EXPLANATORY MEMORANDUM TO

THE LOCAL AUDIT (AMENDMENT OF DEFINITION OF SMALLER AUTHORITY) REGULATIONS 2025

No. [XXXX]

1. Introduction

1.1 This Explanatory Memorandum has been prepared by the Ministry of Housing, Communities and Local Government and is laid before Parliament by Command of His Majesty.

1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Declaration

2.1 Jim McMahon MP, Minister of State at the Ministry of Housing, Communities and Local Government confirms that this Explanatory Memorandum meets the required standard.

2.2 Rosie Seymour, Deputy Director for Local Audit Reform at the Ministry of Housing, Communities and Local Government confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Sophie Squibbs at the Ministry of Housing, Communities and Local Government or email: sophie.squibbs@communities.gov.uk can be contacted with any queries regarding the instrument.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 The instrument amends the definition of a 'smaller authority' in section 6(2) of the Local Audit and Accountability Act 2014 ("the 2014 Act").

Where does the legislation extend to, and apply?

4.2 The extent of this instrument is England and Wales.

4.3 The territorial application of this instrument is England only.

5. Policy Context

What is being done and why?

5.1 Local audit is the process of independently checking the accounts and financial arrangements of local public bodies, such as councils and other authorities. It ensures that public money is being properly managed, spent legally, and accounted for correctly. Local audit usually requires the preparation of financial statements, review by an external auditor, and sometimes a public inspection period. Smaller authorities, defined as those with an annual income and expenditure below £6.5 million, are

subject to a more streamlined process that enables them to prepare and submit an Annual Governance and Accountability Return (AGAR) rather than full financial statements, helping to reduce the administrative burden while still ensuring transparency and accountability.

5.2 On 18 December 2024, the government published a strategy[1] and consultation setting out plans to overhaul the local audit system. On 9 April 2025 the government published the response to the consultation[2]. The strategy intends to overhaul the broken local audit system and commits to a number of measures to achieve this, including a review of the audit framework for smaller authorities in response to concerns about capacity and proportionality. This instrument amends the audit thresholds for smaller authorities. This will reduce costs for the authorities who will benefit from this change and help to reduce pressure on the current local audit backlog.

5.3 Many small authorities do not have the same size, responsibilities, or risks as larger authorities. Raising the audit threshold to £15 million means these smaller authorities will not be required to pay for audits that they do not really need and auditors can focus where they are most needed. Previously, some smaller authorities briefly went over the threshold, often due to one-off grants, and then fell back below it. This resulted in a significant increase in costs. The higher £15 million threshold keeps more bodies under simpler audit arrangements. The change helps save public money, reduce pressure on the audit system, and keep things proportionate for smaller public bodies.

What was the previous policy, how is this different?

5.4 The previous threshold for a smaller authority was £6.5 million and had not been changed since 2014. The threshold has been raised to £15 million to ensure smaller authorities will not inadvertently end up in the principal audit regime which is disproportionate to their level of risk and financially burdensome.

6. Legislative and Legal Context

How has the law changed?

6.1 Currently, under section 6 of the 2014 Act, a relevant authority (defined in section 2 of the 2014 Act) is a smaller authority for a financial year if the higher of its gross income and gross expenditure for the year does not exceed £6.5 million for that financial year, or in relation to either of the two prior financial years. This instrument will provide that in relation to a financial year beginning on or after 1 April 2025, this threshold will be £15 million.

Why was this approach taken to change the law?

6.2 Amending the existing legislation was the only possible approach to make the necessary changes.

[1] https://www.gov.uk/government/consultations/local-audit-reform-a-strategy-for-overhauling-the-local-audit-system-in-england/local-audit-reform-a-strategy-for-overhauling-the-local-audit-system-in-england
[2] https://www.gov.uk/government/consultations/local-audit-reform-a-strategy-for-overhauling-the-local-audit-system-in-england/outcome/local-audit-reform-government-response-to-the-consultation-to-overhaul-local-audit-in-england

7. Consultation

Summary of consultation outcome and methodology

7.1 The December 2024 consultation cited in section 5.2 included a six-week online consultation on proposals to overhaul the current local audit system in England. 239 responses were received via an online survey and email submissions. All responses were given full consideration, including where they provided views and commentary beyond the questions themselves, alongside other representations made during the consultation period. This included a meeting between system and sector leaders and the Minister of State for Local Government and English Devolution, as well as additional engagement and workshops on specific areas.

7.2 The consultation asked, 'Do you agree that smaller authorities' thresholds should be increased?'. 132 (55%) respondents agreed with the proposal, 23 (10%) respondents disagreed with the proposal and 84 (35%) respondents did not answer this question or did not have a view. Many respondents agreed that thresholds should be increased to ease the financial and administrative burden on smaller bodies.

7.3 On the 9 April 2025 the government published the response to the consultation which committed to raise the upper audit threshold for smaller authorities.

8. Applicable Guidance

8.1 No formal guidance will be issued by the Ministry of Housing, Communities and Local Government on implementing these regulations.

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A full Impact Assessment has not been prepared for this instrument because this instrument is related to updating existing regulatory standards.

Impact on businesses, charities and voluntary bodies

9.2 There is no impact on business, charities or voluntary bodies as this legislation applies to the audit threshold of smaller authorities.

9.3 The legislation does not impact small or micro businesses.

9.4 The impact on the public sector is limited. The amendments made by this statutory instrument ensure financial and administrative burden on smaller bodies are reduced.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 The approach to monitoring this legislation is that MHCLG, in liaison with key stakeholders, will keep the effect of these amendments under review.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 None

12. European Convention on Human Rights

12.1 The Minister of State, Jim McMahon has made the following statement regarding Human Rights:

"In my view the provisions of The Local Audit (Amendment of Definition of Smaller Authority) Regulations 2025 are compatible with the Convention rights."

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 ("relevant European Union Acts").