



Department for Levelling Up,
Housing & Communities

Dame Meg Hillier MP
Chair of the Public Accounts Committee
Via Email

Jeremy Pocklington CB
Permanent Secretary

***Department for Levelling Up,
Housing and Communities***

4th Floor, Fry Building
2 Marsham Street
London SW1P 4DF

www.gov.uk/dluhc

Tel: 0303 444 2785
Email: PSPerm.Sec@levellingup.gov.uk

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Dear Dame Meg,

Thank you for your letter of 30 August following my evidence to the committee on 6 July. I am writing to respond specifically to the observations set out in your letter concerning local government finance and local audit.

LOCAL GOVERNMENT FINANCE

During the proceedings on 6 July, the Committee asked how the Department currently incorporates population data in the local government finance funding methodology. Committee members were also interested in the release of Census 2021 and how the changes in population data would be reflected in the local government finance system.

The local government finance funding system is funded through formula grant and local taxation. The Settlement Funding Assessment (SFA) is a key component of determining allocations within the Local Government Finance Settlement (LGFS), accounting for £14 billion in central government resources this year. The formulas within SFA contain various population data including 2012 Office for National Statistics projected population levels for 2013. Population data is just one of many factors which influence the SFA, alongside service needs, deprivation, local taxation, transitional protections, and a central allocation for other costs.

I understand that the recent Census 2021 population data produced by the Office for National Statistics (ONS) could be a cause for concern for some councils where the recorded resident population is lower compared to Census 2011. Some councils have written to the Department stating their view that lockdown artificially depressed the number of people, including students and economic migrants.

The census is designed to capture the position and characteristics of the population on that day. In that sense, it provides the most authoritative and detailed picture of England and Wales's population available to us. The Department, and the ONS, is clear that this data will therefore inevitably be a product of the moment in time it was taken, and the pandemic is likely to have had an impact, some temporary, some longer lasting. The ONS has announced that they are looking closely at the drivers of the changes since 2011 and they have said this could lead to further statistical releases in the future.

In terms of factoring in the movement of people during the COVID-19 pandemic, and considering the use of the 2021 Census date, the Government will therefore carefully consider both current

and future releases by the ONS before deciding how they could factor into future reforms to the funding system. The new census data will not be used as part of the Local Government Finance Settlement this year, and we will of course consult closely with local partners before implementing any substantial changes to the system and give councils time to plan. This is particularly important where this entails changes in funding allocations.

Following on from the Autumn Statement, the Government will work to publish the Provisional LGFS as soon as possible. We will release a policy statement in early December providing forward notice of the measures which will be included in the provisional Settlement and maintained into 2024/25. It is our intention that this will support LAs' budget setting process ahead of the publication of the provisional LGFS.

LOCAL AUDIT

System leadership

In your letter you asked that I clarify the Department's view on what system leadership of local audit should comprise. A key insight from Sir Tony Redmond's [Local authority financial reporting and external audit: independent review](#) was that the fragmentation of the existing local audit structure impeded the system's ability to respond to challenges. Sir Tony recommended that local audit needed a system leader to provide 'clarity of purpose, consistency and public accountability'. Although we did not agree that a new body should be established to fulfil this function, we are in agreement with Sir Tony's overarching principles for a system leader for local audit. We have announced that the Audit, Reporting and Governance Authority (ARGA), the new regulator which the Government intends will replace the Financial Reporting Council (FRC), will assume this role.

Neil Harris commenced his role as the FRC's first Director of Local Audit on 12 September. He has since undertaken a wide range of engagement activity to capture the views and perspectives of key stakeholders in the local audit system. The FRC is now building capacity within a dedicated local audit unit, with shadow system leader arrangements expected to commence in the Spring of next year.

As the committee will be aware the establishment of ARGA as system leader for local audit requires primary legislation. The Government is developing draft legislation that will be published in due course. Meanwhile, we are working closely with the FRC to ensure they are able to fulfil many of the system leader functions prior to the introduction of ARGA.

Since Neil Harris has started in his role, we have worked with the FRC, alongside other stakeholders in local audit, to develop a Memorandum of Understanding (MoU) that will set out the roles and responsibilities that the FRC will assume as shadow system leader. This document will provide the basis for the responsibilities and activities that we believe system leadership should comprise. These include:

- **Leading a coherent and coordinated policy response to challenges arising across the local audit system, working across and between organisations as required:** The system leader will act as a visible leader for local audit, establishing strong relationships with stakeholders across the system to ensure a joined-up approach.
- **Reporting on the local audit system:** We want the system leader to report on the state of the local audit system and to identify trends / risks that are emerging.
- **Leading work to improve competition, bolster capability and market supply:** The system leader will develop a programme to address the long-term challenge of market

sustainability. This will include a workforce strategy, developed in conjunction with audit firms, which will consider the future pipeline of local auditors.

- **Facilitating stronger governance across the local audit framework:** The system leader will support the Appointing Person, ensuring procurement objectives are aligned with the objectives of the wider system, and should foster improved coordination and collaboration across the new framework.
- **Overseeing the entire quality framework for local audit:** The system leader will act as the regulator for local audit, as well as having control of the Code of Audit Practice and associated responsibilities (the Code, currently held by the National Audit Office, requires primary legislation to be transferred so will not be a responsibility of the FRC in their role as shadow system leader).

The Government expects to publish the MoU in January 2023.

Procurement

You also enquired about the recent procurement of audit services for local bodies. The procurement of audit services for the 470 local government, police and fire bodies (99% of bodies eligible for a full audit) was conducted by Public Sector Audit Appointments Ltd (PSAA) over the summer months. PSAA has awarded contracts to six suppliers for the next appointing period spanning 2023/24 to 2027/28. Of these, three are existing suppliers (Grant Thornton, Mazars and Ernst & Young), two are new suppliers (Bishop Fleming and Azets Audit Services) and one is a former supplier that has returned to the market (KPMG). Contracts have been awarded for 99.5% of the audit work detailed in the tender. After taking account of the impact of recent and scheduled local government reorganisations, PSAA has stated that this is sufficient capacity to meet all audit needs.

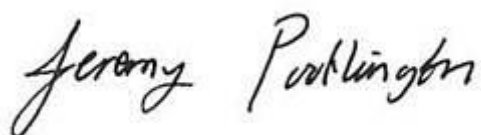
Capacity in the system

Finally, you asked what work is underway to ensure that there is sufficient capacity in the system. Following the [Government's response to the Redmond review](#), we took immediate action to make new regulations to reduce demands on auditors by giving PSAA the ability to standardise fee variations where particular issues had a national or far reaching impact. We also provided £15m of additional funding in 2021/22 to support local bodies to strengthen their financial reporting and meet any new burdens arising from Redmond's recommendations. We followed this with a package of [measures to improve local audit delays](#) in December 2021 which committed to provide a further £45m over the course of the current Spending Review period.

The Government also committed to work on longer-term measures to help stabilise the market and address long-term supply issues. A feature of a strong, resilient market is one that can attract new entrants; the introduction of two new audit firms following the recent procurement is therefore welcomed. To facilitate the realisation of a strengthened market, we are expecting to launch a Local Audit Qualification (LAQ) in the Spring of 2023 and a Technical Advisory Service (TAS) in the Summer of 2023. The TAS will support the capability of qualified auditors by providing an expert service to respond to complex issues. We believe it will be particularly useful to new or challenger firms entering the local audit system who may need additional support with technical queries. In turn, our expectation is that this can encourage more firms to consider entering the market. The LAQ will be a top up for qualified auditors with limited or no experience of local audit who are considering becoming Key Audit Partners. This will provide a new route into local audit and will aid in the formation of a more competitive market between corporate and local audit.

The Government recognises the importance of an effective local audit system and is committed to working with FRC and key partners on a wide range of measures on multiple fronts to address the existing challenges.

Yours sincerely,

A handwritten signature in black ink, reading "Jeremy Pocklington". The script is cursive and fluid, with the first name "Jeremy" and the surname "Pocklington" written in a single line.

JEREMY POCKLINGTON