



ICAEW RESPONSE TO FABIAN SOCIETY PAMPHLET: 'PRIZING THE PUBLIC POUND'

11 August 2021

PRIZING THE PUBLIC POUND

ICAEW is pleased to have been asked by the Fabian Society to engage with them in exploring the ideas put forward in their pamphlet '**Prizing the Public Pound**' on local audit in England and spending effectiveness in central government, in which they call for a future Labour government to reorganise, revitalise and expand public audit in England.

Fabian Society 'Prizing the Public Pound' proposals

- An Office for Spending Effectiveness to check deliverability of departmental spending plans and ensure lessons from NAO and internal audits are learned from and actioned.
- A Place Audit Office to be responsible for audits of councils, combined authorities, NHS trusts, academies, multi-academy trusts, transport authorities, police and fire services.
- More powers for public auditors and stronger governance centrally and locally.

ICAEW response

- We welcome the pamphlet's focus on audit as a tool for improving the effectiveness of financial management in the public sector.
- The pamphlet echoes the Redmond Review in its call for reform of local public audit.
- 'Place-based audit' is a potentially powerful concept that looks across central and local government at the effect of public spending on a local area.
- The specific proposals help inform the ongoing debate across the political spectrum and within the civil service on how government can be made more effective and accountable.

The **Fabian Society**, founded in 1884, is Britain's oldest political think tank and has been at the forefront of developing political ideas and public policy on the left for almost 140 years. The Fabians have a long tradition of innovation in public sector reform, generating ideas that have subsequently appeared in Labour Party manifestos or that have been implemented by Labour governments.

This response of 11 August 2021 to the Fabian Society pamphlet 'Prizing the Public Pound' by John Tizard and David Walker has been prepared by **ICAEW's Public Sector team**, which supports members working in and with the public sector to deliver public priorities and sustainable public finances, including over 8,000 in **ICAEW's Public Sector Community**. ICAEW engages with policy makers, public servants, and others to promote the need for effective financial management, audit and assurance, financial reporting, and governance and ethics across the public sector to ensure public money is spent wisely.

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INTRODUCTION

ICAEW believes that trust in public finances is essential.

Citizens need confidence that public money is being put to the best possible use if they are to support local and national governments in the financial decisions that they make. How well public institutions are managed and governed can often be as important as the policy choices that they are used to deliver. The legitimacy of tax relies on public money being spent well, especially where there may be a need to ask for more.

ICAEW was founded in 1880, some four years before the establishment of the Fabian Society, and we are pleased to work together to debate ideas on how financial management and governance within the public sector might be improved. This is as part of ICAEW's engagement across the political spectrum on the long-term sustainability of public finances and the compact between government and citizens.

ICAEW welcomes the emphasis that 'Prizing the Public Pound' puts on strengthening the quality of public sector audit. Not only is audit an essential component to providing the assurance that citizens and their elected representatives at all levels need, but audits can be an effective tool in improving the quality of spending processes and systems and of decision-making in particular.

The pamphlet echoes a number of the recommendations made by the Redmond Review last year seeking to strengthen local authority financial reporting and audit. This accompanies the wider audit reform agenda and **ICAEW's Audit Manifesto** call for the modernisation of audit.

Obtaining value for money from public spending requires robust financial processes, systems and controls to ensure that policy objectives are achieved, at the same time as tackling fraud, error and waste. Transparency of financial information is key if both decision-makers and those to whom they are accountable are able to fully understand the financial consequences of decisions and so inform the choices they make.

Government is a long-term business and decisions made today can have huge implications for the wellbeing of future generations. ICAEW believes that strengthening financial management and audit in the public sector has the potential to pay dividends, both financially and in the outcomes delivered.

FABIAN PAMPHLET: 'PRIZING THE PUBLIC POUND'

The Fabian Society pamphlet 'Prizing the Public Pound' by John Tizard and David Walker sets out ideas how a future Labour government could reform audit and financial management in the public sector.

They comment in their introduction: *"Effective spending should be economical and efficient and should secure policy goals, using the minimum amount to achieve the biggest result. Spending should be environmentally sustainable. Auditors should also ask searching questions about who benefits, whose needs are served and whether spending makes us more or less equal. The pursuit of social justice and rigorous accounting for social spending go hand in hand."*

The pamphlet has two principal proposals, based on the authors' diagnoses of the challenges facing public bodies in the UK: an overcentralised state accompanied by a weak centre that struggles to deliver on public priorities, and a 'patchwork' of audit bodies.

Their first major proposal combines the ideas of internal audit and budget management to create a new Office for Spending Effectiveness (OSE) that combines pre-spending assessment of departmental plans with an active role in embedding NAO findings and other recommendations taking the lead on ensuring improvements are made, including following up on NAO findings.

The authors believe that there is a gap in the way both local and central government spend money. They believe there is a need for all expenditure proposals to be assessed against the '5Es' of effectiveness, efficiency, equity, equality and environmental sustainability before spending is incurred. They also believe expenditure and outcomes should be audited against the 5Es after it is

spent, stressing the need for public audit to sharpen its focus on financial management, the quality of governance, probity, and adherence to the seven standards of public life in the Nolan principles.

Their second major proposal is focused on how audit can be used to improve the effectiveness of local public spending, introducing the concept of ‘place-based’ audit to identify improvements across local public bodies and services within a particular region or local area. This would involve bringing together the audits of councils, combined authorities, NHS trusts, academies, multi-academy trusts, police, and fire services in order to take a more holistic approach of how public spending is delivering outcomes, led by a new Place Audit Office (PAO).

The authors envisage the PAO as being a distinct entity within the National Audit Office (NAO) in recognition of the need to preserve the NAO’s constitutional position in reporting to Parliament while at the same time enabling the PAO to be accountable to councils and other local stakeholders.

The authors argue that a future Labour government is likely to require public support and confidence in government stewardship if it is to make the case for increased public expenditure to meet the needs of communities and places, finance investment in social and physical infrastructure, to create a fairer and more equal society and address regional and social inequalities. Labour may have to increase taxation progressively to fund some of this expenditure and this will require public confidence in how that money is being spent to gain public support.

‘Prizing the Public Pound’ contains a number of other recommendations to strengthen the powers of public auditors and to improve governance in both central and local government. These include strengthening controls over public services outsourced to the private sector and over suppliers to the public sector, as well as improving governance with both central and local government.

PROPOSAL – AN OFFICE FOR SPENDING EFFECTIVELY

Proposal – Office for Spending Effectively (OSE) in the Cabinet Office and HM Treasury

- Diagnosis: A centralised government led by a weak centre; poor value for money.
- To check deliverability of departmental spending plans, in advance.
- Expenditure proposals to be assessed against the ‘5Es’ of effectiveness, efficiency, equity, equality and environmental sustainability.
- To work with departments to put value-for-money at centre of decision-making.
- To ensure NAO recommendations are actioned and lessons are learned.

ICAEW response

- ICAEW concurs with strengthening the central government finance function to drive value.
- We concur with including environmental sustainability as a key criterion for assessing spending.
- OSE appears to combine elements of a budget office or ministry with a central government internal audit function seeking to drive service improvement.
- Potential to act as a driver for value for money in public spending, with the ability to look across the whole of government outside of departmental silos.
- Risk that budget management becomes the focus over service improvement, with centralised oversight becoming a block to rather than enabler of innovation by departments.

At the centre, the pamphlet’s authors propose the creation of a new function, to sit jointly in the Treasury and the Cabinet Office: an Office for Spending Effectively (OSE). Its primary purposes are to check the deliverability of departments’ spending plans in advance, and to work with departments to improve the quality of their processes.

The pamphlet asks: *“Do they deploy evidence of previous policies; have departments modelled how they will be experienced on the doorstep, by people, in places, with what environmental consequences and effects on equalities? This office should be an avaricious consumer of value for money studies from the independent NAO and ensure that NAO audits are responded to.”*

The latter statement follows on from an assertion in the paper that senior civil servants give the impression of reluctance to make the best of audit. This is not our experience, which is that departments take NAO reports very seriously and do genuinely want to improve. However, we do agree that there needs to be much greater focus and resource applied to addressing NAO recommendations and in strengthening financial management, which will ultimately enable departments to be more effective.

The proposal for the OSE is intended to ensure public spending proposals are assessed against the '5Es' effectiveness, efficiency, equity, equality and environmental sustainability. We welcome the inclusion of environmental sustainability in this list of key criteria, reflecting both the importance of achieving net zero carbon and the wellbeing of future generations.

We also concur with the authors' analysis that government can be too 'siloed' with a lack of coherence between central government departments, as well as between central and local government and that better co-ordination and cross-department working is needed.

The OSE as proposed by the pamphlet's authors appears to contain elements of a budget office or ministry as proposed by other reformers, with the OSE taking on responsibility at the centre for working with departments to ensure financial plans are aligned with policy objectives. For example, this is a core part of the remit of the US Office for Management & Budget or Australia's Department of Finance, distinct from wider fiscal policy responsibilities that sit with their respective Departments of the Treasury.

The authors' vision for the OSE is much wider than that of a budget office. Assessing the effectiveness of public spending proposals by departments both before and after public money is spent combines aspects of internal financial control and internal audit to try and improve the effectiveness of public spending proposals. They believe that rigorous assessment of spending proposals in advance of money being spent combined with post-spending evaluations will help departments to improve both outcomes and cost-effectiveness. In particular, their hope is that the proposed OSE will be able to overcome the traditional departmental silos that makes it difficult to work effectively across government, as well as actively driving delivery.

The pamphlet echoes many other commentators in identifying short-termism in government as an issue to effective decision-making, with an aspiration for an OSE to help to drive a more rigorous approach to public spending that encompasses a long-term perspective.

There is a risk that the budget office aspects of the OSE's role as envisaged could come to dominate, as it would provide a mechanism through which the centre could exercise extensive control over spending departments budgets. Future ministers would need to be committed to ensuring the OSE plays a supportive role to departments, otherwise there is also a risk that by acting as a central gatekeeper for major spending proposals that it could stifle rather than encourage innovation by departments.

PROPOSAL – A PLACE AUDIT OFFICE (PAO)

Locally, the pamphlet authors propose a new office for auditing spending in places – a Place Audit Office (PAO) – that would be responsible for the audit of public bodies and services that serve local communities including councils, combined authorities, NHS trusts, academies, multi-academy trusts, transport authorities, the police and fire services, as well as central government services provided locally. The PAO's remit would include auditing the overall wellbeing of communities, looking at the effectiveness of spending by public bodies in combination.

The PAO as envisaged by the authors would be part of the National Audit Office (NAO) and share resources but would have a distinct identity in recognition of the different accountabilities of local public bodies in contrast with the NAO's responsibility to parliament, independent from government.

The authors advocate the potential streamlining of and better aligning of the roles of the auditors and existing inspectorates such as those in education, health and social care, and police, fire and rescue, with scope for more collaborative work between the inspectorates and auditors. They also recommend that local public bodies collaboratively assess their spending plans.

Proposal – A Place Audit Office (PAO) for local audit, complementing the NAO

- Diagnosis: Local audit and local authority financial management are in crisis.
- PAO to be responsible for audits of councils, combined authorities, NHS trusts, academies, multi-academy trusts, transport authorities, police, and fire services.
- To be part of the NAO but with a distinct identity in recognition of different accountabilities
- To work with local bodies to collaboratively assess spending plans, with PAO looking at effectiveness of spending in each place across multiple bodies.
- Better alignment and more collaboration between auditors and inspectorates.

ICAEW response

- ICAEW concurs with this and the Redmond Review that there is a need for reform.
- ‘Place-based audit’ is a potentially powerful concept with the opportunity to assess the combined outcomes of public spending as a whole.
- PAO would provide a system leader for local audit as recommended by Redmond.
- The PAO needs to be constitutionally separate from the NAO.
- Risk that this is a potential recreation of the former Audit Commission.
- ICAEW believes audit reform is not sufficient on its own – there needs to be much greater investment in local authority finance functions and quality of financial reporting.

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The proposal is for more than just joining-up financial audit across local communities and regions. The authors advocate for a more holistic view of audit, ranging from the environmental and social sustainability of the extended supply chain through to the effectiveness of outputs from the overall public perspective. Examples given include suppliers underpaying staff who are then reliant on the public purse for benefits or the implicit transfers in the cost burden from the NHS to police forces in dealing with mental health difficulties from not properly funding mental health services.

The authors set out a compelling vision of the role audit can play in driving improvements in financial management and cost-effective use of public money. The idea of auditing the collective effectiveness of public spending in a local area across a range of public bodies is a particularly powerful idea that is worth building on.

Although not emphasised, many of the pamphlet’s authors proposals echo themes in the Redmond Review, which recommends significant reforms to the local audit market. In particular, the Place Audit Office could potentially fulfil the Redmond Review’s call for a system leader to take responsibility for local audit across England.

A potential criticism of the pamphlet is that the authors appear to be asking public audit to do a lot of the heavy lifting in trying to improve public services. While we agree that audit has a critical role to play and has the capability of playing a stronger role than it currently does, it should not be forgotten that it is public bodies themselves that have the primary responsibility for delivering public services and ensuring public money is spent effectively – and for reporting on their financial performance and position. That said, strengthening public audit is an important element to improving the ecosystem of local authority accountability to elected representatives and the accountability of elected representatives to the public.

One technical point is that we don’t believe the PAO should be part of the NAO as proposed given the NAO’s constitutional position in supporting a single audit principal in the Comptroller & Auditor General who is solely accountable to Parliament. This contrasts with the multiple audit principals that a PAO would need to have that would need to be accountable to councils, police and crime commissioners, the NHS and others depending on the local public body concerned. However, that should not affect the ability of the PAO to share resources with the NAO, to develop common standards and approaches to public audit, and conduct joint audits and projects, as envisaged by the authors in the pamphlet.

Another risk is that the proposals could be seen as an attempt to re-establish the former Audit Commission, with a wider scope of public bodies that would come under the PAO’s remit. While it is the case that some positive aspects of the Audit Commission have been lost under the current system, many of the problems identified by the pamphlet reflect persistent long-term issues in how local

government operates in England that the Audit Commission was never able to solve. ICAEW believes that it is important that expertise provided by independent audit firms is retained in any reformed system of local public audit, while also ensuring that there is an appropriate level of regulatory scrutiny over both the PAO and audit firms.

A further point to be considered is how consistent the proposal for a PAO is with other policy proposals, such as those for devolution and the expansion of ‘metro’ or regional mayors and combined authorities. For example, the pamphlet does not consider the merits or otherwise of regional audit offices for combined authority areas, similar to the Scottish, Welsh and Northern Ireland Audit Offices that cover their respective devolved administrations – as opposed to establishing a single local audit organisation for the whole of England.

OTHER RECOMMENDATIONS

Other recommendations

- Public sector auditors should be empowered to examine outsourced public services and assess the social, economic and environmental impacts of outsourcing.
- NAO and PAO to be given right to ‘follow the pound’ into accounts of contractors.
- Statutory duty on government departments to respond to NAO reports.
- More collaboration between auditors and inspectorates, review overlaps.
- Local authorities to have duty to pre-assess spending plans and to co-ordinate spending and assessments with national public bodies. DRAFT
- Local authority audit, scrutiny and overview committees to be strengthened.

ICAEW response

- Public auditors do have a role in assessing effectiveness of outsourced services, but the Fabian proposals potentially go beyond audit into policy areas that might risk independence.
- Many public sector contracts already have inspection rights that could be better utilised in practice.
- Departments already respond to NAO reports without the need for a statutory duty; the best results will be found where departments are themselves committed to making improvements.
- Greater collaboration between auditors and inspectorates could add value.
- We concur that there are opportunities to strengthen the budgeting process and improve co-ordination between local and national bodies on spending plans.
- ICAEW continues to support strengthening local authority governance.

The pamphlet makes a number of other recommendations to improve public sector audit, based on the ‘5Es’ framework of efficiency, effectiveness, equity, equality and environmental sustainability.

One recommendation is a call for public sector auditors to have expanded powers to examine outsourced public services, procurement processes and contract performance. This would involve looking at the social, economic and environmental impact of outsourcing, including addressing standards of employment and staff wellbeing, as well as the experience of citizens, staff and services.

These proposals are no doubt aimed at high-profile examples of problems with outsourced public services, but there is a risk that it would extend government inspection to a substantial proportion of the private sector without necessarily addressing issues in the quality of government procurement or how outsourced services are managed. There are also concerns about whether this might compromise auditor independence by asking them to make social judgements, for example on the ‘right level’ of staff pay and conditions in private sector organisations.

The authors also propose that both the NAO and PAO be given the right to ‘follow the pound’ into accounts of contractors, although we note that many contracts with private sector suppliers already provide access rights for public bodies and their auditors that could be better utilised.

Another recommendation is for a statutory duty on government departments to respond to NAO reports, with monitoring and oversight by the OSE. We are uncertain whether a statutory duty will effect change, given that departments already respond to NAO reports as a matter of course. There is perhaps more merit in the second part of this recommendation, as more active monitoring and engagement in addressing NAO findings could help drive improvements in financial management. However, ultimately the best results will be found where the departments concerned are themselves committed to making improvements.

The pamphlet also calls for overlaps and duplication between local auditors, regulators and inspectorates, including the Care Quality Commission, Ofsted and HM Inspectorate of Constabulary and Fire and Rescue Services to be examined, while suggesting scope for more collaborative work between and inspectorates and auditors. The latter recommendation has some merit, as there are opportunities for auditors and inspectorates to draw on each other's expertise in certain areas, provided their respective independence is not compromised.

The pamphlet's final recommendation is to strengthen local authority audit, scrutiny and overview committees and to develop democratic mechanisms for scrutinising public spending across areas (complementing the PAO proposals above). ICAEW welcomes these proposals as a long-standing supporter of strengthening local authority governance and in particular of audit committees.

CONCLUSION

ICAEW welcomes the opportunity provided by the Fabian Society to contribute to the debate on audit reform in the public sector and how it can contribute to trust in public finances.

We are of course not in a position to comment on the political aspects of the pamphlet nor on how effective these proposals might or might not be in improving Labour's electoral credibility and in encouraging public support for a future Labour government's tax and spending plans.

We also do not feel it is appropriate to endorse or reject the specific proposals in the pamphlet for a Place Audit Office or an Office for Spending Effectiveness. These are radical suggestions that would need to be thought through carefully as part of a wider evaluation of the government's operating model and in the context of other policies such as devolution. The reforms to the audit market in the process of being implemented by the current government might also affect these proposals, while capacity in the audit market might constrain the level of ambition that is possible.

However, where we concur with the pamphlet is the stress it places on the importance of auditors as truth tellers, providing evidence and insight that are essential to effective governance. We are also pleased with the emphasis placed by the authors on audit as a tool to drive improvements in the effectiveness of public spending, with lessons from previous spending plans used to inform decision-making.

In particular, the idea of place-based audit to look at the overall effectiveness of public spending across local areas is an important contribution to the debate that is worth exploring further.

The pamphlet's emphasis on strengthening pre-spending assessments, more rigorous processes to address NAO recommendations and more evidence-led policy making are also positive. It also touches on a number of areas where there are opportunities to improve the effectiveness of government, such as better use of data, the effect of policy decisions on the public balance sheet, and the need for a better understanding of how spending in one part of government affects – and may diminish – the value of spending in another.

'Prizing the Public Pound' makes the case for strengthening audit and financial management in the public sector as a prerequisite for trust in public finances and ICAEW welcomes the contribution it makes to the debate.

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