

<b>Item No.</b> 8	<b>Classification:</b> Open	<b>Date:</b> 2 June 2021	<b>Meeting Name:</b> Audit, Governance and Standards Committee
<b>Report title:</b>		Public Interest reports	
<b>Ward(s) or groups affected:</b>		All	
<b>From:</b>		Strategic Director of Finance and Governance	

## RECOMMENDATION

1. That the audit, governance and standards committee note the report and acknowledge the importance of compliance against the CIPFA Financial Management (FM) Code.

## BACKGROUND INFORMATION

2. Under the Local Audit and Accountability Act 2014, it is a statutory requirement of the external auditor to issue a Public Interest Report (PIR) when a significant matter comes to their notice which they believe the council should consider or the public should know about i.e., it is in the public interest to know about.
3. Grant Thornton (GT) have published a report ‘Lessons from recent Public Interest Reports’<sup>1</sup> summarising the findings from the Public Interest Reports (PIRs) at Nottingham City Council (August 2020), the London Borough of Croydon (October 2020) and Northampton Borough Council (January 2021), to illustrate the importance of the way governance operates in local authorities and of the critical importance of scrutiny and challenge.
4. The GT report suggests that there are three key areas where lessons can be learnt from these PIRs:
  - The context of local government in a Covid-19 world;
  - Governance, scrutiny and culture;
  - Council leadership.
5. It also makes recommendations for councils to as to how these governance weaknesses can be avoided.
6. This report draws together the main points of interest from both the GT and PIRs in order to assess and reflect on the importance of governance as a means of avoiding catastrophic failure.

## LOCAL GOVERNMENT IN A COVID-19 WORLD

7. Reductions in central government grant and extra demand for services has

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<sup>1</sup> Grant Thornton ‘Lessons from recent Public Interest Reports’ (2021)

meant that councils have had to make considerable savings as well as draw on new income sources. The GT report suggests that the unexpected shock of the Covid-19 pandemic exacerbated the financial challenges faced by local government in 2020-21 which will likely add to the overall funding gap for local councils.

8. The GT report proposes that this additional financial pressure, has for some councils, exposed chronic financial instability and for others has exposed insufficient reserves. But for those councils that have been able to manage central government grant reductions whilst simultaneously maintaining adequate reserves have been in a significantly better position to manage the financial impact of an unexpected event, the Covid-19 pandemic.
9. External auditors in the London Borough of Croydon issued a PIR as the council had significant issues relating to its financial sustainability due mainly to overspends of £39m over 3 years in children's and adult social care, low levels of reserves and inadequate plans to close the widening budget gap. The external auditors had identified these concerns relating to the council's financial sustainability in 2017/18 and raised recommendations for improvements, but these had not been addressed. A budget gap of £65m was identified in 2020-21, together with £21m of in-year savings but the report to cabinet failed to mention that this was higher than available reserves. Grant Thornton concluded that a key indicator of sound financial management and governance was around maintaining an adequate level of reserves.

## **GOVERNANCE, SCRUTINY AND CULTURE**

10. The GT report stated that the quality of scrutiny varied considerably between councils and that where PIRs have been issued, the level and depth of challenge was nowhere near strong enough and concluded that the measure of the quality of scrutiny should be to ensure that council policies are open to proper challenge and focus. The PIR at the LB of Croydon stated that there insufficient challenge from members on the financial risks in the budget and the deliverability of the savings plan. The council's governance over the budget setting and monitoring again had not been good enough.
11. Nottingham City Council set up a Robin Hood Energy company (RHE) to tackle fuel poverty. But despite the company's deteriorating finances, and losses of £23m, the council continued to make additional loans. The main conclusion from the PIR was that the council did not have in place strong enough governance arrangements, there was a lack of clarity of roles within the governance structure and the arrangements did not establish an appropriate and consistent balance between holding the company to account and allowing the company freedom to manage. In addition, there was a lack of commercial expertise at non-executive Board level and insufficient safeguards built into the policy objective to enable challenge and manage risk.
12. Croydon also established a number of companies including wholly owned and part owned companies. The council had increased the level of borrowing - £545m in 3 years- and used the borrowing to invest in companies and purchase

investment properties. Brick by Brick Croydon Ltd (Brick by Brick) was set up as a limited company, with the council being the sole shareholder to deliver housing development aimed to address the shortage of housing. The council had lent over £200m to the company but had not received any loan repayments. The council's savings plan had included a dividend of £3m but again no dividends had been received. £14m of interest and £110m of loan payments was due by the report date but none had been made. The PIR states that council's governance and oversight of the companies showed insufficient rigor and control. Despite heavy investment from the council, there was no significant return, and there appeared to be a collective corporate blindness to the seriousness of the financial position.

13. Northampton Borough Council made substantial loans (over £15m) to Northampton Town Football Club to redevelop the stadium and create a new range of facilities including a hotel, gym and new homes and offices. But during the project, works and payments to contractors ceased twice due to a dispute between the developer and the football club. Loan repayments started to be late and then stopped altogether. The PIR stated that there was very poor decision making based on inadequate reports leading to public money being lost. There was an inadequate assessment of whether the financial projections put forward by the football club were reasonable. It demonstrated the need for careful thought, independent advice and monitoring in making such decisions on a transaction which was significant and unusual. There was a near complete lack of an approved business case and documented risk management and proper governance process followed.

## **COUNCIL LEADERSHIP**

14. In councils where PIRs were issued, Grant Thornton concludes that auditors identified aspects of political culture that were not receptive to challenge, scrutiny or different perspectives. Having an open culture which encourages challenge and criticism, listens to opposition parties and holds its leaders and officers to account for their actions significantly reduces the risk of catastrophic failure. Adverse outcomes have been allowed to happen where political objectives without challenge have taken place with a failure to conduct due diligence for investing and lending to third parties, however important they are to the local community.

## **GRANT THORNTON- RECOMMENDATIONS FOR COUNCILS**

15. The GT report concludes that important lessons can be learnt from these public interest reports and recommends that councils consider their compliance against the CIPFA Financial Management (FM) Code, which emphasises the importance of financial sustainability and a clear strategy for maintaining adequate reserves.
16. The report suggests that audit risk assurance arrangements and governance are strengthened and that council members should strive to work collegially in making strategic decisions which in turn, will improve transparency. The report notes that in all cases there was a lack of challenge and scrutiny and

recommends that this is critical to establishing a healthy management culture.

## BACKGROUND DOCUMENTS

Background Papers	Held At	Contact
Public interest reports and Grant Thornton report	Finance and Governance, Second Floor, Tooley Street	Geraldine Chadwick

## APPENDICES

No.	Title
Appendix A	(GT1) Grant Thornton Lessons from Public Interest Reports
Appendix B	(GT1) Nottingham City Council Report concerning the Council's governance arrangements for Robin Hood Energy Ltd
Appendix C	(GT1) London Borough of Croydon Report in the Public Interest concerning the Council's financial position and related governance arrangements
Appendix D	(GT1) Northampton Borough Council: Report in the public interest regarding the Council's loans to Northampton Town Football Club (accounts for the year ended 31 March 2016)

## AUDIT TRAIL

<b>Lead Officer</b>	Duncan Whitfield, Strategic Director of Finance and Governance	
<b>Report Author</b>	Geraldine Chadwick, Interim Technical Accountant.	
<b>Version</b>	Final	
<b>Dated</b>	20 May 2021	
<b>CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER</b>		
<b>Officer Title</b>	<b>Comments Sought</b>	<b>Comments included</b>
Director of Law and Governance	N/A	N/A
Strategic Director of Finance and Governance	N/A	N/A
<b>Cabinet Member</b>	N/A	N/A
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