

Breaking out: public audit's new role in a post-crash world

AN ENGLISH PERSPECTIVE



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Founded in 1904, ACCA has consistently held unique core values: opportunity, diversity, innovation, integrity and accountability. We believe that accountants bring value to economies in all stages of development. We aim to develop capacity in the profession and encourage the adoption of consistent global standards. Our values are aligned to the needs of employers in all sectors and we ensure that, through our qualifications, we prepare accountants for business. We work to open up the profession to people of all backgrounds and remove artificial barriers to entry, ensuring that our qualifications and their delivery meet the diverse needs of trainee professionals and their employers.

We support our 162,000 members and 428,000 students in 173 countries, helping them to develop successful careers in accounting and business, with the skills needed by employers. We work through a network of over 89 offices and centres and more than 8,500 Approved Employers worldwide, who provide high standards of employee learning and development.

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Global Forum for the Public Sector

The Forum leads ACCA's work in finance and accounting issues in the international public sector. It brings together senior figures from central and local government and other state institutions from all over the world. The Forum's agenda covers public financial management, budgeting, accounting, audit, governance and regulation.

This paper explores some of the themes set out in ACCA's 2014 publication *Breaking Out: Public Audit's New Role in a Post-crash World*¹ and relates them to the English context.

The public service landscape has changed dramatically bringing with it new challenges of governance, audit and accountability.

This paper summarises discussions from an ACCA roundtable in Westminster in April 2014, which brought together politicians, contributors from the report, academics, journalists, regulators and auditors from across the country to discuss audit and accountability.

1. <http://www.accaglobal.com/gb/en/technical-activities/technical-resources-search/2014/march/breaking-out.html>

The consequences of the 2008 financial crisis continue to play out around the world but the crisis has spurred fresh thought, especially among public auditors. ACCA's paper *Breaking Out: Public Audit's New Role in a Post-crash World* (February 2014) has brought together some of this new thinking; contributors from Bhutan to Scotland have reflected on the role of public audit in a fast changing landscape.

What this publication demonstrates is that despite the varying accountability systems there is a recurring rationale that runs through parliamentary public account committees and audit regimes. Five years on from the crash there are upbeat conversations about the role of audit and how we can achieve more with less.

Exploring the themes from the publication in an English context, ACCA hosted a roundtable in Westminster in April 2014, bringing together politicians, contributors from the report, academics, journalists, regulators and auditors from across the country. Clear themes emerged from the event as well as suggestions for what comes next following the abolition of the Audit Commission in 2015. This paper offers an overview of the key issues discussed, outlines specific highlights and considers what comes next.

THE STATE OF PLAY

Given that UK spending is set to fall by more than a fifth in real terms from 2009/10 to 2017/18 it is inevitable that the next government will have to make bold decisions about where to allocate funding in a stringent financial environment. Audit and scrutiny will play a vital role in ensuring those funds are well spent and holding the Government to account. The stewardship of public funds is critical for public accountability and transparency. Participants were unanimous about the importance of parliamentary scrutiny and audit in providing re-assurance to the public and management that citizens money is being spent wisely. Cuts or no cuts, adequate scrutiny is required to ensure value for money for the taxpayer.

A radically changing public service environment and the abolition of the Audit Commission gave rise to a number of themes discussed by participants for improving the governance and accountability of public services moving forward.

WHERE NEXT FOR PUBLIC AUDIT?

In summary, four key themes were discussed by participants, which included:

- the fragmentation of public services and its impact on good governance and accountability for public spending
- the expansion of the transparency agenda to bridge the accountability gap
- short-termism and the impact of the civil service culture on delivering effective results, and
- approaches to risk management.

FRAGMENTATION OF PUBLIC SERVICES

Half of all public goods and services paid for by the taxpayer are now provided by the private sector. This year's estimated trade spend for local government alone is £30.5 billion. It was generally felt by participants that the current governance, accountability and audit mechanisms were not designed for fragmented public services and as a result are hindering the ability of Parliament to follow the pound.

The concerns are problematic in both central and local government. Following the abolition of the Audit Commission there is a concern particularly at a local level that there will be a lack of accountability as local authorities will be able to appoint their own auditors. These new arrangements have the potential to compromise auditor independence and affect an auditor's ability to pursue an issue without fear or favour.

Public service delivery has altered so radically in recent years that we need to reassess how delivery is governed, audited and scrutinised. Some participants argued that austerity was

driving decision makers to make cuts quickly and make rushed decisions. Rushing to say the best decision is to outsource in response to expenditure cuts has meant in some cases poor value for money and problems with the management and monitoring of big value contracts. There are also examples of outsourced services being taken back under public ownership because of service failure. The skills deficit in procurement and contract management within the public sector is on-going and has had adverse consequences at times making it impossible to see where profits and costs lie and where risks fall.

TRANSPARENCY

Private sector involvement and the development of new forms of public service delivery have led to a piecemeal system of governance and public accountability. The current government's agenda for increasing transparency is an attempt to bridge the accountability gap across all levels of government and from the private companies delivering public services. But this hasn't gone far enough according to participants: for example, an obvious area for improvement, for some, was to make tax returns publically available so that there is a greater ability to assess private companies' suitability to deliver public services.

Participants raised the issue that there is an underlying assumption that transparency is resisted by the companies who are delivering outsourced services. But the Public Accounts Committee found the four biggest outsourcers; Serco, G4S, Capita and Atos, that between them operate £4 billion worth of government contracts, agreed to greater financial transparency allowing government auditors to look at their books and greater leeway on Freedom of Information (Fol) requests.

More often than not resistance comes from government departments as greater transparency makes them open to greater scrutiny. The Department of Work and Pensions (DWP) welfare to work programme, which is an outsourced programme, is an example of a department resisting providing any data that would allow a meaningful assessment of value. However, it is not simply one government department - all departments, and all the main political parties, were considered by some participants to be guilty of allowing politics to get in the way of effective scrutiny. It was generally felt by participants that the issue is pertinent to central government whilst being less applicable at a local level due to the existence of greater statutory duties and roles and open meetings in which decisions are made.

There has been progress in building consensus about the need for greater transparency among private sector companies, but ironically, not yet across the government. According to some participants the key is, if you want to follow the taxpayer's pound you have got to have transparency and open book accounting within all tiers of government, whether it's central or local or agencies and you need the capability and skills to make sense of that. It was noted by participants that where there is open book

accounting, on average, only a third of the time is it used intelligently because there is not the capability to make better use of it. Attendees also agreed that there is a need for a body such as the National Audit Office (NAO) to have access to all contracts so it can see profits and costs, the level of risk transfer and performance.

The creation of the Efficiency and Reform Group in the Cabinet Office was welcomed by participants as a means of understanding where it's possible to make cross government efficiencies in areas such as procurement and shared services, but there is a gap in knowledge about how procurement is being addressed at the local levels and how the skills gap is being plugged.

CULTURE

The issues of the impact of the short-term political cycle on decision making and the culture of the civil service were also discussed. It was argued that the medium-term ramifications of a policy decision need to be balanced with the annual cash cycle and the economic aspects which drive HM Treasury. Currently, it is not. It was suggested that a move away from the annual focus of cash cycles to the medium-term would create less perverse outcomes and better service outcomes.

The discussants agreed that there is an endemic cultural problem, a reluctance to challenge a policy decision that will have create problems. Instead of having an open culture where people are encouraged to come forward and question decisions we rely on a small amount of whistle blowers to come forward and highlight the problem once it's happened. As a result the focus tends to be on cure and not prevention.

The civil service operational structure can also be a barrier to implementing successful policies, particularly as people move around government departments quickly and are often not in place long enough to see a policy or project through or be held to account when the project goes wrong. The consequences of this are that there is no incentive for the person to ensure the long-term success of a project or develop a set of appropriate skills as he/she will likely move on before the project is completed. The operational structure and culture of the civil service also leads to a lack of ability to learn from past mistakes. This is demonstrated by the current and successive governments' track record of information technology disasters, whereby the same issues come around time and time and time again.

There was consensus that we need civil service reform right at the heart of the centre to create an intelligent central financial management function capable of sharing best practice. The government's recent financial management review is welcomed, but it remains to be seen whether the proposals will be successfully implemented across government when there remain divisions between the three key departments; Number 10, the Treasury and the Cabinet Office. A shared political consensus around the need for reform could see much greater success.

Participants supported more proactive early intervention through audit, but were also minded that this intervention could take away part of the responsibility of management to deal effectively with a problem. Audit is important but we should be addressing the symptom not the cause - government departments need a greater skill set and a culture open to change to do the job properly, fundamentally the responsibility must lie with the organisation.

MANAGING RISK

Attendees noted that there is an issue of risk management across both the public and private sectors, and pointed to foundation hospitals that brought in non-executive directors from different industries. The diversity of skills and experience helped act as an effective way of managing risk although the sector is still not without its problems. The ability to start to talk strategically, develop a strategy before implementation and get people early on to look at what could go wrong can result in improved decision-making.

Furthermore, some attendees felt that when audit is discussed in this context the intention is often to refer to external audit only. The nature of external audit is, of course, that it addresses past events. It was felt that internal audit has an important role to play in detecting and resolving potential problem issues at an early stage. We need to charge internal audit not only to manage risk but to perform the validation of plans and strategy. If there is a designated role this could help as long as there is a form of 'protection' through non-executive directors.

SPECIFIC HIGHLIGHTS

There is unanimous support from participants that it is not enough just to audit the books and make sure published financial information is accurate, important though that is. Audit has to move forward, to test efficiency and effectiveness both in how money is raised and how it is spent. This means a closer examination of delivery, of how the machine of government operates and then the translation of auditors' scrutiny into lasting change and improvement. Auditors must intervene earlier in the processes by which money is allocated to departments than projects prepared. Only that way can problems be nipped in the bud.

Non-executive director involvement in the oversight of significant spending projects has the potential to aid better strategy and decision-making. It will also prevent auditors becoming implicated in the decision-making. A strengthened internal audit function will also support better project management.

There is an urgent need to upskill across Whitehall through greater investment in skills development in the areas of data analysis, procurement, project management and financial management. Upskilling could lead to long-term savings and improved service delivery without the need of greater scrutiny.

As highlighted in the report there are opportunities to encourage greater public engagement in the audit process and learn from best practice and innovations in other countries. The press and general public have the power to act as an additional check on government.

Both government and private companies delivering public services must demonstrate greater transparency. An open book policy should be written into any contract to run all or part of a public service, even if this increases the cost of the service as the long-term savings have the potential to outweigh the initial cost. The ability for a wider scope of audit to be undertaken that takes account of performance should also be considered as a means to hold private companies to account in the same way their public sector counterparts are.

Parliament's departmental select committees should take a more proactive role in financial and performance scrutiny, learning from the work done by the Public Accounts Committee. The Parliamentary Scrutiny Unit should be further enhanced to support select committees.

Greater resources need to be invested by Parliament to allow the Public Accounts Committee to undertake more random scrutiny 'hot reviews' and follow up and follow through.

Concerns about local authorities and health bodies appointing their own auditors have not been alleviated. The appointment of auditors was one of the Audit Commission's key statutory duties and the fact that the Audit Commission fulfilled this function meant that it was able to ensure that auditors are entirely independent and, just as important, are seen to be independent.

WHERE NEXT?

ACCA will be continuing its global research in the field of public audit. We are hoping to host similar events across on the issue of public audit around the world. We will also be entering a submission to the Public Administration Select Committee which is carrying out an inquiry into the skills and capabilities the Civil Service needs to ensure good governance for both current and future governments. In the medium term we will be keeping a watching brief on public audit developments in England with a view to developing a business proposition for an audit framework that ensures strong governance and accountability for the new public service landscape.

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