across multiple local authorities used identical quotes attributing them to several different councils and finance officers as evidence they had understood the loans and believed they were in their best interest.

Auditors lack expertise on local government finance

The recent Redmond Review call for views pointed out the need for auditors of local government to have an increasingly specialist skill set:

> *"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."*[27]

Having received submissions from 79 public bodies, the findings of the same review pointed out a significant deficit in sector-specific training and expertise for the majority

27 MHCLG, 17 Sep 2019, 'Call for views for independent review into local authority audit'

of auditors now working on local government audit. The report stated that many local authorities had "significant concerns about the knowledge and expertise of staff working on their audit" and 83% felt the private firms did not have enough understanding of the local authority regulatory framework. Authorities' raised concerns at private auditors:

> *"...not having a full understanding of how local authorities were funded and how this impacted the accounts...a lack of continuity from year to year, or in some cases from week to week...a lack of understanding of local authority specific financial statements such as the Collection Fund and Housing Revenue Account"*

Our findings demonstrate a clear lack of relevant experience and expertise across audit firms currently working in local government audit. Auditors showed a lack of understanding of the regulatory framework guiding local government finance – even where they referred to official guidance from CIPFA, in some instances they clearly misunderstood its content – and misinterpreted the nature of the financial instruments that objections focused on. This was particularly baffling considering that the audit firms also undertake consultancy services, including on PFI, and should therefore have a working understanding of basic concepts of finance such as the cost and risk of fixed rate vs variable rate borrowing.

In the context of local government debt, CIPFA's Treasury Management Code[28] states clearly:

> *"It is concerned with both interest rate risk (the risk that fluctuation in the levels of interest rates create an unexpected or unbudgeted burden against which the authority has failed to protect itself adequately) and refinancing risk (the risk that borrowing cannot be refinanced on terms that reflect the provisions made to do so or on terms inconsistent with prevailing market conditions at the time)".*

However, both in the case of LOBO loans and PFI it appeared the auditors either dismissed these risks, or lacked a basic understanding of them. This is particularly concerning in the context of evaluating the public interest of public sector borrowing.

The cost of LOBO loans over the term of the loan is very hard to estimate due to the embedded derivatives and the length of the loans and, as CIPFA guidance clearly stated:

> *"While a LOBO's contractual maturity may be, for example, 50 years, comparing the headline rate to that available through 50-year PWLB [Public Works Loan Board] is overly simplistic."*

28 CIPFA, 2017, 'Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes'

Yet all auditors claimed to have demonstrated the lawfulness of LOBO loans simply by benchmarking them against PWLB loans.

Similarly, exit penalties[29] for LOBO loans are high compared to loans of similar length and are unpredictable because they are at the discretion of the banks who issue them and can only be estimated via specialist pricing software. This makes it unaffordable for local authorities to pay the loans early. In comparison, when councils borrow from the central government's Public Works Loan Board (PWLB), the exit fees are predictable and the rates are publicly available. Yet auditors inexplicably thought it was sufficient to use the same rates for both:

> *"In the absence of comparative redemption rates [= exit penalties] for LOBO loans, as exact redemption figures would be calculated by the lender were the Council to consider redemption, the Council have opted to use PWLB redemption rates to calculate the repayment costs of their LOBO portfolio. This is, in our view, a reasonable approach given the lack of information on LOBO redemption rates."* (EY)

Contrary even to CIPFA guidance[30] auditors argued there was no need for councils to consider the high exit costs on LOBO loans:

> *"The Council does not enter into external borrowing with an intention to exit arrangements in advance of maturity dates. The 'exit cost' of the Council's LOBO portfolio is therefore a purely hypothetical concept."* (Grant Thornton)

Despite early exit costs for LOBO loans being a purely hypothetical matter in Grant Thornton's opinion, for the 45 local authorities with RBS LOBOs they have proven to be very real. FOI requests sent by Research for Action detail a total of 90 loans terminated early by RBS,[31] with a total principal amount of £1.43bn and exit fees paid by the councils to the RBS amounting to hundreds of millions of pounds.

Where PFI objections raised this same issue of whether proper consideration was given to potential exit costs when entering into contracts, auditors simply denied this was a relevant issue. PFI objectors cited the 2016 report by the European Services Strategy Unit[32] which draws attention to

29 When taking out a loan, a borrower usually considers the refinancing risk, because they might want to borrow from elsewhere to pay the loan early if their situation changes. When the borrower exits early, the lender loses interest income they had expected to get; it is therefore common for long-term loans to come with an exit penalty.

30 CIPFA/LASAAC on how local authorities should account for LOBO loans, 16 May 2018,

31 The Guardian, 23 March 2019, 'RBS to wind down £1bn worth of contentious local council loans'

32 Whitfield, 2017, 'PFI/PPP Buyouts, Bailouts, Terminations and Major

the numerous PFI projects which have been terminated and many other instances where public bodies were considering termination due to a variety of issues. And yet KPMG simply argued:

> *"...the council did not enter into its school PFI arrangements with the intention of existing them in advance of the maturity date of the contracts. The exit costs are therefore, to an extent, hypothetical..."*

Councils charged additional costs

Not only were objections handled poorly and with lengthy delays, but an FOI request to all English local authorities has shown auditors have been charging additional fees for the work. Since 2015, auditors have charged local authorities anything between £892 and £40,000[33] for dealing with a single objection, even though this did not include the work of carrying out a public interest report or making a high court referral. Residents, on the other hand, were frequently reminded of the potential cost of their objection or inspection requests either by the auditors or in some instances by local authorities. Lambeth People's Audit described how the council publicised the inspection rights, alongside the cost of dealing with previous years' inspections:

> *"The council prominently displayed the cost of dealing with public audit inspection questions, along with big red crosses (and some green ticks) which is not exactly inviting."*

Residents understandably expressed concerns about how much the auditors were charging councils for delivering such poor responses and that money was being wasted. As one objector described:

> *"I was feeling a bit nervous about how much this was going to cost the council. My motivation to do this is that if conflicts of interests and bad decisions are happening to put the council into debt – all during a period of austerity when central government is stripping out funding – that is bad. But I did not really want to get the council to have to pay even more money to the auditor."*

In addition, many of the investigations carried out by auditors remain concealed from the public and in some cases from the local authorities themselves. This point was addressed in the Redmond Review which stated that "a not insignificant number of authorities" who submitted evidence as part of the review felt that auditors were levying substantial additional charges without providing any evidence that additional work had been done. According to the report:

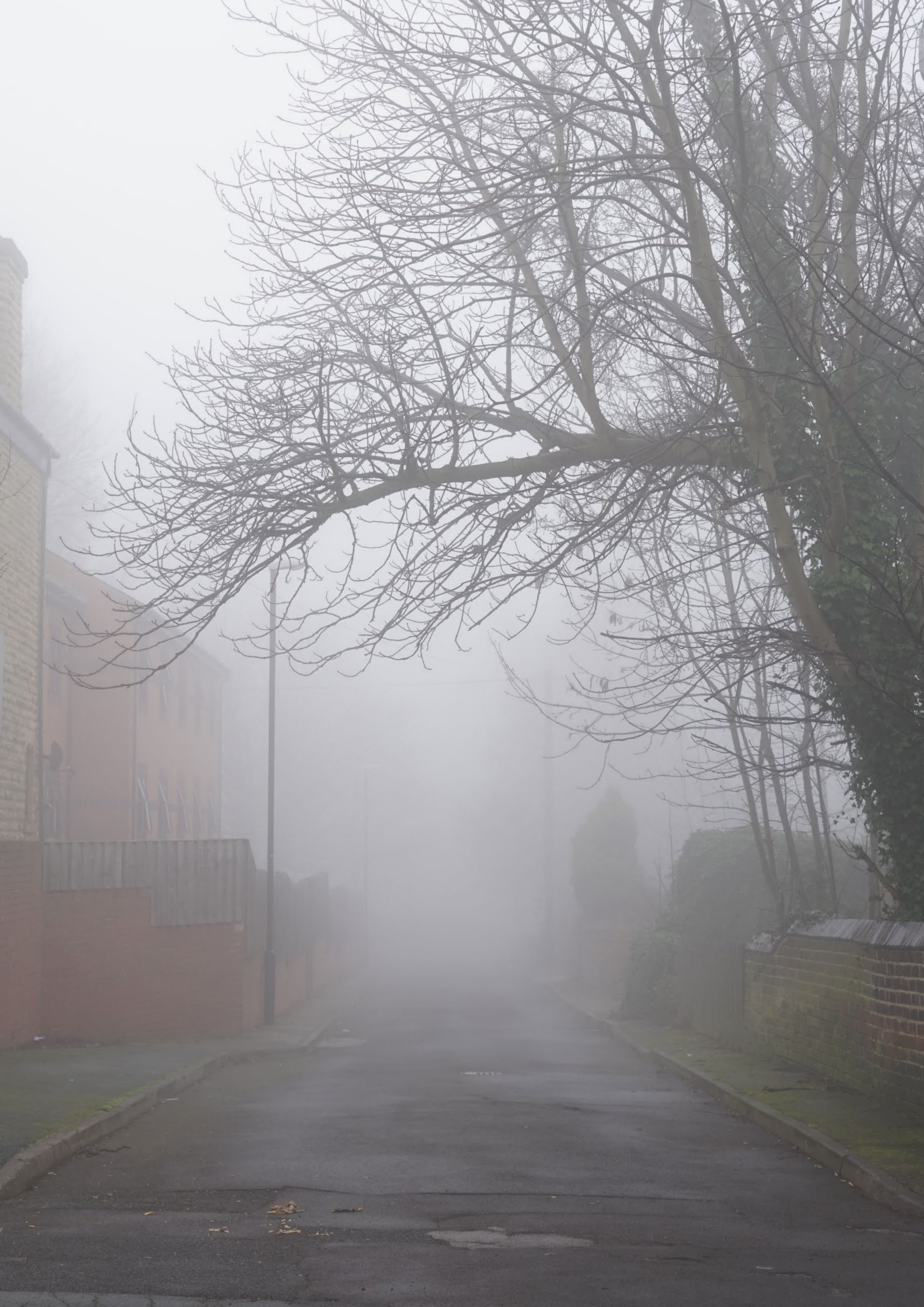
> *"Some local authorities passed examples to the Review of auditors, representing more than one audit firm, refusing to provide evidence to support a requested fee variation."*

Meanwhile auditors' submissions to the same review included complaints that they were not able to charge enough to cover the cost of the work they undertook. The findings of the review have now recommended a revision of the current fee structure "to meet the full extent of local audit requirements".

What is clear from the findings presented in this report – as well as authorities' evidence to the Redmond Review – is that it makes no sense to allow auditors to charge even more money for substandard work with no public transparency or accountability benefit. This is particularly striking given the strong arguments over wasteful spending which preceded the Audit Commission's abolition. Instead, there is a need to challenge the persistently low quality of the work done in response to citizen objections and to curtail auditors' ability to charge for this 'additional work'.

Problem Contracts in UK'

33 Breckland Council (£892) and Croydon Borough Council (£40,000), figures obtained through a Freedom of Information request in September 2019



3. FINDINGS: INSPECTION OF COUNCIL ACCOUNTS

Introduction

The previous section looked at the auditors' role in responding to, or thwarting, the public's legal rights to scrutinise local government finance. This section focuses on public inspection rights and examines the role of local authorities in interpreting and implementing the same legislation.

Unless specified, legislation quoted from is the LAA Act rather than LAA (Scotland) Regulations either because there is little or no practical difference, or because the examples given apply only to England. Where variations occur or are relevant, these will be shown as LAA Act followed by [LAA(S)R]. As well as asking the auditor questions and objecting to accounts, the legislation also allows residents to request and inspect items relating to them. The council's annual statement of accounts must be made available for inspection during a window of 30 [15] working days each year to "any persons interested". In England the Local Audit (Public Access to Documents) Act of 2017 has extended this right to journalists, including unpaid citizen journalists. The legislation enables people to:

> *"inspect the accounting records for the financial year to which the audit relates and all books, deeds, contracts, bills, vouchers, receipts and other documents relating to those records"*

Apart from the introduction of "and other documents" this wording is identical to the previous legislation (Audit Commission Act 1998). The significant difference is that while the previous legislation only excluded personal information from any inspection request, following a controversial and landmark case at the Court of Appeal[1] which saw PFI waste contractor Veolia successfully use European Convention on Human Rights to stop a local authority from disclosing information on a PFI contract under the 1998 Act, the 2014 legislation now excludes any commercially confidential information where:

> *"(a) It's disclosure would prejudice commercial confidentiality, and*
> *(b) There is no overriding public interest in favour of its disclosure"*

The legislation has been further weakened by the removal of S.14(3) which stated that anyone who tried to obstruct a person in the exercise of a right under this section or didn't provide copies to someone entitled to obtain them was "guilty of an offence and liable on summary conviction and to a fine not exceeding level 3 [£1,000] on the standard scale".

The evidence in this section relates to inspection requests submitted over three years by the authors of this report who have made frequent use of these inspection rights. The findings presented in this chapter focus primarily on 72 inspection requests submitted by authors on a range of different subjects. Pilot research in relation to PFI involved conversations with finance and information officers in several authorities and, where it is pertinent, some of their comments have been quoted here. We have also interviewed members of Lambeth People's Audit and collected experiences through an online questionnaire. Any reference to statistics does not include questionnaire respondents as their contribution focused on their general experiences rather than the granular detail of their requests.

Based on our findings, the apparently wide-ranging inspection powers of the LAA Act are being undermined in a number of ways by local authorities. Councils often fail to publicise rights (even though the legislation requires this) and take so long to respond that residents cannot file objections informed by the information received. Councils frequently treat inspection requests as FOI requests; question non-residents' rights to inspect and are inflexible in making documents available online. They also interpret the legislation as narrowly as possible, refusing to share documents related to the accounts, and often present the inspector with the data in a form that is simply impenetrable. Only a very small number of people reported being able to access useful information in a manner intended by the legislation.

This lack of transparency has serious implications for residents' ability to hold their local authorities – and elected representatives – to account. When access to information is curtailed, local people do not even know what money is spent on, and without information do not have the evidence to challenge those decisions. This is further amplified when the council enters into outsourced or arms-length arrangements to provide services such as PFI schemes, housing associations, or tenancy management organisations.

The authors of this report and questionnaire respondents have also used the inspection rights in relation to other issues. These include requests to Kensington and Chelsea Borough Council regarding the refurbishment of Grenfell Tower. The 2017 tower block fire that killed 72 people was a shocking reminder of the consequences of neglecting proper scrutiny and refusing to allow residents to hold their local authority to account.

1 Veolia v Nottinghamshire County Council [2010] EWCA Civ 1214, (2010)

Failure to publicise rights

Councils are required to publicise the period during which an inspection can be made and "details of the manner in which notice should be given of an intention to inspect the accounting records and other documents" under the Accounts and Audit Regulations (2015) Section 15(2)(b).

While some authorities do provide a dedicated email address, our experience shows that it is far more common for there to be no helpful contact information available on council websites. As one requester put it:

> *"Unless you are actively looking for the notice, there is no way you would find it. I would be surprised if that web-page gets as many as 100 web-hits per year."*

Not only is the publication of information relating to these rights inconsistent – awareness of the rights within local authorities is not always high, leading to a general experience where even submitting a request was a needlessly complex process. In some instances this even prevented an inspection request from being submitted.

Other than providing the name and address of the local auditor, authorities are not specifically required to provide an email address or even direct phone number to assist members of the public to submit an inspection request. The inevitable impact of this is to reduce awareness of the right and make it more difficult for people to exercise it. This is especially hard for those who do not have access to the internet.

In many cases the title of the officer responsible for overseeing the audit was published, but no name or contact details. This role, officially known as the Section 151 officer, is not a public-facing post and tracking down a name, phone number or email was a time consuming process. Telephone calls to councils met with little or no understanding either of the Section 151 officers role, or of the law itself. Calls were most often transferred either to the FOI department or went round in circles through legal, governance and accounts departments. On six occasions when an email address was published or located, requests bounced back with an out of office reply as the relevant officer was not even in work throughout the inspection period, which occurs over the summer.

One Section 151 Officer, who we spoke to during pilot research,[2] felt the new Act had not been sufficiently updated and said:

> *"Even the Act in its updated form is quite archaic and harks back to a time when we used to print off a copy of the accounts and leave them at reception."*

2 This was part of a pilot request to local authorities to determine how inspection requests were logged, conducted as part of her PhD research by Megan Waugh

Newham Borough Council appeared to have updated its own practices and in 2017 published their inspection notice on the council's website including a phone number and email address of the Chief Accountant. However, the phone number did not work and when alerted to this on Twitter[3] the council simply stated it was correct. The requester tried to contact the finance department number but it was not answered. It took three attempts before getting a response from the Chief Accountant's email.

And in Scotland, during the 2015/16 inspection period, 26 local authorities with PFI education schemes were identified by campaigners to receive identical requests for information. Of these 26 authorities, only six published an email address either on the accounts page or in the public notice of inspection. The remaining 20 provided either a name or a title whose contact details were not always easy to find. This meant that in more than half the cases, the requester had to ring the local authority to ask for the relevant contact name and email.

While the legal duty to publish may have been met, these experiences suggest that councils lack the necessary resources and carry out little forward planning to ensure they can respond to any requests.

Officers did not understand the legislation

It was common for council officers not to be aware of the LAA Act and instead refer inspection requests to be dealt with as FOI requests. Various attempts were made to avoid this when submitting inspection requests, such as including the name of the LAA Act in the subject header of emails or specifically stating "this is not an FOI request". However, these made little difference.

Tower Hamlets Council in 2017 – despite being clearly told the request was under the Local Audit and Accountability Act – took 61 days to respond to a request. They refused to provide the information, citing an exemption under the Freedom of Information Act.

Responding to a 2016 inspection request, Falkirk Council claimed they had received the request after the inspection period had closed and therefore transferred the request to FOI(S)A. Their audited accounts for the year pointed out the council had breached regulations by not having the public notice of accounts on display throughout the inspection period.

Nearly half (45%) of authorities which provided a response to inspection requests treated them as an FOI request. Those that were dealt with under FOI were then subject to various non-compliant behaviours in relation to that Act. Finally, only

3 Fanny Malinen on Twitter, 12 July 2017

Requests were refused in their entirety with blanket applications of commercial sensitivity.

one council who transferred the request to FOI, provided information within the legally stipulated 20 working days.

Other requests were refused in their entirety with blanket applications of commercial sensitivity being applied, or with requesters being arbitrarily labelled as 'vexatious'.

Also in Newham in 2016, officers appeared not to understand the LAA Act and when a resident visited her local library for a pre-arranged visit to look inspect a contract, she was met with confused staff who didn't know what she was talking about and directed her, incorrectly, to the auditors who are not responsible for dealing with inspection requests.

> *"I got to the library on time. I asked to see the accounts, the accounts were not there. The documents that I requested were not there. And everyone seemed bewildered that I had turned up. They then said I had to speak to the auditors"*

Time taken to respond

Regardless of whether the councils responded under the correct legislation or under FOI, only four responses were provided within the 30-day inspection window, and therefore in time to inform the objection process. Worse, no acknowledgement or response of any kind has been the most common 'response' to citizen efforts to exercise their right to inspect accounts and related documents.

Of all the inspection requests submitted, 54% received no information, either as a result of a refusal or non-response, and where a response was received only four of these were provided within 20 working days. The remaining requests took anything from 22 days to more than a year to respond with Hackney (391 days) and Leeds (103 days) being the slowest.

Lambeth Council regularly routinely rejected requests on the basis that it would take too long to find the information, despite the fact that, under the LAA Act, there is no limit to how much time can be expended providing information.

The LAA Act does not specify a time limit for authorities to provide information. However, we believe, it is implicit in the legislation that the inspection period exists to allow the public to scrutinise aspects of the accounts and to then be able to further question and potentially object to the accounts, within the annual allocated time window. If the information is not provided within that window, it does not serve its primary purpose of establishing or extending the basis of a decision to object.

One Corporate Finance Officer commented on this exact issue:

> *"we have one resident who always objects. If they don't get the information...within the objection window, that makes it harder for them to object. It's not that I am encouraging people to object but it seems in the spirit of the act to provide the information within that period"*[4]

Based on the collective experiences set out here, we have found this timely response rarely happens. One resident who had requested documents in the first week of the inspection period reported that he did not receive them until 5:45pm on the final day of the inspection and objection window.

Disputes over related documents

The legislation specifically states that inspection rights apply not just to "the accounting records for the financial year" but extend to "all books, deeds, contracts, bills, vouchers, receipts and other documents relating to those records". Despite this, we found enormous inconsistency in the application of this section which included frequent misquoting or narrow readings of these rights that were experienced as an attempt to stall or obstruct requests.

Some authorities accepted that a contract entered into ten years prior, for which payments were ongoing, constituted related and relevant information. Others refused to accept this.

Responses in some cases revealed that inspections requests were not read carefully and that stock phrases such as 'falls outside this financial year' were being sent out as an automatic response.

In response to a 2016/17 request for information relating to LOBO loan restructuring, Newham Council wrote:

"With specific regards to the last two items of information requested, I believe this is outside the scope of the Act, as paragraph 1 of section 26 of the Local Audit and Accountability Act 2014 states:

> *"At each audit of accounts under this Act, other than an audit of accounts of a health service body, any persons interested may—*
> *(a)inspect the accounting records for the financial year to which the audit relates..."*

The information you have requested is outside of the period of the 2016/17 accounts. If you hold a contrary view, please could you reply to myself setting out your reasons why."

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4 This was part of a pilot request to local authorities to determine how inspection requests were logged, conducted as part of her PhD research by Megan Waugh

The inspector replied quoting the missing part of the legislation:

> *"(a)inspect the accounting records for the financial year to which the audit relates and all books, deeds, contracts, bills, vouchers, receipts and other documents relating to those records"*

However, this only resulted in another seven months of correspondence, at the end of which there was no disclosure.

In 2017, following the Grenfell Tower fire, requests were made to Kensington and Chelsea Borough Council for expenditure on fire safety certificates, legal advice and completion certificates as well as copies of the agreement and contracts which were part of the refurbishment work of the tower. This request resulted initially in just six sheets of photocopied excerpts from spreadsheets with no supporting documentation or key to aid understanding the referencing system used. Further emailing for information relating to payments for the work as well as relevant insurance payments made during the 2016/17 financial year produced this response:

> *"The documents you have requested fall outside of the scope of the provisions of the Local Audit and Accountability Act 2014. Inspection of documents under this legislation must be about the accounts or linked to an item in the accounts...your request asks for information which is not relevant to the accounts, payments and expenditure (such as fire risk assessments) and as such that would not be considered to be 'supporting documentation'".*

'Interested person' status questioned

Both English law and the equivalent Scottish regulations clearly differentiate between the rights to object to an authority's accounts, which are only provided to a local elector, and the rights of inspection, which are granted to what the law defines as "interested persons".

In 2017, the Local Audit (Public Access to Documents) Act expanded public access to information to include 'any journalist' and provided a definition of 'journalist' as "any person who produces for publication journalistic material (whether paid to do so or otherwise)."

Despite this we found it common for local authorities to demand a local postal address and questioning the status of the 'interested party' has often been perceived as a delaying tactic.

As one inspector told us:

> *"I often felt that questioning my status was being used as a delaying tactic. The most blatant example of this was when I challenged a decision not to deal with my inspection request because I wasn't a local elector. I received an email conceding that I qualified as an 'interested person' and then heard nothing for weeks. When I followed up on this, I was told the inspection period had closed...when I submitted a similar request the following year, I received exactly the same initial response telling me they wouldn't respond because I wasn't a local elector!"*

Insisting on outdated town hall inspections

The issue of whether the 'right to inspect' in a digital age encompasses the right to request information to be sent electronically or whether it remains limited to a right to attend council offices to inspect paper documents was a frequent point of contention.

While the majority of councils make draft accounts available online for public inspection, others, notably Kensington and Chelsea, had to be prompted to make them available, despite the inevitable and understandable scrutiny they were under in the weeks following the Grenfell Tower fire.

Most councils also accepted requests for information in an electronic format, however there was a small but persistent number of authorities who insisted on an appointment being made to visit council officers to view the documents.

Over the course of four years, Oldham Metropolitan Borough Council refused to provide information electronically and pointed out the Act does not require them to do so:

> *"Under the new Act we are not required to make this information available to you electronically. Please could you therefore come in person to inspect the Council's accounts."*

One Newham resident was told she could only view the item of accounts she had requested at her local library and had to take a whole day off work to do so.

> *"I thought well that's annoying, because I'm self-employed and I earn hundreds of pounds a day actually, and to lose hundreds of pounds to exercise my democratic right, and all the work I've had to do to get to this stage has put some strain on my business. But it is something I believe in."*

Other councils bizarrely insisted that the majority of information requested (contracts, invoices) was not held electronically. In 2017 in response to a request relating to PFI contracts and safety issues, Sheffield City Council stated:

> *"Due to the volume of information we hold on the PFI contracts, and as the majority of this is not electronically available, the best option is for yourself to inspect the*

documentation in person at the Council office as per the recommended option under the Public Rights Notice."

Variation in response quality

When authorities did provide information, there was enormous variation in the quality of responses. In response to identical questions about PFI education schemes, councils' responses ranged from a one-page letter stating "information not held" or a response which simply stated "not applicable,". In contrast another council sent a CD which contained 300 separate documents. Documents were frequently provided with no explanation, spreadsheets were sent in low resolution PDF format making them impossible to search electronically, or as with the Kensington and Chelsea, spreadsheets had coded headings but no key to explain what these codes actually referred to.

Lambeth People's Audit experienced multiple obstructions and inconsistencies in how the law was applied. While most councils routinely publish councillors' and officers' expenses on their websites, when a member of People's Audit requested to see them, the council responded saying they could not disclose this as it was personal information. In 2017, Southwark Council provided a contract to a member of the public who wanted to challenge the costs on behalf of leaseholders. When the same person requested to see the same contract a year later the council denied them access, stating that the information was commercially confidential. And when Lambeth leaseholders living in the same road requested to see the details of major works to their properties, leaseholders on one side of the road received detailed breakdowns, while neighbours on the opposite side of the road (managed by a different team in Lambeth) received nothing during the inspection period and only limited information after it.

Lack of a formalised complaints procedure

There is no complaints procedure relating to the Public rights section of the LAA Act. When information is refused either by the council, in relation to inspections, or by the auditor in the case of a question, the requester cannot ask for a review or take the issue to an independent body. This contrasts to FOI Act, where an initial refusal of information still leaves scope for an internal review, referral to the Information Commissioner's Office and ultimately an appeal to a tribunal.

The lack of an avenue for complaints also affects the objection process. As detailed in this report, objectors found the auditors' behaviour and the quality of responses woefully inadequate and were at times concerned with the potential conflicts of interest that could influence the conduct and decision-making of the auditors. However, when objectors inquired about who they could complain to, they were told to use the internal complaints procedure that each audit firm had

"I do not know who to complain to. I guess the only place is the high court, and I do not have money for that."

in place, reducing the issue to a question of customer service, rather than public interest. This also highlights the absence of consideration that the auditors might be conflicted, as there is no independent oversight body to monitor their conduct or professional standards.

The LAA Act does not allow an objector the right to appeal when the auditor refuses to issue a public interest report. When the auditor refuses to refer an issue to the high court, the objector can appeal but only through a court procedure that would carry considerable personal cost. Many objectors equated it with the Schedule 11 preventing sharing information, leaving them feeling that they had taken a risk of getting into legal difficulty when submitting the objection. As one LOBO objector said:

> *"My husband was worried about me, as he said we cannot have you being arrested. I said this is something I have to do, but it is something I would warn others about."*

When auditors refused to refer issues to the high court, none of the objectors we spoke to were willing to take on the risk of initiating legal action: with legal aid curtailed and out of reach for most people, this could have left residents vulnerable to accumulating significant court costs.

Some of our interviewees thought the objection process was too much of a waste of time to even consider complaining, even if that had been possible. Others said they would have complained, had they known who to:

> *"I do not know who to complain to. Do I go to the FCA? I do not think so. Do I go to the council? Of course not. I guess the only place is the high court, and I do not have money for that."*

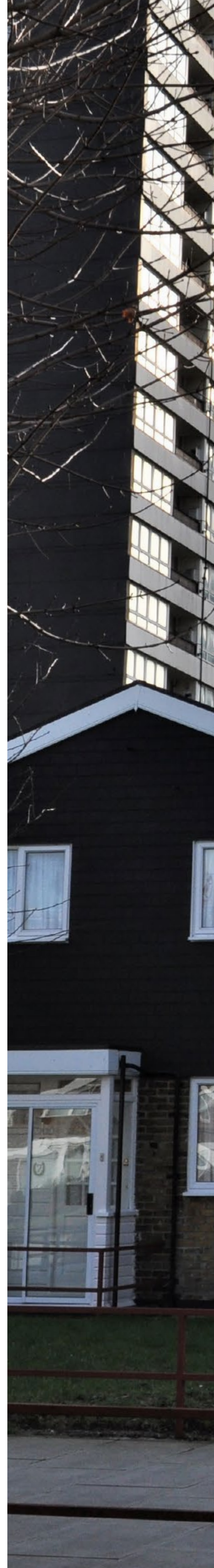
> *"I didn't [complain]. Because I cannot reply to them. And I did not want to respond to the letter I got – as it said any further queries would incur cost. So I did not really know who to complain to."*

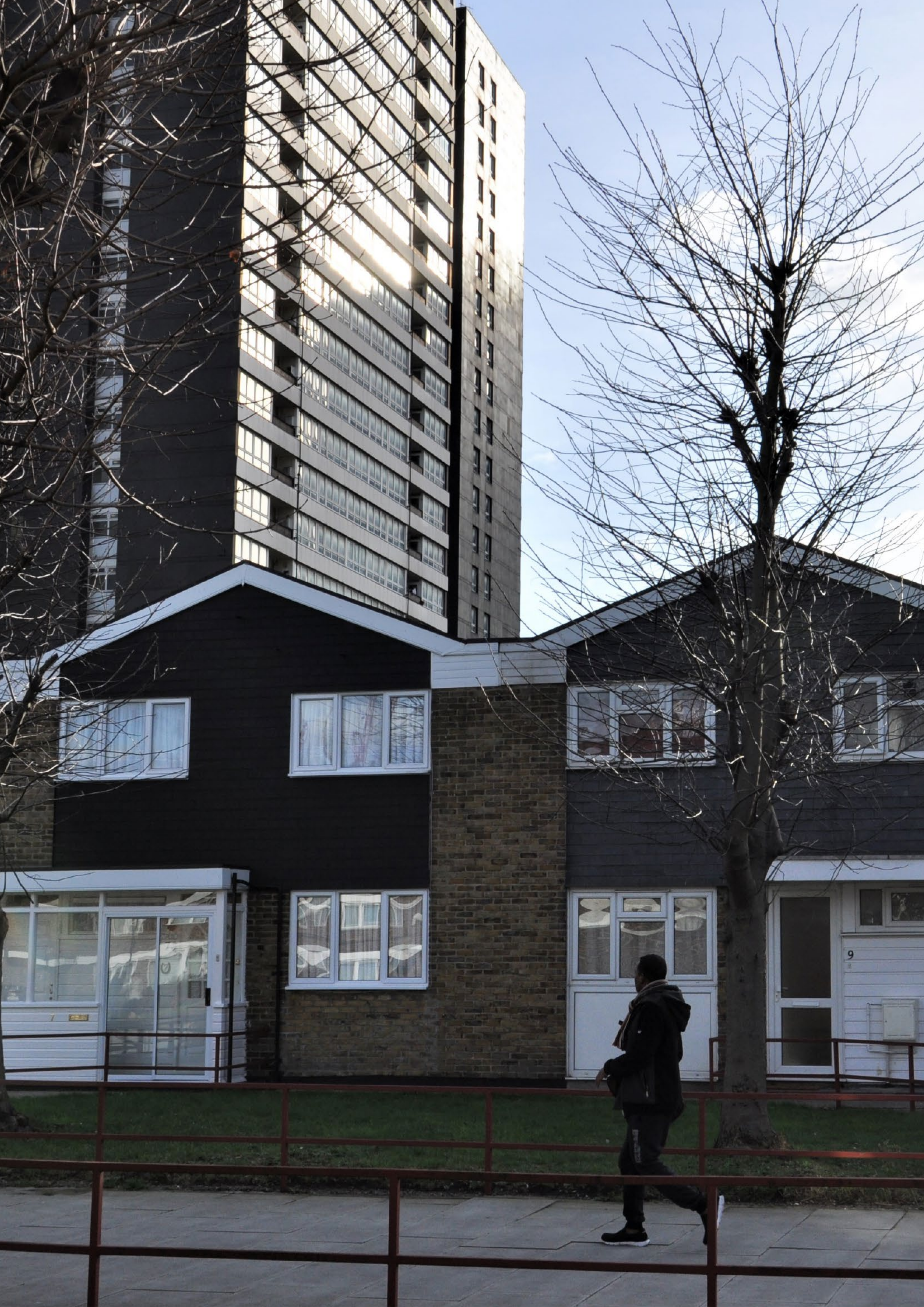
Members of Lambeth People's Audit tried to raise complaints about the council's auditor KPMG. One person went to the PSAA only to be told that complaints about auditors performance did not fall within the PSAA'a remit; another complained to the Institute of Chartered Accountants in England and Wales (ICAEW). The ICAEW initially stated that complaints about failures of service or maladministration by KPMG should be directed to the PSAA. However, as the PSAA had checked KPMG's response before it was issued

to Lambeth People's Audit, the resident argued that "any complaint I made to the PSAA would mean them effectively investigating themselves". The ICAEW have now been asked to consider whether KPMG's performance is a breach of the ICAEW's code of ethics. The matter had not been resolved at the time of writing – however, it seems that even where any complaints procedure is available, it will narrowly concern auditors' professional conduct rather than wider concerns about their work and powers.

The inability to take further action when the auditor had not investigated the matter properly was seen to undermine the scrutiny function of the legislation and underlines the wider failings of what should be a powerful accountability mechanism. As one objector put it:

> *"It is a massive problem that they can give a really vague response and tell you you have to pay a huge sum of money [to take the issue further]. And you have no right to complain, so it means you do not really have the full right as a citizen that you should have, so you have the right to scrutinise and object, but if what you get is a half-hearted response that is really expensive and that does not take you seriously. All that means you do not really have that right."*





4. CONCLUSION

At a Public Accounts Committee hearing on Local Government, Governance and Accountability in March 2019,[1] Chair of the Local Government Association, Lord Porter, made the bold claim that there was very little to be concerned about in relation to accountability in local government. Given the wide access the public to information, the fact that residents were not complaining was clearly evidence that nothing was wrong:

> *"…if you are bothered about your council wasting your money, you can check everything they spend… If the public have access to the information they need to hold us to account and they choose not to do anything with it, I think it is fairly safe to take a view that they are more or less content with what is going on."*

The findings presented in this report show that this is far from the case. Even though in theory, the LAA Act gives the public rights to inspect council accounts, ask questions about them and file objections on issues they believe should be investigated, in practice these rights are not fit for purpose. Councils and auditors alike obstruct their use. In many cases the auditors did not even respond to questions or objections – and where they did, auditors' investigations were very delayed, of poor quality and did not result in further action being taken to challenge councils' decisions. The right to object exists solely at the discretion of auditors who have no definition of the public interest, act without proper external regulation or oversight and frequently take no action where there are clear conflicts of interest. The existence of meaningful inspection rights in turn depends entirely on the professionalism, resources and attitude of the council, who act as gatekeepers to the information necessary to proceed with using the objection rights to hold councils to account.

The people we spoke to who had tried to engage with the LAA Act described hostility from the councils facing scrutiny.

> *"There is a kind of bunker mentality. It is a skewed and narrow view of engagement. It is incredible. I don't think people realise…as soon as you start to raise issues with them, they try to discredit those asking questions. They get into nasty stuff."*

Objectors who tried in vain to get the auditor to take action on their concerns questioned the very functioning of the local audit sector:

> *"Who the hell are these auditors, one of the largest firms in the country – if not the world. They have these incredible resources, and this is an indictment on a system, which is it's not just privatised, but it seems to operate with impunity."*

> *"I think it is really clear that there is too much concentration of power in the audit sector, this goes for the public and the private sector being audited. Because they can do what they want, and they will still get contracts."*

We have also evidenced the fact that residents' concerns are significant enough that behind the scenes they are being taken seriously and acted upon by regulators, auditors and central government. Yet, there is a persistent refusal to intervene in any way that would open these concerns out into a public conversation – such as publishing public interest reports that have to be debated in a council meeting or referrals to the high court. Even when residents' objections have been key for raising the alarm on issues that have gone on to require intervention, such as LOBO loans and PFI they are publicly ignored.

By replacing a public audit body – the Audit Commission – with private audit firms in England, the coalition government paved the way to allow the profit motive to dictate how the public interest is defined and served in local government. The result of this process has seen the widespread delay of investigations into objections; audit firms maximising their fee income whilst whitewashing local residents and elected members' concerns. The auditors have invariably failed to publish their findings and blocked all requests for a high court referral, even regarding toxic loans which could have seen multiple authorities pushed into bankruptcy. These loans were also assessed as the highest risk rating in the NAO documents disclosed under FOI.[2]

This documented failure to identify and serve the public interest calls into question the decision to grant private audit firms a monopoly on local government audit. Auditors, who are neither lawyers nor experts in public finance, have been given quasi-judicial powers to act as gatekeepers to public scrutiny. They act as barriers to accountability by restricting flow of information and separating financial issues from the context in which those decisions take place.

Although there have been separate inquiries and reports on different aspects of the post Audit Commission landscape, these have not constituted a comprehensive

1 Public Accounts Committee, 27 March 2019, Oral evidence: Local Government Governance and Accountability, HC 1738

2 Risk Rating in Local Government Technical Issues Logs November 2016 - February 2017: disclosed in response to Shepway Vox Team FOI, 2018

Even when residents' objections have been key for raising the alarm on issues that have gone on to require intervention, such as LOBO loans and PFI they are publicly ignored.

parliamentary review of the LAA Act. The narrow scope of the Redmond Review report is indicative of a lack of interest and commitment to understanding the wide-reaching implications of the privatisation of local government audit in England and illustrates the denial about the accountability vacuum that has been created.

The cumulative effect of the various behaviours and tactics by auditors described in this report have been to emphasise the relative lack of power and resource of the objectors and to isolate them from any collective efforts to coordinate and support uses of these rights. We believe this is a deliberate result of the privatisation of audit that was brought in under the pretext of austerity, together with its individualising narrative of the 'Big Society' and 'armchair auditors'.

Our work arises from a tradition of citizen audit, which both challenges the armchair auditor narrative and shows its limits. As citizen auditors, we do not only seek transparency and access to information. We also seek to create new, democratic notions of accountability, create processes that can facilitate democratic participation and claim ownership over the information we access and produce.

We have found the current legislation hinders rather than helps these efforts. It blocks any attempts by citizens to participate in local government audit and to hold both councils and auditors accountable for failing to manage and spend resources responsibly and in the public interest. In fact, it obscures the whole concept of public interest and leaves no place for the public to define it.

Since the 1980s and increasingly since the coalition government came into power in 2010, UK government policy has been guided by an ideology that has sought to shrink the state and replace its responsibilities with profit-driven private interests and the voluntary sector. Successive governments have created market opportunities for private companies to profit from functions that were previously public. This is the context in which the abolition of the Audit Commission and privatisation of local government audit has to be seen, and the experiences described in this report demonstrate the extent to which the LAA Act works to absolve the state of responsibility for meaningful accountability.

Eric Pickles' army of armchair auditors is part of the Big Society narrative, creating an illusion of public participation to legitimise the abolition of any public scrutiny body.

However, the smokescreen of the Big Society quickly dissolves when people try to make use of the public rights in the Act. Currently, the LAA Act and its interpretation by auditors and local authorities restrict these efforts by delaying and deferring responses to residents' requests.

Whilst it was unrealistic from the start because residents lack the resources, the expectation that armchair auditors could deliver a meaningful scrutiny function is further impeded by restricting information sharing. The sustained effort required to question, scrutinise and challenge is better suited to collective endeavour: not individuals sitting in their armchairs, but by communities of citizens comparing notes and learning from one another. Although the Covid-19 pandemic has taught us ways to organise together despite being physically separated, people need to be able to share resources and learn from one another in order to effectively challenge financial decisions in their local authorities. The experiences presented in this report show that current audit practices create a context where this is actively prevented from happening.

The recent Redmond Review into local government audit in England drew attention to 'coordinated' objections as if this was something negative. The review explicitly referred to the objections we have been discussing here in the following way (our emphasis):

> *"Some local residents have specific issues with their local authority's expenditure on one or more items and raise objections on the same matter every year. The second type of objection is where special interest campaigns <u>have tried to get local residents to object</u> to the same item in accounts across a number of local authorities. This type of objection has been made in relation to PFIs and Lender Option Borrower Option loans (LOBOs).. "*

Rather than seeing objections as a positive sign of public engagement with an accountability process, those who support residents to try and hold their councils to account are characterised as coercing people into submitting objections. When people are put off engaging with the law because it is too complicated, this is taken as evidence that nothing is wrong, yet if people act collectively to educate themselves to engage with the legislation, they are seen as an obstruction to things continuing as usual. One resident said:

> *"I live here, pay my council tax and try to be a good citizen and I'm trying to help. But it is not seen as help. You are just seen as troublemakers."*

The authors of this report have made submissions to several inquiries: Communities and Local Government Committee's Overview and Scrutiny Inquiry in 2017 and more recently, the Redmond Review as well as the NAO's consultation on the new Code of Audit Practice, based on our extensive experience using the LAA Act. Following this consultation,

Most of the serious issues we have raised have been ignored and there is an urgent need for wholesale reform in public sector audit.

the new Code of Audit Practice, published in 2020, has now introduced a recommended time limit for responding to objections, which is an important step towards patching some of the flaws of the legislation. However, most of the serious issues we have raised have been ignored and there is an urgent need for wholesale reform in public sector audit.

The crisis in council finances is well-documented, even if auditors have lacked the professional scepticism to proactively uncover problems, or act upon them when brought to their attention.

In October 2020, auditor Grant Thornton issued a public interest report as a response to the serious mismanagement of Croydon Council's finances,[3] quickly followed by a section 114 notice by the council, effectively declaring bankruptcy. This rare intervention is indicative of the serious risks facing local government at the moment: over the course of 2020, the government's £9.1bn injection of funds into councils averted, in the words of the NAO,[4] a "system-wide financial failure". After a decade of funding cuts and reforms that have not made clear how the local government sector should finance itself, it is no wonder that council finances are hitting a dead end. Yet auditors are only now starting to wake up to issuing reports in the public interest in response to financial and governance failures that have been building up: in 2020, Nottingham City Council narrowly avoided bankruptcy through government support following the collapse of its energy company – subject to a public interest report in August that year.[5] In January 2021, KPMG published a public interest report into loans to a football stadium by Northamptonshire Borough Council.[6] Northamptonshire County Council issued a Section 114 notice in 2018 and both authorities have since been abolished in a restructuring. These are all reports where the auditor has used their powers to issue them – there has been no such increase in acting upon resident concerns. As well as the three most recent reports mentioned here, there have been only four others in the seven years since the LAA Act came into force and only one of these (City of York, 2016)[7] was in response to an issue raised in a public objection.

As the pandemic deepens the financial hardship of already underfunded – and too often mismanaged – local authorities, it is more important than ever that citizen auditors are valued and residents' concerns are acted upon. The private audit firms that took over after the abolition of the Audit Commission have proven themselves unable to define or serve the public interest, with neither residents nor councils satisfied with their performance. It is time to rethink local authority audit.

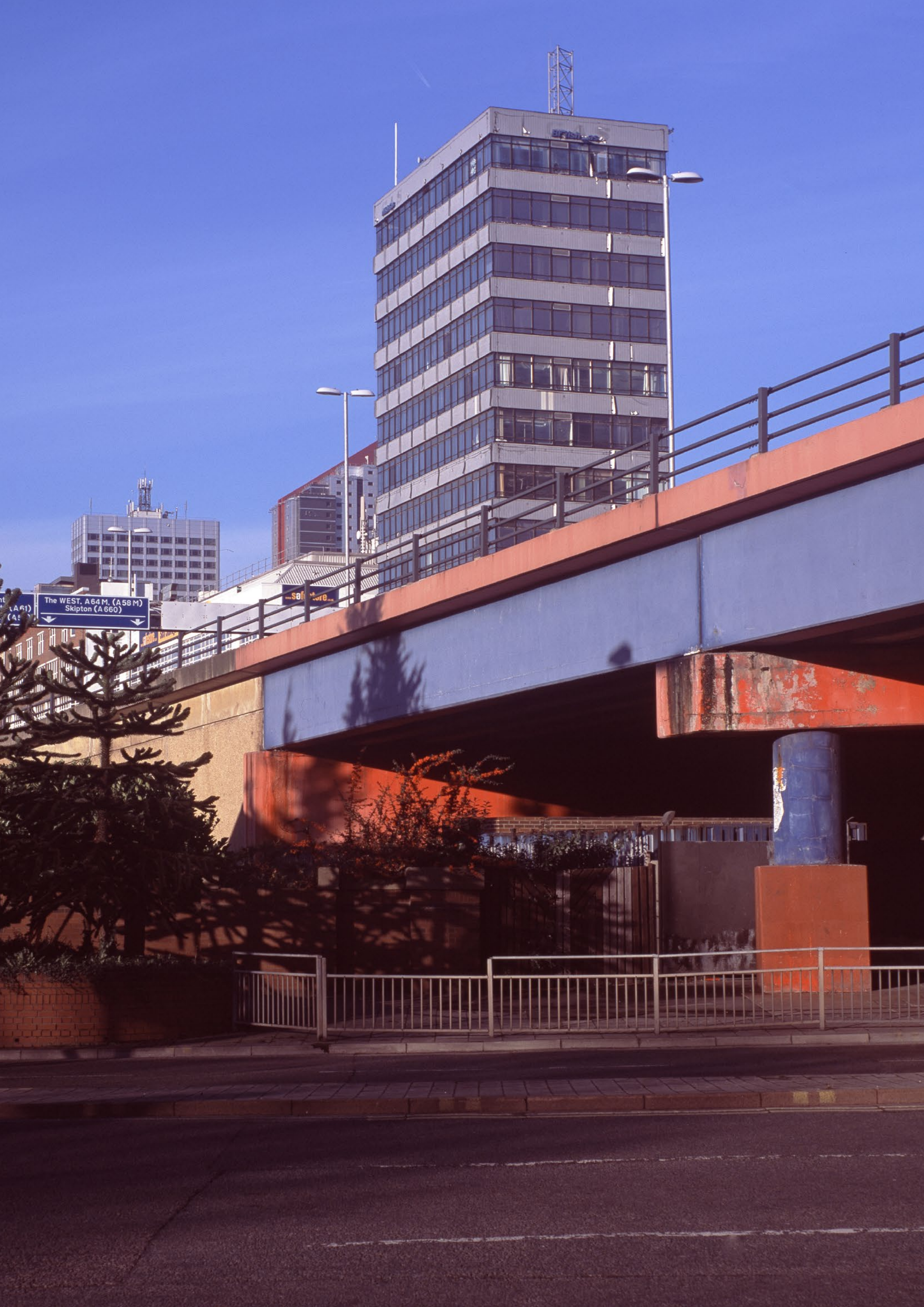
3 Grant Thornton, 23 Oct 2020, ' London Borough of Croydon: Report in the Public Interest concerning the Council's financial position and related governance arrangements'

4 NAO, 10 March 2021, 'Local Government Finance in the Pandemic'

5 Public Finance, 13 Aug 2020, 'Finance director 'raised concerns over struggling energy firm''

6 Public Finance, 28 Jan 2021, 'Auditor finds 'significant failures' over stadium loans'

7 Mazars, February 2016 'Public Interest Report Governance issues in relation to remuneration of Council officers for work as Directors of City of York Trading Ltd'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5. RECOMMENDATIONS

About auditors and their work

- Private companies should not audit local government. We also recommend the following immediate steps to mitigate the current problems with local government audit and accountability:

Transparency about work undertaken:

- All investigations by the auditor, whether they result in further action or not, should be published in an accessible format (i.e. it must be searchable) on the website of the council within a month of completing the investigation
- Any actions short of a public interest report i.e. recommendations (statutory or not) should be published and a public meeting held within a specified timeframe
- Information about whether there are pending objections, their subject matter and status should be published on council's website and kept up to date
- As part of their final response to an objection, auditors should produce a list of documents they have requested and received from the council as part of their investigation

Avoiding auditors' conflicts of interest:

- Auditors should not handle objections where they have, or have had, involvement in any contracts or professional involvement with a company whose contracts with the council are being scrutinised by the objection
- Auditors should not undertake other work (e.g. consultancy) for the same council they are auditing

Changes to legislation and code of practice

Criteria for public interest reports:

- 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 affecting the auditors' ability to sign off on the councils accounts.

Extending the rights:

- The public inspection and objection rights in Part 5 of the LAA Act (and Scottish equivalent) should be extended to cover NHS Trusts and NHS Foundation Trusts

Schedule 11:

- Auditors should be prevented from applying Schedule 11 of the LAA Act to any communications with objectors

Response times:

- Recently introduced guidance on time limits on auditors' response should be effectively monitored and enforced, with financial sanctions for late responses which cannot be passed onto local authorities
- Objectors should be given two months to respond to a provisional view
- Authorities should provide information requested within the inspection time window. If they provide information late, residents' right to submit objections should then be extended by a period of not less than ten working days from the date of receipt.
- An appeals process should be available for the breach of time limits, both in relation to auditors and authorities

Regulation:

- A single oversight body specifically for public audit should be created and should be accountable to the public. This body 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.

Appeals and complaints:

- 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
- Inspection rights under the LAA Act should come under the remit of any new supervisory body for public audit, who would be responsible for monitoring and enforcing the rights in order for them to function alongside the Act's objection rights
- Legal assistance and/or financial support for taking an appeal to the high court should be introduced
- The period within which objectors are able to challenge a decision notice to the high court should be extended from one to three months

Reporting:

- A central depository of all objections should be created and updated on an annual basis, including a centralised database of public interest reports. Auditors and local authorities should also have to publish these figures annually for the relevant authorities.
- Auditors should provide more detailed reports of their objection handling to the local government audit oversight body and planned audit regulator ARGA, including time taken and fee charged. This data should be made publicly available.
- Councils to publish the number of inspection requests received and responded to, including time taken to respond
- Local authority Audit and Scrutiny and Oversight Committees (or similar) should have clear remit to monitor authorities' compliance with inspection requests on an annual basis

Facilitating greater use of the Act

- Information should be made accessible in whatever format the requester needs it, similar to Freedom of Information requests. All PDFs should be published in an electronically searchable format.
- Guidance should be made available to local authorities on inspection rights to specifically distinguish LAA Act rights from the rights under the FOI Act
- In order to facilitate greater use of the LAA Act in a way that recognises the value of collective uses, a publicly funded bespoke web tool for managing inspection requests and objections should be created

Review and rethink public audit

- The Local Audit and Accountability Act should be urgently reviewed in light of ongoing failings of the audit sector
- A fundamental reassessment of public audit should take place, with civil society central to that process
- Public interest should be clearly defined as part of the steps to review the legislation and improve audit processes

Research for ACTION

Research for Action is a workers' co-operative producing research to support social, economic and environmental justice. Through in-depth investigations into vested interests and corporate power as well as researching alternative economic models, Research for Action produces informative, reliable and accessible material for the general public, the media, civil society and grassroots organisations to help strengthen their activities in bringing about long lasting change.

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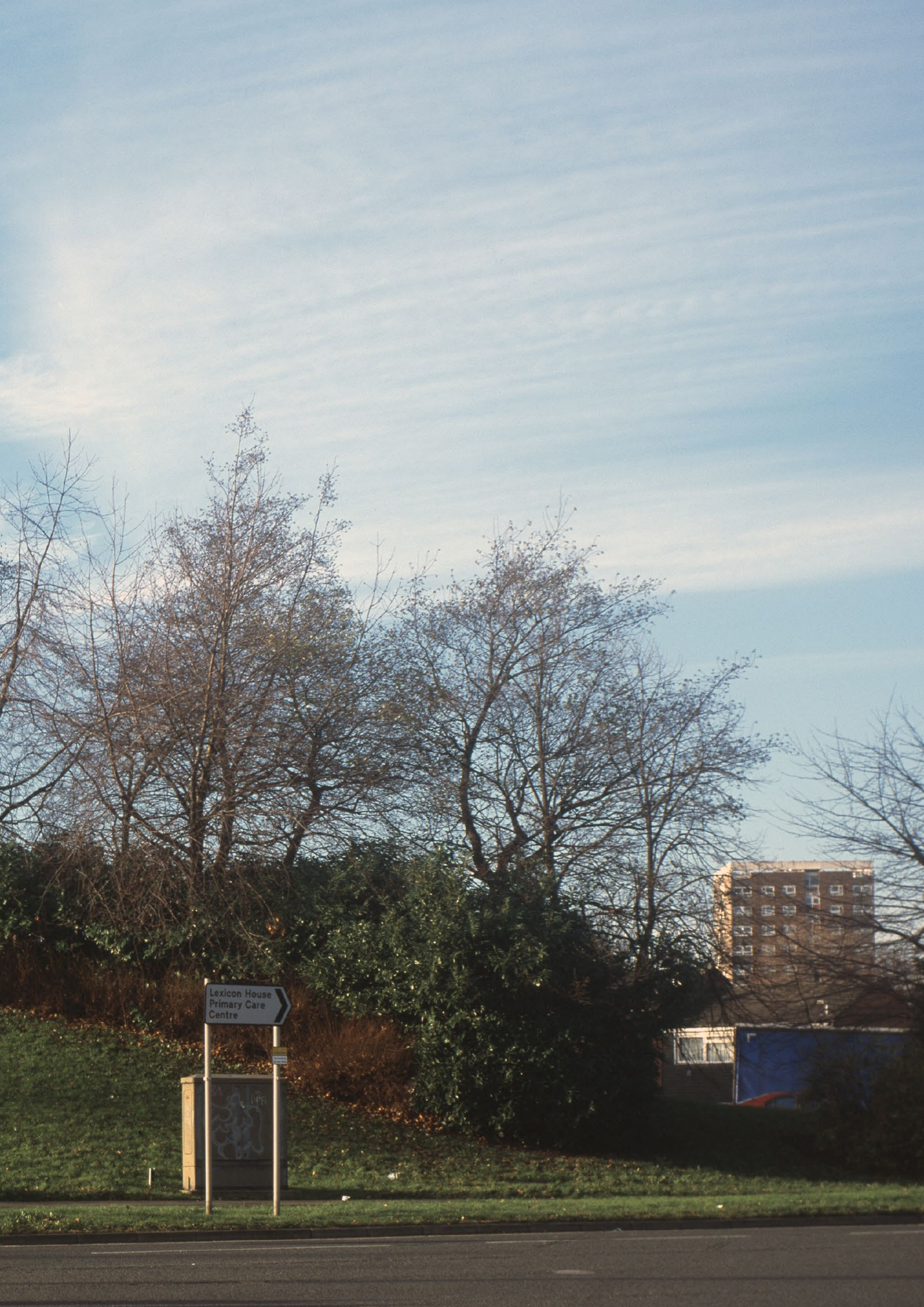
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