Ministry of Housing,
Communities &
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Permanent Secretary

Ministry of Housing, Communities & Local Government
2 Marsham Street, London, SW1P 4DF

The Chair
Committee of Public Accounts
House of Commons
London
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15 January 2020

Dear Chair,

RESPONSE TO REPORT ON LOCAL GOVERNMENT GOVERNANCE AND ACCOUNTABILITY

1. Following the Committee's hearing on Local Government Governance and Accountability on the 27 March 2019, I am writing to set out how the Department has implemented recommendations made by the Committee in its subsequent report.

2. The Department has accepted the recommendations of the Committee's report in full, as outlined in the Treasury Minute published in July 2019. In the Treasury Minute, the Department committed to write to the Committee in November 2019 setting out its overall plan for improving its oversight of local government.

3. This letter sets out the plan, and the progress that the Department has made on its related work including its governance evidence base, the Local Authority Governance and Accountability Framework Review Panel, working with other government departments, local authority commercial investments and ventures, and transparency of engagement with the sector.

4. I will write separately in the Spring on recommendations 2 and 5 which have an implementation date in Spring 2020.

The Department's plan for improving its oversight

5. In response to recommendation 1a, the former Secretary of State for Communities, James Brokenshire, wrote to the HCLG Select Committee and to the Local Government Association, in March 2019, setting out our aim to enhance our oversight of the accountability and assurance system for local government. The Department has taken account of the Committee's recommendations in enhancing its oversight and leadership of the accountability and assurance system, which includes local authority governance.

6. The plan for improving the Department's oversight covers both:

a) **The operation of the system as a whole,** where the Department aims to improve our understanding of how the system overall is operating, and to enhance it - in particular by playing a stronger role as system stewards in convening the component parts of the accountability and governance framework

b) **understanding** the **individual local authorities which comprise the sector** and **enhancing** the support available to them.

7. The Department is delivering on the first of these elements by bringing together our partners with responsibility for individual components of the system, in the Local Authority Governance and Accountability Framework Review Panel. This body will be the principal mechanism for gathering the views of key organisations with a national focus on the sector as a whole, and on overseeing the sector

regarding the health of the framework, and will help the Department identify areas where corrective action is required. As the context in which local authorities operate changes, it is necessary to continually assess the framework for governance and accountability to identify if it is still fit for purpose. For that reason, the Panel has been created as an ongoing, rather than a time-limited body. It will not be offering a snapshot view of the system but continually reviewing it and its components, under the leadership of the Department.

8. In respect of the second component, regarding individual authorities, the Department is increasing resources to engage directly with more individual local authorities, to understand better the challenges that local authorities are facing. As a department we are also increasing our engagement with the sector more widely, to better understand what is needed to support improvement in local authorities. The Department has developed closer working arrangements with our partners in other Government departments and will use these relationships to share the knowledge we gain from our increased engagement to build a richer, shared picture of the issues facing individual authorities across the range of their responsibilities. This information informs shared approaches to addressing any challenges. The Department has also included a new requirement in the memorandum of understanding on sector support for improvement with the LGA in 2019/20 that 25% of the grant it provides for improvement support should be spent through external suppliers. This is intended to make the best use of existing specialist expertise and to grow the market for the future.

9. Actions taken since the Committee's report in May include:

- Establishing and holding the first meeting of the Local Authority Governance and Accountability Framework Panel. The Panel was established in September 2019 and further details about its work are provided below.
- Supporting Centre for Public Scrutiny and Localis research on how local authorities can diagnose and reduce the risk of failure in corporate governance. The study was announced in October 2019 and findings and a toolkit for local authorities will be published in May 2020.
- Discussions with colleagues in the sector to inform the government response to the Committee on Standards in Public Life report on ethics in local government.
- Commissioning the independent Redmond review of the local authority financial reporting and audit regime (The review's full terms of reference are available at: https://www.gov.uk/government/publications/review-of-local-authority-financial-reporting-and-external-audit-terms-of-reference).
- Conducting a review into the risks of fraud and corruption in local government procurement
- Having instituted formal monthly meetings with other government departments and extended the scope of the Department's contact, including engagement with: the Department for Education (covering schools funding as well as children's services) and the Department for Health and Social care (covering public health as well as adult social care) on a monthly basis, and quarterly contact with the Department for Culture, Media and Sport (relating to local authority library provision). This is providing a shared view across departments of where authorities are experiencing challenges.

10. As a department we welcome the publication in October of CIPFA's Financial Management Code, which also supports the accountability framework for the sector, which the Framework Panel reviews.

11. The Department's next steps include:

- Publication of response to CSPL report on local government standards (tbc)
- Further consideration of evidence base gaps on sector-wide non-financial governance issues (Framework Panel, early 2020; department, early 2020)
- Publication of review on fraud and corruption
- Completion of the Redmond Review (2020) and government response to it (2020)
- Refreshing our approach to formal data sharing with OGD partners

The Local Authority Governance and Accountability Framework Review Panel

12. In response to recommendation 1c, in September 2019 the Department convened the first meeting of the Local Authority Governance and Accountability Framework Review Panel. The Panel is chaired by the Director General for Local Government and Public Services. The Panel's membership is: National Audit Office, Local Government and Social Care Ombudsman, Local Government Association,

Society of Local Authority Chief Executives, Centre for Public Scrutiny, Chartered Institute of Public Finance and Accountancy, Lawyers in Local Government and the Association of Local Authority Treasurers. Its principle objective is to assess the Framework to determine whether it is fit for purpose. Panel members will represent their organisations by providing feedback on thematic elements of the governance and accountability framework and the assurance model, which the Department will take into account when providing its Accounting Officer assurance advuce. At the Panel's first meeting, in September 2019, Panel members agreed the terms of reference for the Panel. As regards its programme of work, at the first meeting, the Panel agreed to discuss the following themes at future meetings: standards, conduct, probity and organisational culture; data; local government finances; and local audit. The work programme will be reviewed by the Department and the Panel on a regular basis.

13. The second meeting of the Panel, held in December 2019, discussed the themes of conduct, behaviours and culture in local government. The Panel will continue to meet throughout 2020 on a quarterly basis. The Department will keep the Panel's effectiveness under review and shall determine the success of the Panel via the feedback and recommendations it provides to the Accounting Officer for Local Government that must: i) be focussed on achieving practical improvements to the Framework; and ii) be feasible to implement in the medium term. The Panel is operating in a transparent manner, with the minutes of meetings and the terms of reference to be published.

The governance evidence base

14. In response to recommendation 3, effective governance is of course essential for local government, in order to underpin propriety in decision making and effective use of public resources. The new Local Authority Governance and Accountability Framework review panel, in its first meeting, expressed the view that the accountability system is broadly working well.

15. The Department's approach in assessing governance to date has been a risk based one. We have looked in particular at those authorities where there are risks relating to leadership and governance, finances or service delivery, drawing on a range of further sources and triangulating with partners in those cases, Risks have been identified in particular through the Department's comprehensive financial data, and through engagement with partners across government and with the LGA, as well as (to a lesser extent) media reporting.

16. The Department does not maintain a single database of evidence on each LA's governance and performance, and to do so would be a large scale enterprise with a significant resource implication. The Department has reviewed our governance evidence base; this is summarised in the table provided at Annex A. This indicates that the evidence around the financial health of local authorities in particular is strong, underpinning the Department's responsibility for the sector's use of resources. And it shows that the Department is able to triangulate evidence from a range of sources relating to the operation of governance, and performance, in individual authorities. Where issues are identified with how one local authority was calculating its minimum revenue provision, the Department carried out a review of all upper tier local authority accounts and held a conference call with Chartered Institute of Public Finance and Accountancy to identify whether this was one-off behaviour or part of a wider pattern. The Department is now reviewing the scope to amend the capital framework to prevent similar practices in future.

17. As part of the ongoing Post Implementation Review (PIR) of the local authority capital finance framework, the Department has sampled local authority capital strategies to assess how far they are adopting the new approach. Part of the sample was selected on the basis of potential risk factors using government data on capital investment, borrowing and commercial income streams. The Department's findings will be reflected in the PIR report once complete and used to inform future policy development. The Department has identified that over-spending on services for children and young people with special educational needs and disabilities, as part of the DfE Dedicated Schools Grant, was causing a number of authorities to be holding deficits, creating a risk to financial sustainability. The Department undertook a review of the reserves and deficit position for all affected local authorities to identify both systematic and individual local authority risks. The Department is now working with Department for Education, CIPFA and the sector to address the issue.

18. The review of the Department's governance evidence base confirms findings in the PAC's report, and identifies some gaps, in particular relating to the non-financial aspects of governance. This will be

discussed with the Framework Panel. Governance evidence is probably the most difficult category of evidence because it is often qualitative and subjective (unlike e.g. financial indicators or Ofsted inspection outcomes). As an illustration of the challenge, an examination of committee papers from a local authorities' overview and scrutiny function will expose what issues the committee is examining, but will not say whether the organisation's culture welcomes and responds to robust challenge and how ready officers are to give 'bad news'. There are a number of options for enabling the sector's professionals to offer an honest assessment of the health of these aspects of the system. One is (as the NAO did) to survey the relevant groups of officers and elected members – the statutory officers; auditors; chairs of overview and scrutiny committees. Another approach would be to develop reference groups for each of these categories, such as the Department has already developed for monitoring officers – an option which has the benefit of being able to draw out more complex qualitative evidence, but may not have the same coverage across the sector. A third would be to require formal returns from all individuals in these groups across the sector.

19. As the Department develops views on how best to strengthen our governance evidence, it will take into account the views of the Framework Panel, and the findings and recommendations of the Redmond review of audit on this issue. It is important to avoid prejudging the outcome of the review. The Department will also weigh cost and sector views of proposed individual measures, as well as the degree to which options provide comprehensive coverage of the sector and enable in-depth consideration of the issues.

20. The Local Authority Governance and Accountability Framework Review Panel is adopting a thematic approach, scrutinising individual parts of the Accountability Framework, and will inform the Department of what further evidence may be required to provide assurance that it remains effective. Through its work with local areas experiencing challenges, the Department recognises that the quality of leadership and organisational culture is particularly significant in shaping the effectiveness of organisational governance. In the light of the gaps in the evidence base referred to above and recognising the particular and distinct roles played by the three statutory officers with a governance remit, from its next meeting, the Panel will include representation from Monitoring Officers, through Lawyers in Local Government, as well as Heads of Paid Service and Section 151 Officers and through SOLACE, CIPFA and the Association of Local Authority Treasurers. The impact of organisational culture will be one of the Panel's first themes of examination. The Department will ask the Panel to form a view on what qualitative, rather than just quantitative, evidence is required to assess the health of local governance, taking into account the view of the statutory officer groups. This has been included to focus on the evidence base within the Panel's terms of reference (see below).

21. The Department is also supporting the Centre for Public Scrutiny/Localis independent research into enhancing councils' understanding of how to diagnose and reduce the risk of failure in corporate governance. This will identify key indicators for the Department, and also enable individual local authorities to diagnose governance strengths and weaknesses.

Publication of information and learning following formal interventions

22. In response to recommendation 5b, as was explained in the response to the Committee's recommendation (5b), formal, or statutory, interventions are highly transparent. The powers are set out in sections 10 to 15 of the Local Government Act 1999. Best value inspections, which seek to establish the evidence base for a statutory intervention, are normally announced to Parliament and the resulting report is published. Any decision to intervene under best value powers is subject to formal consultation and parliamentary debate. Commissioners' reports are published regularly during the intervention together with the Secretary of State's responses. The decision to end an intervention is subject to similar rigorous scrutiny, including a consultation process.

23. The Department is aware that learning from the steps taken by Commissioners to improve local authorities and restore their compliance with the best value duty may be useful for others in the sector, who are responding to less serious challenges. The Department published the lessons learned review by Rotherham Commissioners on 18 September 2019. To further increase information on interventions, the Department will publish a short guide for local authorities on intervention. Two further "lessons learnt" documents (on local authority financial controls and overall culture) are also in the pipeline. These draw on the experiences of local authorities, best value inspectors and Commissioners

involved in intervention and are designed to help other local authorities identify the signs that may not be within in their financial controls and/or overall culture.

Work with other government departments on service sustainability

24. In its response to recommendation 1b the Department referred to its letter of 19th December 2018 regarding the Financial Sustainability of Local Authorities, in which it outlined its plans to engage with other government departments to understand service sustainability in preparation for the spending round. The objective of this engagement has been to develop a robust evidence base and collective understanding of revenue and capital spending pressures and potential income streams. This work has included regular bilateral engagement with individual government departments, and trilateral engagement with DHSC and DfE to ensure a shared approach to social care. The Department has held a series of cross-Whitehall policy roundtables chaired by the Director and Director General, attended joint roundtables with the sector hosted by the LGA, and conducted joint visits with other departments to individual councils.

Local authority commercial investments

25. In response to recommendation 4, in the Department's role as system steward, we have continued to develop our analysis of potential and emerging risks to the sector created by commercial activity. Specifically, the Department has been working with HM Treasury to monitor available data on borrowing and commercial investment at a local authority and sector levels in order to identify risks to financial sustainability. This work is on-going, and we continue to carefully consider the need for further interventions. We also continue to update estimates of debt servicing costs held by local authorities which relate to commercial investments, which contributes towards our assessment of risks associated with financial exposure to commercial activity.

26. The Department is also working to finalise the post implementation review of the updated guidance to understand how local authorities have responded to recent changes that were made in 2018, and to evaluate the effectiveness of the framework. Once the review has been concluded, the Department will begin to consider how those findings might contribute to the future policy development of the current framework.

27. In addition, The Chartered Institute of Public Finance and Accountancy continues to support the work of the Department to further ensure that the capital framework is appropriately understood and implemented across the sector. In consultation with the Department and other stakeholders, CIPFA has developed new guidance for local authorities on prudent property investment purchases which is anticipated to be published in November. The guidance will set out that local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed.

I hope that the Committee finds this letter helpful.

MELANIE DAWES

Annex A: The Governance Evidence Base – current and forthcoming evidence

Type of information *What is this evidence of?*	**Evidence Source** *What is the source for this information?*	**Universal or partial coverage?** *Is there data on all local authorities, or only some?*	**Individual authority/ sector-wide analysis/ both?** *Does the data enable conclusions to be drawn about individual authorities, or the sector as a whole?*	**Currently Available? (Y/N)** *Is the data currently available?*
LA finances	LA financial data returns – income, expenditure, reserves, capital	universal	both	Y
Financial management and governance and value for money opinion	LA Audit outcomes	universal	both	Y
Assessment of education services	Ofsted inspection reports	universal	both	Y
Assessment of adult social care systems	Care Quality Commission reports, e.g. System Reviews	partial	individual	Y
Information on LA / sector-wide concerns	Local Government and Social Care Ombudsman reports	universal	individual	Y
Issues affecting leadership, governance, performance in individual councils/sector-wide concerns	Sector intelligence from the LGA regional Principal Advisors	universal	individual	Y
Issues affecting service delivery / wider LA performance in individual councils	Sector intelligence from other Government departments and commissioned reports may cover both service-specific matters and issues relating to a council as a whole	universal	individual	Y
Concerns relating to individual LA performance/governance	Correspondence received from local councillors, Members of Parliament and members of the public.	partial	individual	Y
Activity of individual councils/committees	Data published on local authority websites	Universal	individual	Y
Activity of individual councils/committees	Media reports	universal	individual	Y
Views of operation of governance and accountability framework relating to Monitoring Officer function in particular	Monitoring Officers reference group	partial	sector	Y

Type of information *What is this evidence of?*	Evidence Source *What is the source for this information?*	Universal or partial coverage? *Is there data on all local authorities, or only some?*	Individual authority/ sector-wide analysis/ both? *Does the data enable conclusions to be drawn about individual authorities, or the sector as a whole?*	Currently Available? (Y/N) *Is the data currently available?*
Survey of sector governance	National Audit Office 2019 report on local authority governance; PAC 2019 report on local authority governance	partial	sector	Y
Resident views of quality of local authority governance and service delivery	LGA resident satisfaction survey	universal	sector	Y
Risk of fraud and corruption in local government procurement	review into the risks of fraud and corruption in local government procurement, with case studies	universal (but case study component partial)	sector	N (review to be published later this year)
Evidence of operation of governance	CfPS/Localis study	partial (study to be based on case studies, but also take account of wider views)	tbc	N (study to be carried out in 2020)
Evidence on functioning of audit regime	Redmond review of audit	universal	sector	N (review to be published 2020)
Evidence of quality of LA whistleblowing policies	LA whistleblowing policy documents	universal	individual (separate analysis required to enable qualitative, sector wide view)	Y