ORIGINATOR: ERNST & YOUNG LLP (EXTERNAL AUDITORS)

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SUBMITTED TO: AUDIT COMMITTEE – 24 JULY 2026

SUBJECT: FROM RESET TO RECOVERY REPORT

Summary

1. The report attached is the From Reset to Recovery Report.

Recommendation

1. The Audit Committee is requested to consider the attached report.

From reset to recovery

Restoring confidence and accountability in local government audit

June 2026

The better the question.
The better the answer.
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Foreword

Local government audit in England has reached a pivotal moment. The statutory reset has largely delivered what it set out to achieve: historic backlogs have been cleared and timeliness has been restored to a system that had ceased to function effectively.

For the first time in several years, most councils now have published audit opinions for recent financial years. That progress matters. But the reset was never intended to complete the recovery. This report is published at a point after the reset, but before confidence has been fully rebuilt. While timeliness has improved, assurance has not yet caught up. The next phase must be judged by restored assurance – not simply by whether opinions are issued on time.

Disclaimed and modified opinions are now widespread, reflecting necessary compromises made during an exceptional period. The real issue is therefore not technical compliance or opinion labels alone. It is whether local government financial reporting is once again fulfilling its fundamental public-interest purpose:

- Enabling elected members to govern effectively
- Supporting transparency in the use of public money
- Sustaining confidence in local financial reporting

Ernst and Young UK LLP (EY UK) has been centrally involved in the delivery of the local audit reset and is the appointed auditor to around a fifth of the local government sector in England. In 2024-25, we worked closely with government, PSAA and audited bodies to deliver against statutory backstop dates, while maintaining focus on public-interest risks, value-for-money reporting and governance concerns. That experience gives us a clear, practical view of what is working – and where risks remain.

This report draws directly on our local government audit work during the reset period. It reflects what we have seen across our audits of councils at very different stages of recovery, and what differentiates those building assurance successfully from those where recovery is stalling. Our aim is to share evidence, lessons and insights that can help the system move forward. In doing so, we see our role as constructively supporting government objectives, system leadership and the sector itself – by helping to clarify what "successful recovery" now looks like, and what practical actions can support it.

Stephen Reid, Head of Government and Public Sector Assurance – EY UK

> "The question facing the sector is no longer whether audits can be delivered on time — but whether financial statements provide the confidence and accountability that local democracy, taxpayers and government deserve.

Contents

Outline summary

Local government financial reporting in England has entered a new phase. The statutory backstop regime has largely succeeded in clearing the historic audit backlog, but it has done so by design, at the cost of assurance, with large numbers of disclaimed opinions across the sector. The challenge has therefore shifted: from restoring timeliness to rebuilding assurance in a system that remains fragile.

Sound financial reporting and governance underpin all public bodies, but local authorities occupy a unique position of trust, directly accountable to their local council taxpayers for the use of resources and the stewardship of public funds. Failures in financial reporting or governance can have direct consequences for the communities they serve, making reliable assurance essential for elected members and citizens alike.

Local government continues to operate under significant pressure. Finance functions are increasingly asked to act as strategic business partners, driving the sector's approach to financial sustainability and resilience. Reorganisation raises the stakes for the underlying quality of assurance, systems and governance arrangements. Against this backdrop, we have examines progress towards the Local Audit Liaison Committee's aspiration of restoring the audit system by 2026-27.

Local government financial reporting has failed in recent years. Well-understood issues including technical complexity, resource constraints within finance teams, and fragility in the audit market, which led to widespread failures to publish audited financial statements. The government's approach to reset the timeliness of reporting has been successful in clearing the backlog, but it was just a starting point.

Our review of the local government audits performed by EY UK for 2024-25 demonstrates substantial progress in the level of assurance achieved across most of the bodies we audit, reflecting concerted efforts by councils and auditors alike. At the same time, it highlights a critical challenge: without targeted support and sustained focus, councils in the most difficult positions risk falling behind as the wider sector moves forward in its recovery.

While assurance levels have improved, most bodies that met backstop dates continued to receive disclaimed opinions, reflecting incomplete audit procedures and ongoing gaps in cumulative assurance. This highlights the scale of the recovery challenge ahead. Our findings point to the need for a sustained and deliberate focus on rebuilding assurance, alongside practical action to strengthen decision-making and demonstrate stewardship of public resources.

While most local government bodies are well-placed to return to unmodified opinions within the window set out in national guidance, a small but significant minority are lagging behind. There is a real risk that the recovery trajectory for some councils means that they will never achieve all assurances. The same councils report higher rates of significant weaknesses in value for money arrangements, and internal control failings, often in areas that demonstrate how far behind parts of the sector have fallen.

We examine the factors behind these diverging trajectories. While it is well-documented that the financial reporting framework does not fully meet the needs of the sector, there is a risk that for some councils the financial statements process is seen as irrelevant or low priority during a period where local government faces pressure across a range of factors. Our evidence suggests that this position risks reinforcing or accelerating the decline in financial governance, ultimately failing elected members, decision-makers, and the communities that they serve. In other cases, we found councils that can balance external pressures and internal complexity while supporting the external audit process, delivering robust financial statements ahead of the recovery curve. With the reset complete, readiness for audit has emerged as the clearest differentiator between councils that are rebuilding assurance and those at risk of falling behind. Our 2024-25 experience shows that audit readiness is no longer an operational matter — it is now a core test of financial governance maturity.

Our aim in this report is to share the lessons that we have learned from 2024-25, highlighting what good looks like and supporting the sector to shape the future with confidence.

Good practice is characterised by strong relationships: engagement with external audit throughout the financial year, a finance team with sufficient capacity to meet increasing demands and support from the active elected members, particularly those on Audit and Risk Committees.

Outline summary

The report focusses on practical actions across the relationships with audit that matter the most.

Collectively, we found a number of factors that create the conditions needed to rebuild confidence and restore assurance in local government audit:

- Leadership that prioritises assurance
- Finance functions with sufficient capacity and capability, engaged and informed Audit and Risk Committees
- Systems and controls that support sustainable, high-quality financial reporting

The next phase requires deliberate management of assurance recovery. Success should be judged by restored assurance – not just signed opinions.

1. **Section 151 Officers:** Responsible for leading audited bodies' response to assurance recovery and overall financial governance maturity. They hold the key relationship with external auditors and are uniquely placed to act where recovery is stalling and provide recommendations to elected members to invest in capability and systems.

2. **Audit and Risk Committees:** Responsible for reinforcing the framework of internal control and oversight of any fragility in finance teams or resourcing. We recommend that they move audit readiness from a year-end issue to a continuous governance risk, and focus their scrutiny on assurance, not timeliness.

3. **System leaders:** Restoring confidence in local government audit now requires system leaders to target support to councils at risk of entrenched failure, aligning audit resource with recovery objectives. In our view, there is a need to accelerate reform of the local government reporting framework – financial reporting simplification should be seen as a recovery-critical intervention, not a long-term improvement project.

Section 1

1 **Reset:** from backlog to a new assurance problem

1. **Reset:** from backlog to a new assurance problem

Statutory backstops have largely succeeded in clearing the historic audit backlog

The reset succeeded in clearing the backlog, but fundamentally changed the meaning and value of the audit opinion. By 2022-23, it was clear that the local audit system in England was no longer functioning as intended. Publication rates for audited accounts had collapsed, audit backlogs spanned multiple years, and confidence in local financial reporting had been materially eroded.

The Minister of State for Local Government flagged that just one percent of councils and other local bodies published audited accounts on time in 2023. This directly contributed to the National Audit Office disclaiming the Whole of Government Accounts (WGA) for consecutive financial years – a first in the history of the WGA – and highlighting a failure of local financial accountability.

The causes were systemic rather than cyclical: increasing technical complexity within the financial statements, low resilience within local government finance teams, fragmented audit system leadership and declining audit capacity. Changes in PSAA appointments in 2023-24 meant in some cases new auditors were taking on financial statements that had not had audit opinions under the previous five-year contract.

The government's response, the introduction of a series of statutory backstop dates, represented a deliberate policy choice to prioritise timeliness over completeness. The objective was not to perfect historic audits, but to reset the system so that attention could return to current financial years.

The reset stage in the period to 27 February 2026 aimed to clear the backlog of over 1,000 local government opinions and to set in motion the reestablishment of normal timescales for both preparation of the financial statements, and the issuing of unqualified audit opinions across the sector by 2026-27. Auditors' other statutory duties, including reporting on Value for Money, making statutory recommendations and issuing Public Interest Reports remained a high priority.

The reset has largely been achieved (Figure 1). Audit opinions have been published for the vast majority of bodies for financial year 2024-25, including across EY UK portfolio, where the audited body was able to support completion.

The reset was a deliberate trade off – speed was prioritised over assurance

In the initial reset years, this represented a deliberate trade-off – the statutory backstop dates forced the publication of financial statements, and getting financial data into the market, whether the balances were fully audited or not. But the reset has changed the nature of local audit output. Disclaimed opinions are now widespread because auditors continue to be constrained by time, evidence availability and statutory deadlines.

The challenge for local government finance has therefore changed: from restoring timeliness to rebuilding assurance in a system that remains fragile.

Clearing the backlog has fundamentally changed what an audit opinion now means

Disclaimer opinions are usually exceptionally rare in the public sector. The disclaimer opinion means that auditors cannot obtain sufficient appropriate audit evidence on which to base an opinion, and therefore the possible effects of undetected misstatements could be both material and pervasive. It is very much at odds with the values that we hold ourselves to as public sector auditors: instead of strengthening public-interest assurance, it highlights its absence.

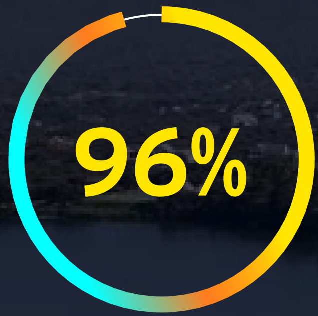
Local government financial statements are lengthy and complex documents. The financial reporting framework is based on International Financial Reporting Standards (IFRS), with a series of statutory provisions and overrides to reflect the nature of local government bodies.

The level of complexity depends on the nature of the body and particularly the nature of the reserves. Complexity is increased by the statutory need for reserves relating to both revenue and capital transactions.

This is critical for individual councils: if there is a misclassification between usable (spendable) and unusable reserves (that cannot be spent), the council's financial resilience may appear stronger than it really is.

Figure 1
Current progress against backstops

2023-24

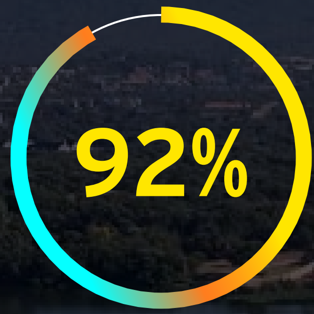


As at 31 December 2025, 96% of all 2023-24 Local Government audits were signed.

Nine EY UK audit opinions remain outstanding caused by:

- Prior year audits remaining open by predecessor auditor
- Late appointment as the entity's auditor
- Financial statement preparation issues within individual bodies
- Significant value for money issues

2024-25



On 27 February 2026, over 92% of audit opinions were signed (excluding pension fund audits). EY UK signed the opinions for 106 of 121 bodies (88%) within our portfolio.

Issues impacting the completion were the same as 2023-24, including:

- Financial statement preparation issues
- Significant value for money issues

Following a disclaimer, assurance gaps roll forward and compound over time

In normal circumstances, auditors can check any movements in-year and rely upon last year's audited closing balance as the opening balance. After a disclaimer opinion, the auditor cannot rely upon the opening balance, because it was never audited. Instead of checking what changed this year, the auditor has to consider whether the entire balance, built up over several years, is materially true and fair.

The challenge of opening prior year financial statements (in some cases by predecessor auditors), prior year disclaimers, and the complexity of local government reserves means that auditors have adopted a phased approach to auditing transactions.

EY UK adopted a deliberate, public interest-led strategy to support both government objectives and the audited bodies that we work with

The scale of the reset and prevalence of disclaimed opinions across local government bodies presented auditors with a balancing act. The volume of disclaimed opinions and assurance gaps meant that attempting to rebuild assurance uniformly across all bodies would risk diluting the impact of finite audit resource and therefore delay the recovery timeline overall.

In response, EY UK adopted a structured prioritisation model that:

- Focusses early effort on bodies with the highest likelihood of recovery.
- Maintains Value for Money scrutiny where public interest risk is highest, even where financial statement recovery is slower.

This approach was not intended to reduce standards, it was about maximising meaningful assurance during an exceptional period.

EY's approach to prioritisation of audits was built around two key factors:

1. Public interest

Audit effort is prioritised where it is most likely to:

- Support a return to unqualified audit opinions.
- Provide meaningful assurance to taxpayers and stakeholders.
- Highlight and report significant governance or value for money concerns promptly where they exist.

2. Deliverability and readiness

Experience shows that audit timeliness is driven primarily by the audited body's ability to support the process. We therefore take account of:

- The quality and timeliness of draft financial statements.
- The authority's capacity to provide evidence and respond to audit queries.
- Historic delivery and engagement with the audit process.

The challenge has shifted from timeliness to assurance recovery

With the backlog cleared, the critical question facing the sector is no longer whether audits can be completed on time. The sector now needs to consider:

- How assurance is being rebuilt with a finite resource pool and imposed deadlines.
- Why recovery trajectories differ so significantly across councils.
- What actions are required to prevent temporary assurance gaps becoming entrenched failures.

The reset created the conditions for recovery. It did not complete it.

Reframe success around restored assurance, not simply timeliness

System leaders should now explicitly redefine what "success" looks like for local audit. Clearing backlogs was a critical first step, but widespread disclaimer opinions represent a material loss of public assurance. National metrics, communications and oversight mechanisms should therefore shift focus from backstop compliance to progressive restoration of assurance, including movement from disclaimed to qualified and ultimately unmodified opinions.

Without this reframing, there is a risk that the system mistakes procedural completion for genuine accountability.

2

Section 2

An uneven recovery: assurance is improving but with diverging trajectories

2. **An uneven recovery:** assurance is improving but with diverging trajectories

Rebuilding assurance requires multi-year effort and targeted audit focus

Assurance is rebuilding, but not evenly. While many councils are progressing along an expected recovery path, a small but significant minority are falling materially behind and risk becoming left behind without intervention. The vast majority of local government audits in 2023-24 were disclaimed. Within EY UK's portfolio this reflected difficulty in performing planned in-year audit procedures. Where disclaimer opinions were provided, there were key gaps in assurances on significant balances across the sector including:

- Reserves
- Property, Plant and Equipment
- Comprehensive Income and Expenditure
- Cash Flow Statement
- Grants Received in Advance and, where relevant
- Collection Fund balances

These areas represented key gaps in cumulative assurance that had to be addressed in 2024-25. The challenge of opening prior year financial statements (in some cases by predecessor auditors), prior year disclaimers and the complication of local government reserves, means that local government auditors have operated a phased approach to audit transactions and therefore build-back assurance.

This can involve interrogating data over several financial years, not just the immediately prior year and relies on finance teams being able to produce historic audit evidence and therefore tests organisational record keeping and corporate knowledge.

Build-back rarely restores a clean opinion immediately. A simplified trajectory is:

Year 1:	Year 2:	Year 3:
Disclaimer (or disclaimer with emphasis on remedial work)	**Qualified opinion** (e.g., limitation of scope confined to specific balances)	**Unmodified opinion**

Auditors assess the direction of travel, not just the end-state of the assurances delivered. As a result, Phase 2 of the backstop dates are intended to prevent a recurrence of the backlog and allow assurance to be rebuilt over multiple audit cycles. Guidance in the NAO's Local Audit Reset and Recovery Implementation Guidance (LARRIG) 01 (Appendix A) sets out an expected timetable for the rebuilding of assurance, reflecting aspirations to restore the whole audit system to unqualified audit opinions by 2027-28.

Audit and Risk Committees:

Audited bodies and their Audit and Risk Committees need to move beyond a sole focus on meeting backstop dates and explicitly manage the multi-year rebuild of assurance, recognising that disclaimers create cumulative assurance gaps.

The recovery should be actively managed in line with the expected trajectory (disclaimer → qualified → unmodified), rather than assuming assurance will "reset" automatically.

There was a step change in the level of assurance achieved in 2024-25 – but with significant variation

Overall audit outcomes within our portfolio significantly improved in 2024-25:

- The level of disclaimed opinions fell from 76% in 2023-24 to 59%.
- A rise in the number of qualified opinions from less than 1% to 24%, representing councils where gaps in audit procedures were confined to a limited number of specific balances, rather than pervasive gaps impacting the whole of the financial statements.
- The level of unmodified opinions rose from 1% of councils to 22% in 2024-25.

However, while LARRIG 01 was based on the understanding that the majority of opinions in 2024-25 would continue to be modified, Figure 2 highlights that most of the opinions that we issued in 2024-25 remain disclaimed. Our experience in the 2024-25 local government audits points to a much more challenging and uneven recovery pattern.

A small but significant minority were not signed on the backstop date, reflecting the status of prior year audit opinions by predecessor auditors, financial statement preparation issues and/or significant value for money issues. The level of assurance varies across bodies – unmodified opinions remain concentrated in pension funds and a small number of local government subsidiary bodies with strong financial governance where the level of complexity within financial statements, including usable and unusable reserves, is less pronounced.

The critical question is therefore no longer whether the system has reset, but how assurance is being rebuilt – and why some bodies are progressing faster than others.

Rebuilding assurance is inherently cumulative

Following successive years of disclaimed opinions, assurance gaps do not reset automatically. Instead:

- Opening balances cannot be relied upon.
- Auditors must rebuild assurance over cumulative balances, often spanning several years.
- Progress is therefore uneven across different areas of the financial statements.

In 2024-25, the ability to complete in year procedures was critical to progression, forming an integral element of the overall build-back approach and our assessment of the organisation's progression. Overall, assurance was rebuilt more quickly in areas subject to in-year testing. In contrast, assurance over cumulative balances – particularly reserves and property, plant and equipment – lagged behind (Appendix B).

This pattern explains why many councils progressed from no assurance to partial assurance, but not yet to unmodified opinions.

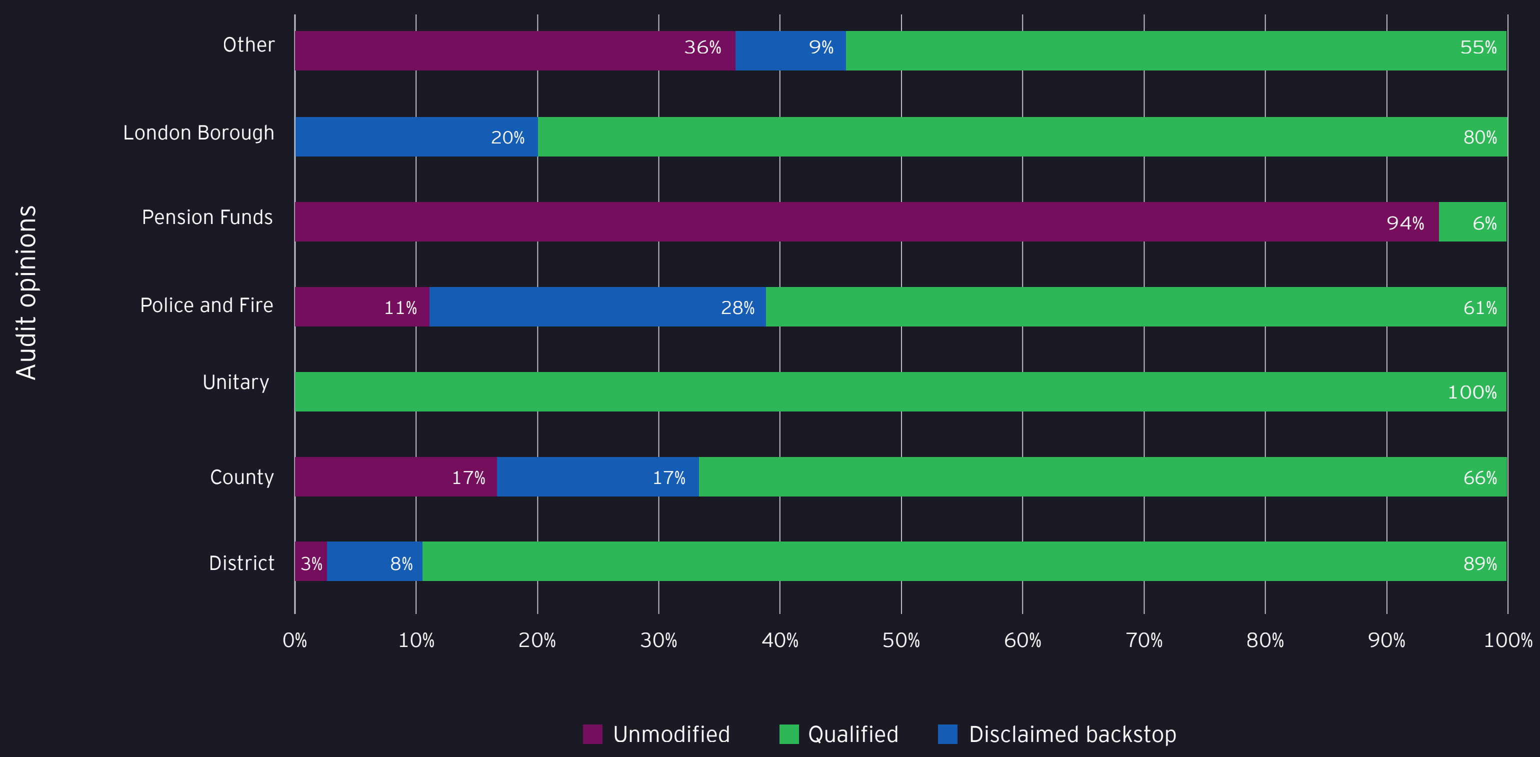
Strengthen audit readiness across the organisation

Ensure early, high-quality draft financial statements are supported by robust working papers. Address recurring issues such as unresolved prior-year errors, poor record-keeping and weak evidence trails.

Figure 2

For all but pension funds, the majority of EY UK opinions remained disclaimed at the 27 February 2026 backstop date.

Individual audit results reports provided visibility on where assurance has been successfully rebuilt and where gaps remain.



What good looks like in rebuilding audit assurance

We considered the factors present at a number of the councils where most progress has been made.

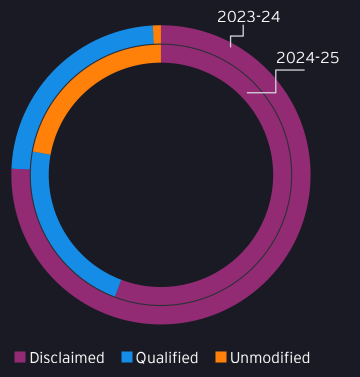
Strong progress in rebuilding audit assurance is typically underpinned by deliberate investment in finance capacity, enabling councils to support the audit process effectively alongside wider corporate responsibilities. Where additional resource has been prioritised, finance teams are better able to produce high-quality, timely working papers and respond promptly and constructively to audit queries, improving both efficiency and assurance outcomes.

Effective councils also place strong emphasis on member engagement. Regular, structured briefings with the Audit and Risk Committee promote transparency, allow emerging issues to be surfaced early, and ensure Members remain well-sighted on progress, risks and challenges throughout the audit cycle, rather than only at year end.

This progress is reinforced by stable, well-embedded finance systems that support statutory reporting requirements without reliance on complex manual work-arounds. Robust underlying systems enable clearer audit trails, more reliable data and greater consistency in financial reporting.

Alongside this, a strong and independent internal audit function provides critical assurance over governance and internal control, helping to identify and address weaknesses before they impact external audit outcomes.

Figure 3
There were significant year on year improvements in the level of assurance that EY provided across the sector

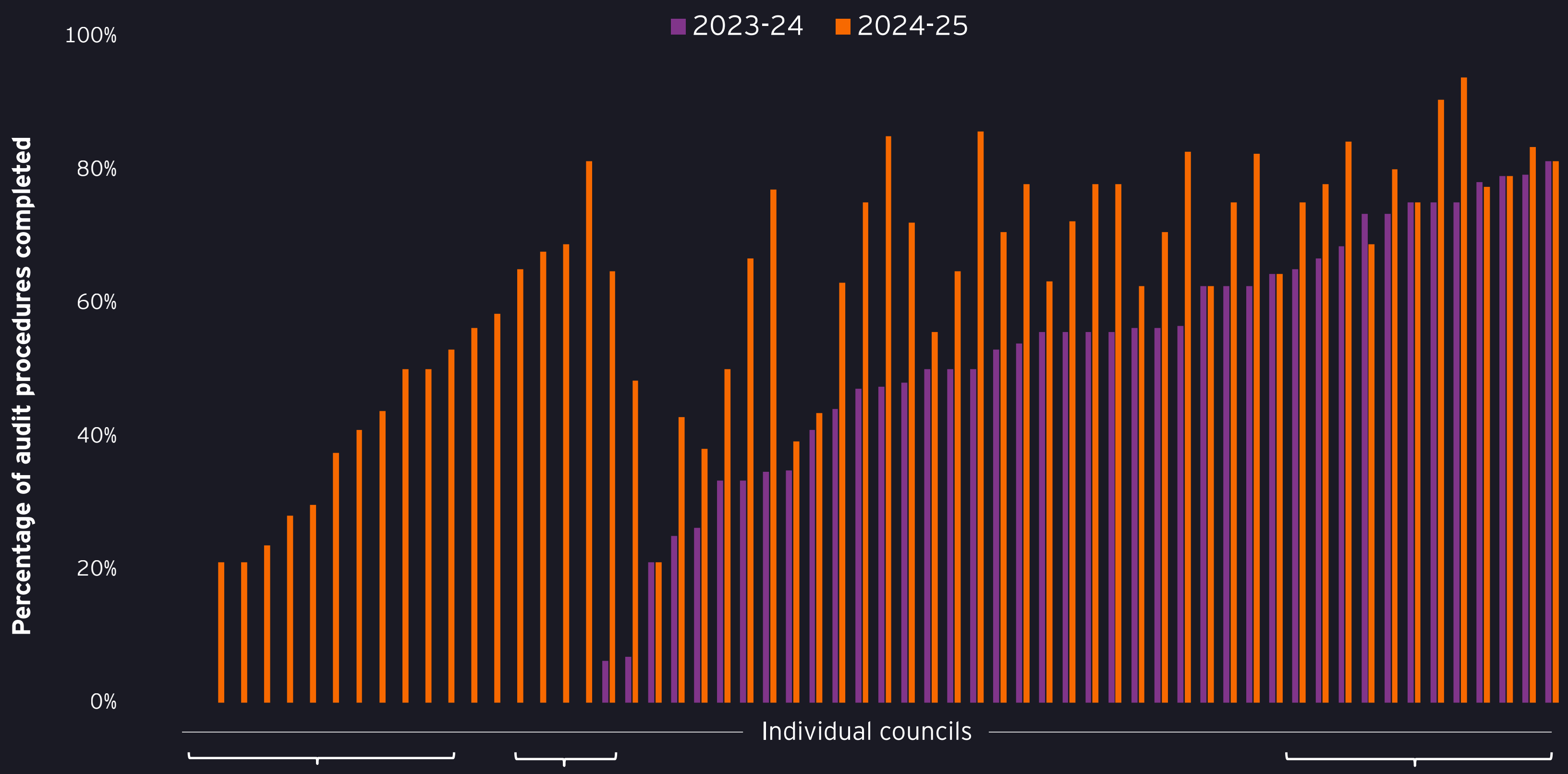


In 2023-24, 87 (76%) of opinions that we issued were disclaimed as we were unable to complete planned audit procedures. By 2024-25, this had fallen to 63 (59%) of the opinions issued by EY.

Figure 4

Improvements in assurance were not driven by body type or scale. Across individual bodies there was significant variation in the extent that we were able to complete audit procedures

Individual audit results reports provided visibility on where assurance has achieved and where gaps remain.



Significant gaps in assurance remain and individual bodies are at risk of failing to meet the Reset and Recovery Implementation timescales (LARRIG 01).

Some councils with no assurance in 2023-24 made significant in-year progression in 2024-25, representing an improvement in assurance overall and supporting future year audit activity.

More advanced progression against LARRIG 01 timescales. Higher level of assurance and therefore more likely to be qualified rather than disclaimed.

Complexity explains some variation but not the full divergence in outcomes

We expected the level of assurance that we could obtain to vary across the type of local government body (Figure 5) because of the complexity of reserves, particularly in Unitary, District and London Borough councils, where the level of complexity is increased as a result of the reliance on usable and unusable reserves impacted by:

- High asset values and the impact of the revaluation of housing stock and investment properties.
- Transport and other infrastructure assets, including statutory override to respond to valuation difficulty.
- Council tax and non-domestic rate collection, including large debtor and creditor balances and, the need to estimate bad debt and appeal likelihood.
- Commercialisation and required group accounting for trading companies and joint ventures.

We found some evidence of this. In audits where a disclaimer or qualified opinion was issued, no assurance over reserve balances was given, or was only partially established. This had an impact on our procedures — for example, 78% of procedures were completed for Police and Fire bodies, compared with 51% for Unitary authorities. However, it was clear that this was not the whole story.

Bodies of similar type are experiencing materially different outcomes

The evidence from our audits in 2024-25 demonstrates that rebuild trajectories differ considerably across organisations and are not always driven by size or scale (Figure 6).

Notably, some large and complex bodies were able to support completion of all audit procedures other than those relating to reserves, resulting in a qualified opinion.

Most local government bodies are capable of supporting meaningful build-back and may return to unmodified opinions within the current backstop window.

Others face persistent barriers including poor quality draft financial statements, fragile finance teams, unresolved legacy auditor issues and ongoing statutory intervention, that materially limit progress. For these bodies, system-level oversight is likely to be required to provide targeted support.

Variation in recovery therefore points to a deeper issue than complexity alone. The next phase of recovery will be determined by how effectively individual bodies govern, resource, and prioritise financial reporting.

Without targeted focus, uneven recovery risks becoming entrenched

If not actively managed, diverging recovery trajectories create systemic risk:

- Councils that fall behind face compounding assurance gaps that become harder to resolve over time.
- Audit resource is increasingly concentrated on bodies capable of progress (in line with directions within a Ministerial letter dated 27 November 2025), further widening the gap.
- The credibility of local financial accountability is weakened where a subset of councils remains persistently unauditable.

Figure 5
We were more likely to complete full audit procedures for less complex bodies, including Police & Fire bodies, but this was not consistent

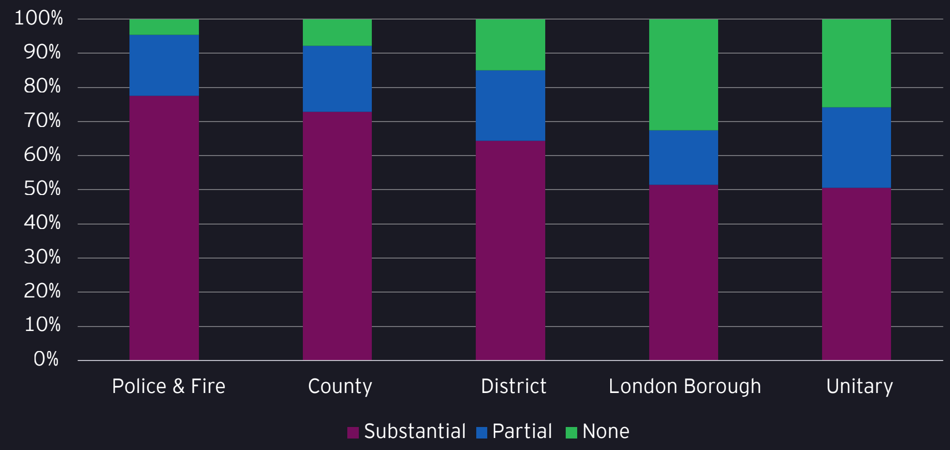
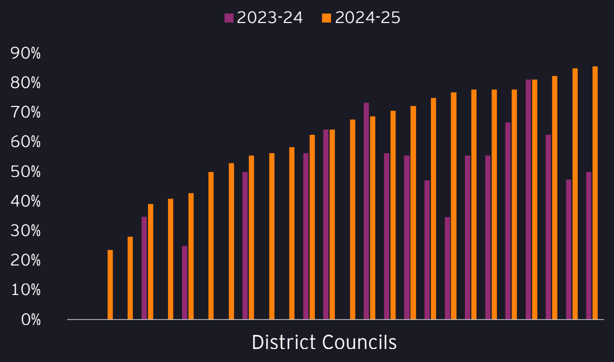
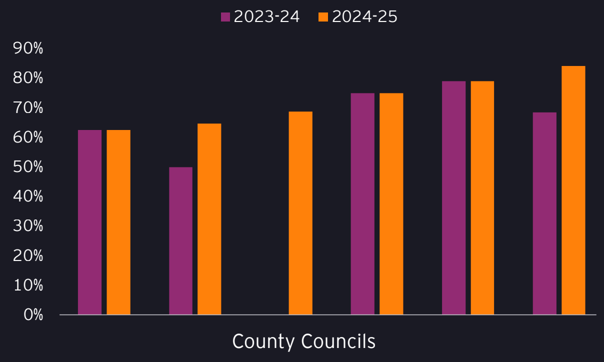
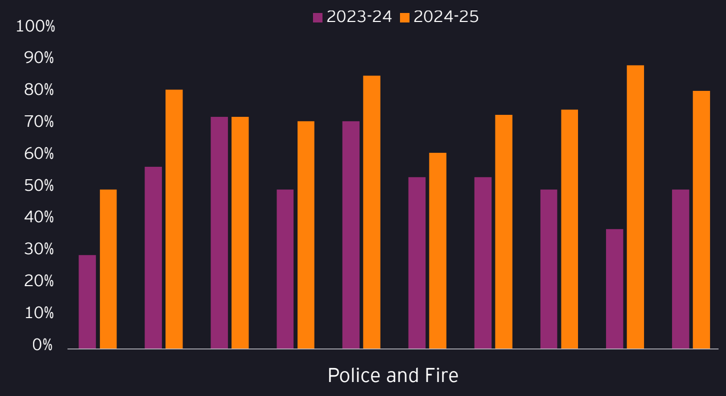
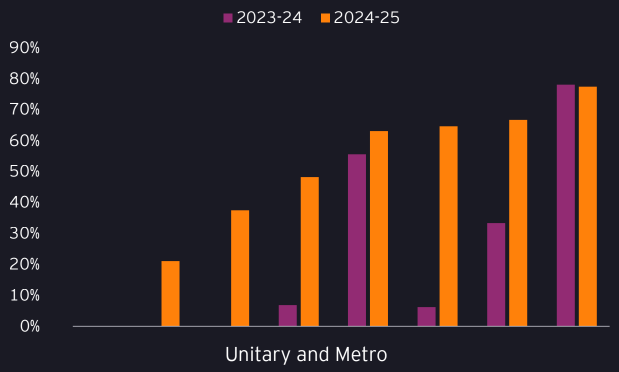


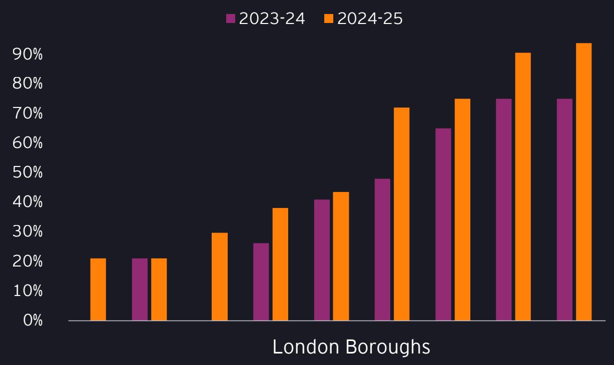
Figure 6
The level of assurance varied significantly within the individual types of local government body, confirming that complexity alone does not explain delays in rebuilding assurance.

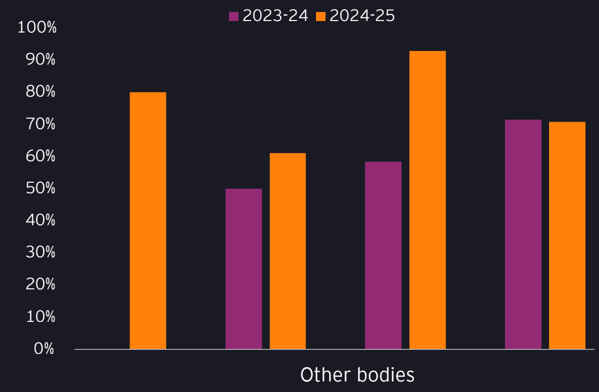












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Section 3

Readiness for audit: the acid test for assurance recovery

3. **Readiness for audit:** the acid test for assurance recovery

With the reset complete, the defining question is no longer whether the system can recover – but why recovery is uneven, and what distinguishes councils that are moving forward.

Local government financial reporting is inherently complex. Local authorities are required to prepare financial statements that align with the same requirements as large listed entities, including:

- Complex asset valuations, including social housing and infrastructure.
- Pension assets and liabilities requiring actuarial judgements.
- Significant estimation uncertainty across reserves and collection funds.
- Increasing commercialisation and group structures.

The complexity requires finance teams with public sector experience and access to internal and external experts, including valuers and actuaries to support required disclosures. Yet statutory overrides mean that the impact of valuations and pension movements are reversed, together with a plethora of other sector specific technical accounting adjustments, and so have no effect on the level of council tax, or on how the council is managed.

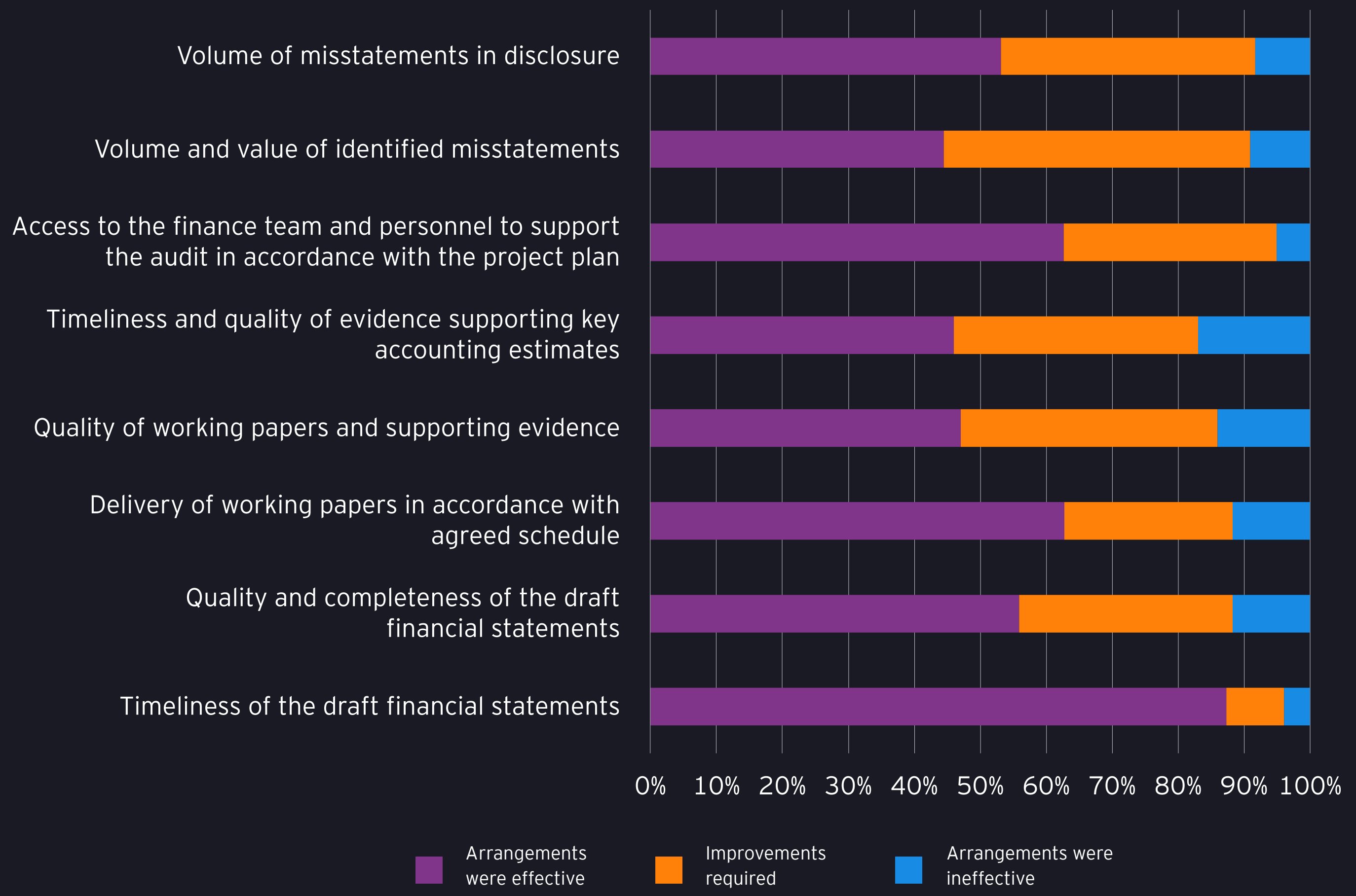
At the same time, the lack of external audit assurance for successive years has coincided with a time when local government is facing severe financial challenges with resulting capacity and capability constraints within the workforce, particularly in finance teams. Awards for Exceptional Funding Support (EFS) rose from £270 million across seven councils in 2020-21, to £1.264 billion for 28 councils in 2025-26, a rise of around 370%.

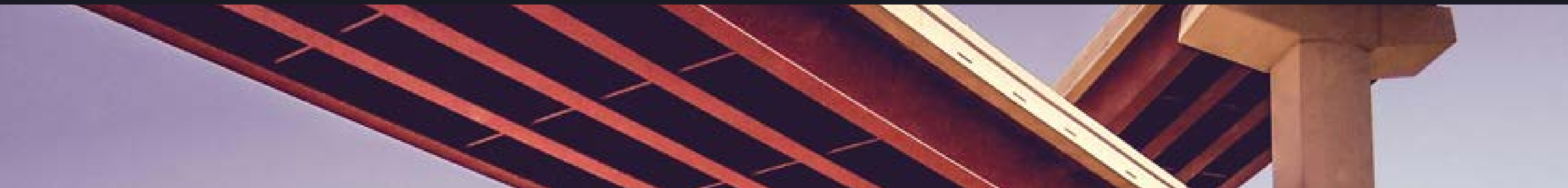
In these circumstances, for some councils the financial statements have been viewed as a compliance exercise rather than a tool for transparency and accountability. However, our experience in 2024-25 points to the importance of the readiness for audit as an indicator of how effective financial governance is overall. For the cohort of councils who are falling behind the timelines set out in LARRIG 01 for recovery of assurance, this should be a key governance issue for Audit and Risk Committee members.

Audit readiness is emerging as the clearest early indicator of successful assurance recovery

In 2024-25 we conducted an assessment of the readiness for audit for individual local government bodies. Our ability to complete the audit is dependent on the timely formulation of appropriately supported accounting judgements, provision of accurate and relevant supporting evidence, access to the finance team and management's responsiveness to issues identified during the audit. As a result, we assessed the preparations for audit against 8 criteria and reported the results to Those Charged with Governance at respective councils within our annual reporting (Figure 7).

Figure 7
Most local government bodies were well prepared for audit and met deadlines for the delivery of draft financial statements that were of a good quality.





Most bodies met deadlines — but quality, not timeliness is now the differentiator for audit readiness

In 2024-25 we found that:

- Almost 90% of local government bodies met earlier timescales for the production of the financial statements.
- However, quality and completeness — not speed — increasingly constrained audit progress.

The most persistent challenges related to:

- The quality of working papers supporting key accounting estimates.
- Valuation evidence, often sourced from valuers using inconsistent methodologies.
- Reconciliation of fixed asset registers to valuation and estate records.
- In some cases, the volume and recurrence of misstatements.

These issues directly affect audit efficiency. Where working papers cannot be reconciled or relied upon, audit testing is delayed, repeated, or curtailed — compounding pressure on both finance teams and auditors.

Audit readiness correlates strongly with assurance outcomes

Our audit experience in 2024-25 demonstrates a clear relationship between readiness and assurance:

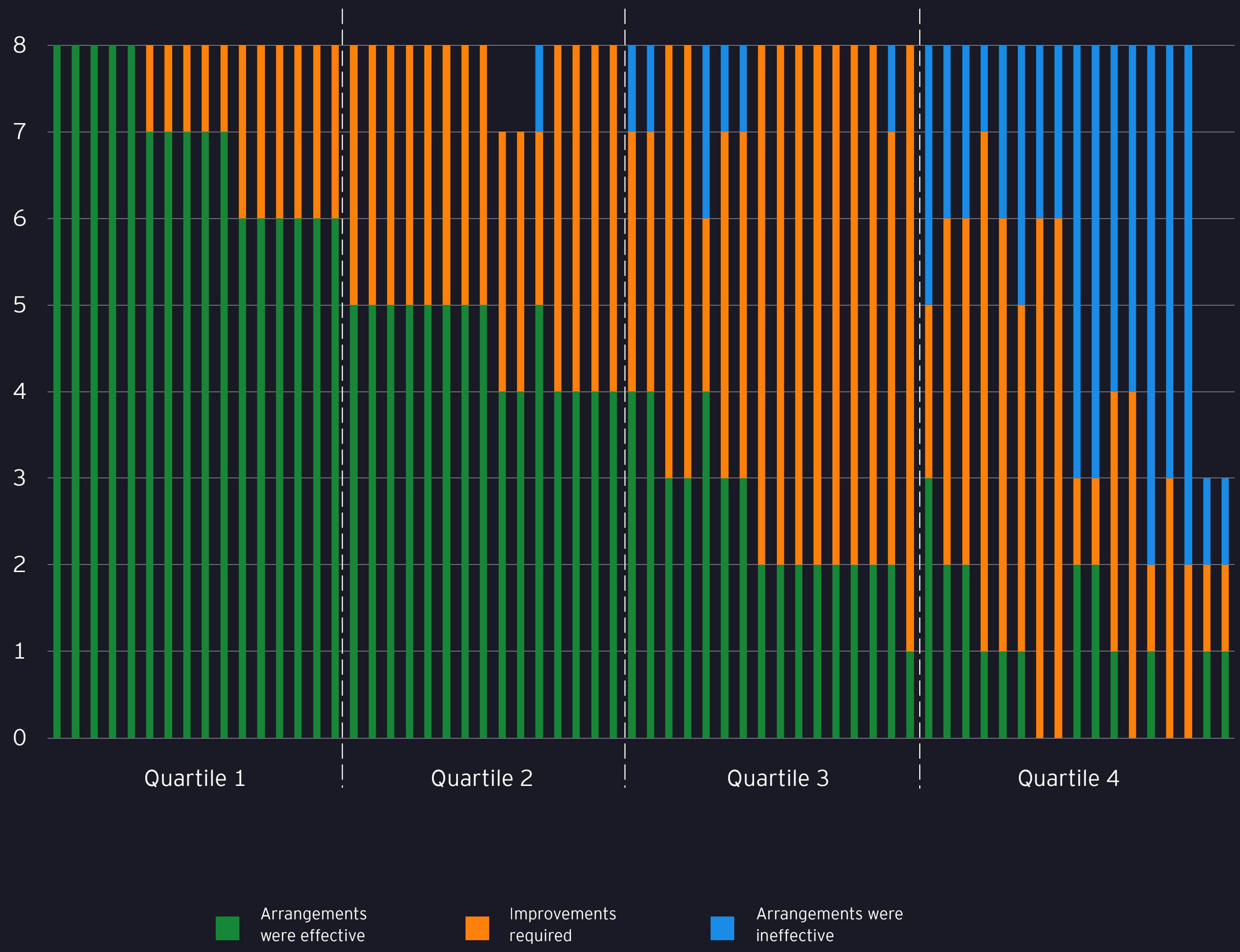
- Councils that were able to produce well-supported draft financial statements and respond effectively to audit queries were significantly more likely to progress from disclaimer to qualified opinions.
- Where readiness remained weak, auditors were often unable to complete sufficient planned procedures, regardless of the body's complexity or size.

We found that we could split councils into four main groups, with advanced, well-prepared bodies in Quartile 1. Quartile 4 represents a cohort of councils that are not meeting the requirements expected for the sector, refer to Figure 8, over page. Reasons include:

- Cases where 2024-25 was the first substantive audit that the council has had for a number of years and the systems and processes therefore require to be re-established.
- Insufficient capacity within the finance team to deliver the external audit alongside other operational commitments.
- Failure to respond to material prior year errors;
- Lack of support for audit requests to other departments across the Council.
- Significant changes in personnel within the finance team, including the Section 151 Officer.

In two cases within Quartile 4, we were unable to assess five of the criteria because the working papers and evidence needed for audit were not provided prior to the backstop date.

Figure 8
We found that we could split councils into 4 main groups, with advanced, well-prepared bodies in Quartile 1. Only 5 bodies were assessed as fully ready for audit.



Audit readiness is the decisive factor in assurance recovery.

Figure 8 shows a clear divide between councils that are rebuilding assurance and those falling behind. This divergence reflects governance focus and capacity – not body type – and highlights where recovery risks are becoming entrenched.

Three lines of defence

In some councils there is a clear need for Audit and Risk Committees to reinforce internal control and the "three lines of defence."

These councils must resolve basic control failures (e.g., reconciliations, journal authorisation, asset registers).

Ensure internal audit provides independent and effective assurance, rather than compensating for weak first-line controls.

Where readiness is weaker, the same mechanisms work in reverse

We reported on around 280 internal control weaknesses across councils, with the number and severity weighted towards the less well-prepared bodies. Many of the recommendations reflect the scale of challenges impacting these bodies in capacity, systems and financial governance.

A key objective of our audit reporting is to add value by supporting the improvement of the use of public money. We aim to achieve this through sharing our insights from our audit work, including observations in relation to where processes can be improved and the pace of improvement, including the effectiveness of response to prior year recommendations. This approach allows us to assess how effectively councils are governed and are addressing fundamental risks.

External audit forms part of the independent assurance that councils and their Audit and Risk Committees use to assess the effectiveness of the internal control environment. Every council should have its own arrangements in place, typically known as the three lines of defence model, to manage risks and controls and ensure that they are performing consistently and compliantly.

CIPFA guidance on the Local Code of Corporate Governance is underpinned by the model, and on the assumption that systems are in place to ensure that:

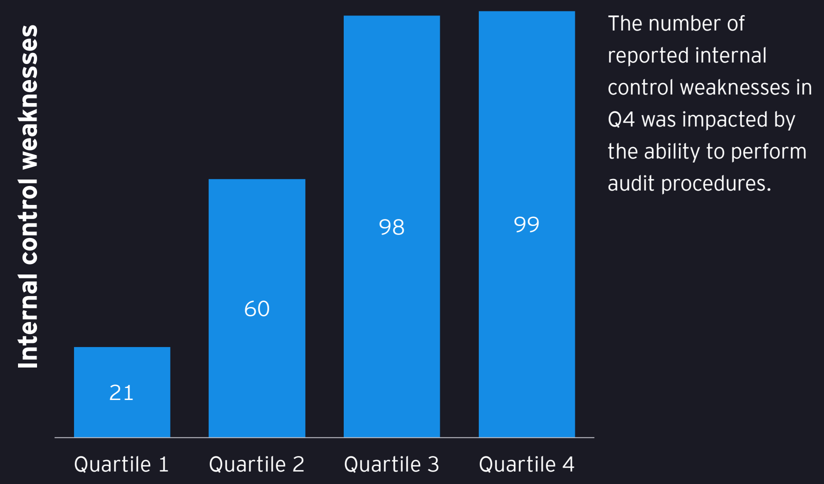
- Management manages risk where it arises, for example in rent collection and compliance or in ensuring that budget monitoring controls work effectively.
- Oversight functions such as IT security and Finance provide support and challenge.
- Internal audit provides independent assurance and cannot therefore act as a layer of management or review.

However, too often, the recommendations that are made within our audit reports reflect basic control failures that indicate weaknesses in day-to-day governance and risk management. Some of the examples of internal control failings that we identified include:

- Failure to conduct bank reconciliations (five councils)
- Failure to reconcile suspense accounts (three councils)
- Inadequate review or authorisation of journals (10 councils)
- Significant weaknesses in fixed asset register controls, including maintenance of the fixed asset register, valuation errors and reconciliation to the general ledger
- Weaknesses in contract management arrangements

Significantly, there were widespread problems with the implementation of a new International Financial Reporting Standard on Leases in 2024-25 – we were unable to complete audit procedures for two-thirds of councils.

Figure 9
The level and seriousness of internal control weaknesses was higher in less well-prepared councils.



Significant weaknesses in value for money arrangements were much more likely in the same councils that were not prepared for the audit.

Most of our value for money findings related to governance (46 weaknesses). Of those, around 37% related to the councils ability to support the financial reporting process, including the preparation of financial statements and were therefore over-represented in Quartile 4. All of the statutory recommendations that we raised impacted the councils in Quartile 4.

Other areas of weaknesses included:

- Contract management and procurement weaknesses (impacting eight councils).
- Housing standards including regulatory findings (11 councils).
- Financial resilience, including reliance on extraordinary financial support (three councils).
- The capability and capacity of the finance team (four councils).
- For four councils, the Chief Internal Auditor had provided limited assurance over internal control arrangements.

Invest selectively in capability and systems

Address skills gaps, capacity pressures and reliance on a small number of individuals.

Reduce dependence on manual workarounds by improving underlying financial systems and data quality.

Readiness should now be actively governed as an indicator of the effectiveness of financial governance arrangements

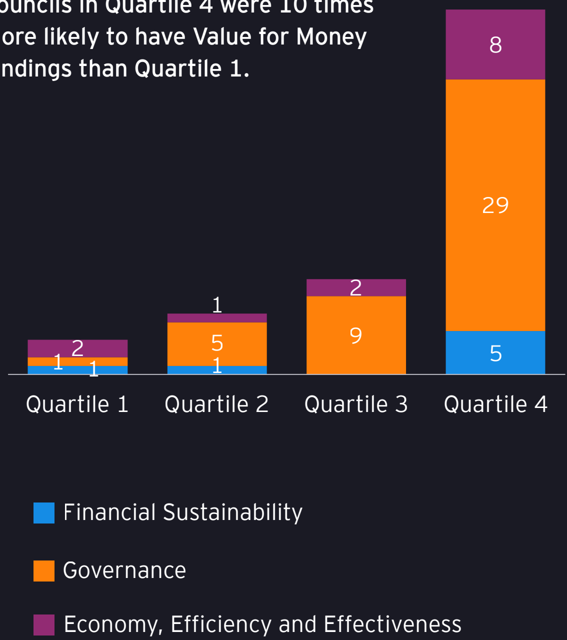
For councils that are behind the recovery trajectories set out in LARRIG 01, audit readiness should be treated as a standing governance risk, not an annual process issue.

In practice, this means:

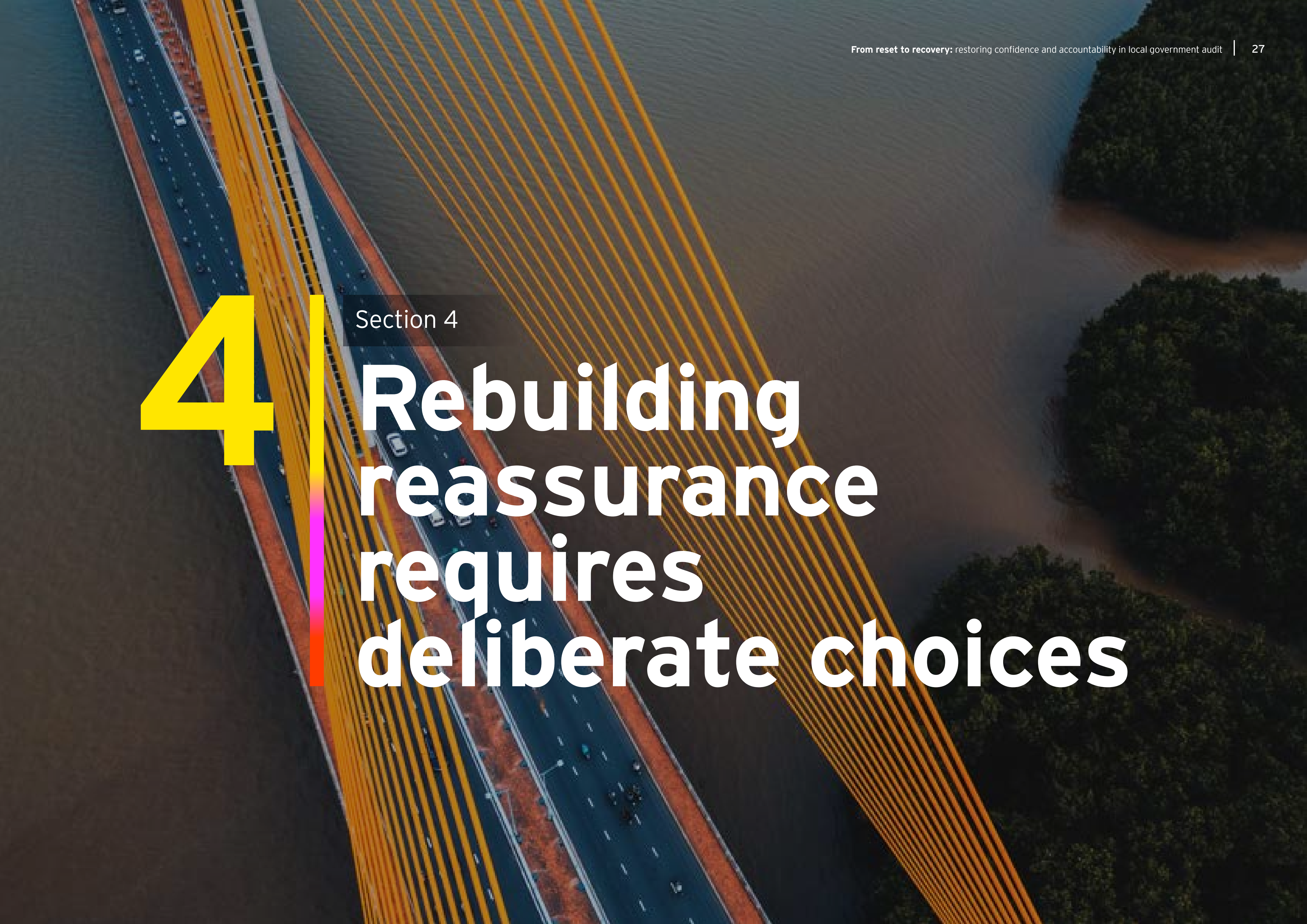
- Audit and Risk Committees should receive early visibility of readiness assessments, not just 'after the event' year-end outcomes from auditors.
- Readiness assessments should inform resourcing, prioritisation and use of Internal Audit.
- Persistent weaknesses in readiness should trigger targeted intervention, not repeated acceptance of delayed assurance.

Taken together, our findings show that assurance recovery is no longer primarily a technical or system issue. It is a question of governance focus, leadership capacity, and deliberate prioritisation. The next phase of recovery therefore depends on what councils, auditors, and system leaders choose to do next.

Figure 10
Councils in Quartile 4 were 10 times more likely to have Value for Money Findings than Quartile 1.



All of the statutory recommendations that we raised in 2024-25 related to the Councils in Quartile 4.



4

Section 4

Rebuilding reassurance requires deliberate choices

4. Rebuilding reassurance requires deliberate choices

Recovery is achievable – but it requires active governance and targeted system support

The evidence from 2024-25 shows that most councils are capable of rebuilding assurance within the current framework, although risks remain for the expectations around timelines for completion set out by MHCLG. Where recovery is stalling, councils and system leaders need to make deliberate choices about governance focus, capability and prioritisation. Without this, uneven recovery risks becoming entrenched.

Audit and Risk Committees and system leaders each have a distinct role to play in ensuring that recovery trajectories remain realistic, proportionate and focussed on restoring confidence – not simply meeting deadlines.

Assurance recovery must be actively managed, not left to run on default

Our 2024-25 audit experience indicates that assurance does not rebuild evenly or automatically. Without deliberate prioritisation, existing gaps risk becoming entrenched. The rebuild phase therefore requires explicit choices about where resources are focussed, how progress is assessed, and how risks to recovery are identified early.

One of the unique aspects of local government organisations is that the skills and knowledge within governance arrangements are based on the democratic make up of the council. Audit and Risk Committee members often have limited experience of financial or corporate governance, and are being asked to scrutinise financial statements that many people do not understand. Until the statutory support framework was introduced, the use of disclaimer opinions was extremely rare and the subsequent build-back process is technically challenging to implement and explain to lay-members.

The rebuild phase now determines whether local government can restore confidence in how public money is governed and accounted for. That outcome will depend less on rules and timetables – and more on leadership, capability, and sustained attention to assurance. As a result, we looked at some of the best councils, to assess what they had done differently to stay ahead of LARRIG timescales and to improve the level of assurance that Audit and Risk Committees could take from the audit process.

The most progressed councils had engagement and buy-in to the audit process within key relationships

The first consistent factor in councils that are ahead of LARRIG 01 timescales relates to people, including the engagement and buy-in to the audit process by the Section 151 officer and their team. This includes:

- Engagement in the finance process at the top tier of the Council, including the Section 151 officer.
- An appropriately resourced finance team with good capability.
- Regular reporting to members including explanation of key areas of difficulty and plans to recover.
- Good understanding of finance issues across the council and the financial implications of policies and projects.

In addition, council finance teams need to be able to robustly explain and document key judgements, including valuation assumptions. Often this involves a strong working relationship with other parts of the council, including the estates team.

This is increasingly challenging for councils to achieve. Our own research points to the growing demands placed on finance teams as a central actor in service design, transformation, capital investment and organisational survival. This growing influence is being exercised under extreme strain. Severe recruitment and retention pressures mean that too much of the system now rests on small numbers of highly skilled individuals often operating at capacity.

Our survey found that 90% of councils are concerned about the ability to attract and retain talent within the finance function. This creates risks of the loss of corporate memory, technical depth and independent challenge that councils increasingly depend upon.

Steady and effective financial systems underpin the recovery

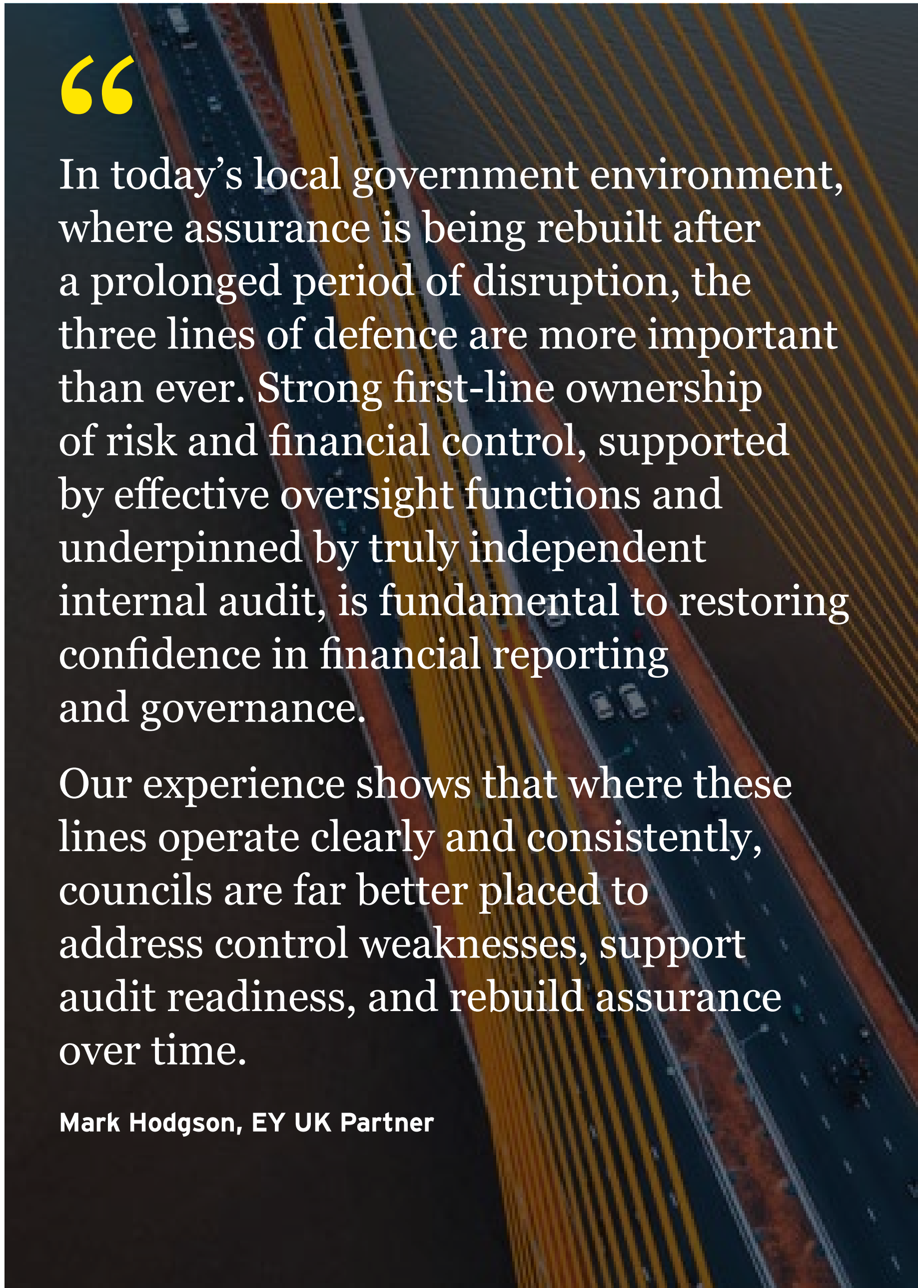
The underlying financial systems need to reflect the complexity of local government accounting without the need to deploy manual, wraparound systems.

Many of these factors relate to our benchmarks for auditability (the end state that the build-back programme is aiming to reach). The ability to perform an audit depends on access to complete, accurate and reliable data. This means that the council must be able to provide evidence for balances and transactions from underlying records.

Digitised datasets are a prerequisite for data-enabled audit techniques, deployed by EY audit professionals globally. Reconcilable and complete populations allow:

- Analytical procedures
- Full-population testing
- Identification of anomalies

However, we note that the quality of data in local government audits means that only around 38% of councils can support full data sets that can be easily audited. Collectively, local government should demand more from the systems they deploy.



> “In today’s local government environment, where assurance is being rebuilt after a prolonged period of disruption, the three lines of defence are more important than ever. Strong first-line ownership of risk and financial control, supported by effective oversight functions and underpinned by truly independent internal audit, is fundamental to restoring confidence in financial reporting and governance.
>
> Our experience shows that where these lines operate clearly and consistently, councils are far better placed to address control weaknesses, support audit readiness, and rebuild assurance over time.
>
> **Mark Hodgson, EY UK Partner**

Internal controls must be designed, documented and repeatable

The council's internal control arrangements — one of the three lines of defence that are put in place to protect the organisation from risk — must be operating well, not merely intended.

The council must also have effective internal audit arrangements to provide independent assurance about the effectiveness of controls, highlighting areas of concern and allowing weaknesses to be addressed prior to the external audit process.

System leaders need to address a financial reporting framework that does not work for the sector

Local government financial statements are too difficult to understand and often cannot answer the questions that elected members need the answers to. The risk is that financial statements become a compliance exercise rather than a management tool, increasing error rates and reducing ownership.

We support CIPFA/LASAAC's plan to reform financial reporting but we believe more immediate and substantive modifications are essential in the short to medium term to support the sustainable recovery of timely local government financial statements production and audit processes. These would include:

- Whether the benefit of accounting for operational PPE at current value justifies the cost, even after the move to quinquennial valuation supported by indexing.
- The need to account for adjustments between the accounting basis and funding basis.
- Consideration of accounting for the Local Government Pension Scheme (LGPS) as a defined contribution scheme. This would reduce the necessity for extensive actuarial input, and decrease the number and complexity of disclosures required in the financial statements.

The urgency for simplification is heightened by anticipated local government reorganisation, which will introduce further short-term demands on both financial statements preparers and auditors. For merged bodies, the status of the financial statements will be constrained by the weakest assurance position among the constituent bodies. The impact may include the need for extended audit effort and procedures precisely when audit readiness is most fragile, raising the risk of further delays or modified opinions. Ultimately, uneven recovery trajectories could become entrenched as assurance gaps are combined.

5

Section 5

Priorities for the year ahead

What Audit and Risk Committees can do now

If the system continues to judge success by timeliness alone, assurance recovery will remain fragile and uneven. The priorities for the year ahead must therefore focus explicitly on rebuilding confidence, not simply issuing opinions.

1 Treat audit readiness as a standing governance risk

Audit readiness should no longer be viewed as a year-end process issue. For councils that are behind recovery trajectories, it should be:

- Explicitly recognised as a strategic governance risk.
- Monitored with the same level of discipline that we would expect to be applied to financial resilience or Value for Money concerns.

In practice, this means:

- Receiving early and regular reporting on audit readiness, not just final audit outcomes.
- Understanding which balances and assertions remain unaudited and why.
- Tracking progress against recovery milestones including assurance across specific areas of the financial statements, not just statutory deadlines.

2 Prioritise finance capacity and stability

The evidence from 2024-25 shows that recovery is strongly correlated with:

- Stable finance leadership.
- Adequate capacity within finance teams.
- Access to specialist expertise where required.

Audit and Risk Committees should:

- Challenge whether finance functions are realistically resourced to deliver recovery alongside the wider corporate roles that they must play.
- Support targeted investment where it unlocks assurance progress.

3 Judge success by restored assurance

- Look beyond whether an opinion was issued.
- Understand what assurance sits behind that opinion.
- Focus on whether communities, elected members and stakeholders can rely on the financial information presented.

Key actions for the Section 151 Officer:

1. **Provide visible leadership of assurance recovery**
   - Personally sponsor the audit recovery agenda and communicate clearly with Members on progress, risks and trade-offs.
   - Ensure early and ongoing engagement with external audit throughout the year.

2. **Embed audit readiness into routine management**

   Ensure robust, repeatable processes exist for:
   - Key judgements and estimates
   - Valuations and reconciliations
   - Evidence retention over multiple years

   Treat readiness as a reflection of overall financial governance maturity.

3. **Invest selectively in capability and systems**

   Address skills gaps, capacity pressures and reliance on a small number of individuals. Reduce dependence on manual workarounds by improving underlying financial systems and data quality.

4. **Act early where recovery is stalling**

   Where the authority is behind LARRIG recovery expectations, initiate targeted intervention rather than relying on future audit cycles to resolve gaps. Ensure that unresolved assurance issues do not compound, especially ahead of reorganisation or structural change.

“

Rebuilding audit assurance is never achieved by process alone — it is built through leadership, partnership and trust. Engaged Section 151 Officers lead an open, constructive dialogue with both auditors and Members create the conditions for real progress. By investing in capability, embracing transparency, and working collaboratively towards a shared goal, some councils show how confidence can be restored and assurance rebuilt, step by step.

Ben Lazarus, EY UK Partner

Key actions for system leaders:

1. **Shift success measures from timeliness to assurance**

The system narrative so far has worked – 'backlog cleared' now needs to evolve to explicit measures of assurance recovery, recognising that widespread disclaimer opinions represent a material loss of public assurance. Without a shift in success criteria, recovery risks being superficial and uneven.

2. **Target support to councils at risk of entrenched assurance failure**

In our view, there is a cohort of councils that fall materially behind recovery trajectories and will be unable to meet the current deadlines for unqualified opinions set in LARRIG 01. Targeted, sustained intervention should be provided for this group, rather than relying on the audit process alone to resolve structural problems. This could include finance capacity funding or support packages and/or enhanced oversight where local governance is demonstrably fragile.

We support the continued prioritisation of audit resource based on public interest and deliverability, and therefore on where assurance recovery is realistically achievable. There is therefore a need to ensure that councils with persistent weaknesses are not silently deprioritised without alternative support mechanisms in place.

3. **Accelerate reform of the local government reporting framework**

In our view, the current IFRS-based framework is not proportionate to the sector's financial reporting capacity and undermines ownership, auditability and understanding. As a result, financial reporting simplification should be treated as a recovery-critical intervention, not just a long-term improvement project. There is a real need to progress and expand CIPFA/LASAAC reforms, including:

- Further simplification of PPE valuation requirements
- Reduced emphasis on accounting treatments that have no funding or service consequence
- Reconsideration of LGPS accounting complexity

4. **Strengthen the role and capability of Audit and Risk Committees nationally**

We would welcome a step-change in Audit and Risk Committee effectiveness through:

- Enhanced national guidance focussed on post-reset responsibilities
- Targeted development support for members dealing with disclaimed and qualified opinions
- Clearer articulation of Audit and Risk Committees' role in overseeing multi-year assurance recovery

5. **Plan for reorganisation with assurance risk explicitly in view**

Structural change cannot "reset" assurance; we instead need to plan for extended recovery periods where assurance gaps are inherited. Local government reorganisation requires early assessment of:

- The weakest assurance positions among constituent bodies
- The compounded audit and reporting risks created by mergers

Appendix A

The rebuilding process: assurance carry-forward

2023-24:

Disclaimer opinions pervasive

- Pervasive gaps over opening balances, comparators, and in-year movements.
- Lack of assurance over Property, Plant and Equipment (PPE) valued on a cyclical basis, from the 2022-23 audit.
- Lack of assurance over reserves.
- Auditor focus on in-year transactions together with closing balances such as cash, debtors and creditors. By adopting this approach, the assurance gap is at least not deteriorating.

2024-25:

Disclaimer opinion remains most likely outcome

- Expected lack of assurance over comparator balances from 2023-24.
- Continuing pervasive gaps in reserves and PPE assurance.
- Audit procedures to rebuild assurance over opening balances and year end closing balances.
- Increasing time and evidence pressure on finance teams to support.

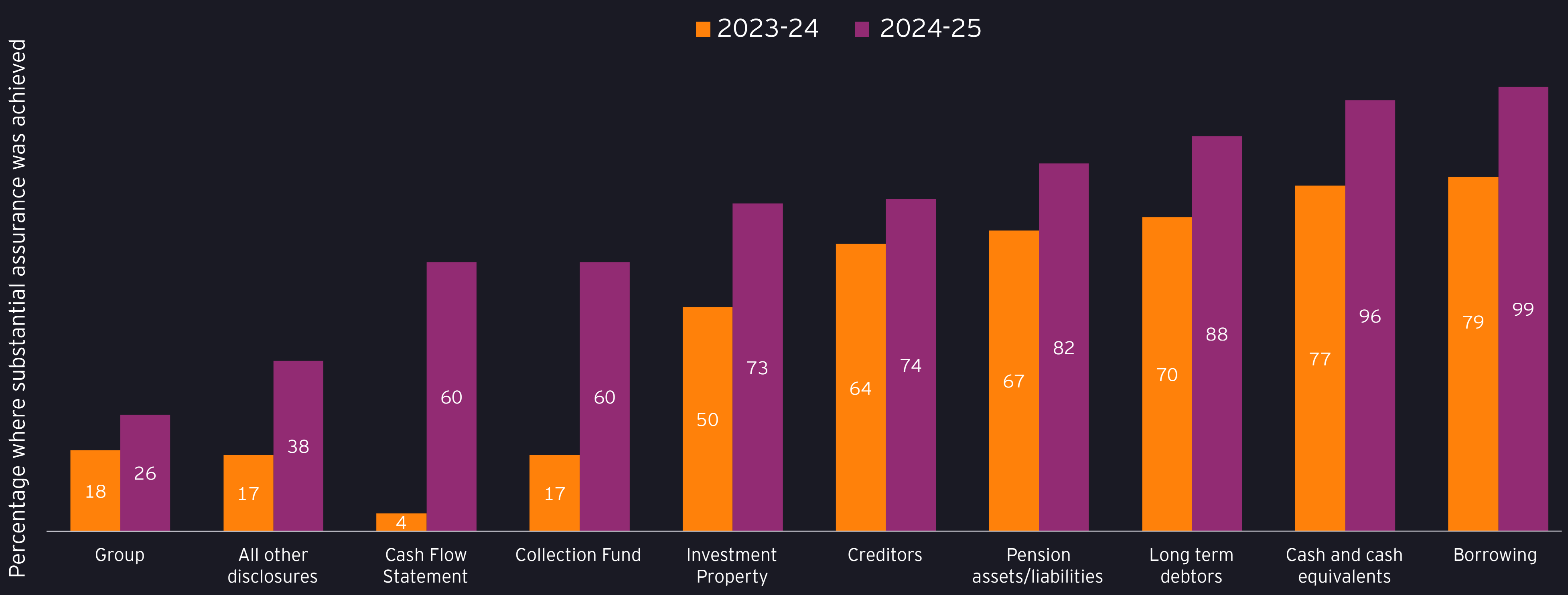
2025-26 - 2026-27:

Moving towards Qualified (except for) opinions

- The aim is that assurance will be in place over opening and closing balances and assurance gained over each in-year movement.
- Likely gaps will remain over PPE due to the extent that items have not been valued since 2022-23.
- Impact on income and expenditure balances and reserves assessed on an individual basis.
- Increasing probability that the gaps in audit procedures can be specifically identified leading to a higher likelihood of a qualified opinion.

Timescales outlined in LARRIG 01

Appendix B
The ability to complete in-year procedures significantly improved in 2024-25.



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