Value for money and accountability: a report on the Birmingham City Council section 114 bankruptcy

Report authors:

Dr James Brackley

James is a Lecturer in Accounting at the University of Sheffield and member of the Audit Reform Lab. He is an ICAEW Chartered Accountant, qualifying in the Public Sector practice of PwC in 2012. His PhD thesis was on the use of the ringfenced public health grant in local authorities in England. He has extensive teaching experience Audit, Financial Reporting, and Public Sector Accounting, and is leading an ICAEW funded research project on audit quality in the Big-4 Accounting firms. He is also an advisory member of the Sheffield City Council Audit and Standards Committee.

Professor Adam Leaver

Adam is Professor in Accounting and Society at the University of Sheffield, Director of the Centre for Research on Accounting and Finance in Context (CRAFIC), and founder of the Audit Reform Lab. He also has a fractional position at Copenhagen Business School.

Acknowledgements

This report is written by Dr James Brackley and Professor Adam Leaver as part of the Audit Reform Lab at the University of Sheffield. It has been co-commissioned by UNISON, Unite, and GMB.

Executive Summary

This report analyses the financial situation at Birmingham City Council and the factors that led to the issuance of the section 114 notice in September 2023. We find that the financial problems were initially attributed to a prematurely disclosed and potentially overstated equal pay liability. This attribution deflected public attention from i) ongoing service level pressures that resulted from austerity budgets and increased demands after the Covid pandemic, and ii) the disastrous implementation of a new 'Oracle Cloud Fusion' IT system ('Oracle', hereafter). As a result of this attribution, the government initiated a process that would lead to deep cuts and asset sales that raise serious concerns about best value and financial sustainability.

Our core finding on the revenue budget is that the city is now cutting capacity in crucial front-line services to pay for a temporary overspend on a failing IT system. On the capital budget, a 'fire sale' of £750m worth of assets was initiated to pay for an equal pay liability that remains speculative and unaudited. In terms of public accountability, we find that there was little public consultation on either the 2024/25 revenue budget or the asset sales. The resultant proposals, pushed through under statutory direction, are likely to lead to a breach of the Council's statutory duties, undermine business-critical operations, and contribute to cost spirals and worsening outcomes for the city. At the end of the current period of capitalisation support (April 2026), the city will still be left with substantial deficits and may struggle to set a lawful budget without further support.

We suggest that by refocusing the intervention away from cost-cutting and asset sales, to focus instead on best value delivery, that there is a more supportive route to recovery for Birmingham. We therefore recommend that the current capitalisation direction be redrawn and extended to April 2028, capitalising against the costs of the Oracle IT system because Oracle seems the more likely explanation of Birmingham's problems (see section 6). Adding the caveat that our proposals are based on publicly available information, and that final details may need to be revised if new information arises subsequently.

Our revised capitalisation direction would set the revenue budget on an evidence-based approach through to April 2028, with future proposals impact-assessed up to that date and subject to proper public consultation. We would advise against any fire sale of assets that simply underwrite transfers between reserves, recommending that asset sales are only advisable where they have a demonstrably net positive impact on the revenue budget (i.e. the sale of loss-making assets only).

Finally, in compiling this report, we found a central ambiguity around the status of the equal pay liability figure of £760m, which appeared to be both unaudited by Grant Thornton yet unquestioned by key actors, often after receiving correspondence from the auditor. Getting to the bottom of that process, whereby a sense of certainty can be created around an unaudited liability figure, to the extent that a council is deemed to be bankrupt, should be an important matter of public concern with regard to transparency and accountability at the council. This is not to suggest the council is in otherwise good health, but rather that the causes of the financial problems at Birmingham City Council may require different kinds of solutions. To that end, we recommend that further investigations are needed to address these concerns.

Recommendations for a revised intervention in Birmingham City Council:

(1) An independent audit of the equal pay liability and a review of potential threats to auditor independence See section 5.

(2) A restructuring of the exceptional financial support package – capitalising against the cost of Oracle rather than equal pay, and extending the period of the support package to April 2028. See section 6.

(3) Proper public consultation on the 2025/26 budget from the Autumn of 2024 and for proposals to be put forward on a demonstrable best value rather than cost reduction basis. See section 7.

(4) An independent inquiry into the issuance of the section 114 notice in September 2023 and whether the Secretary of State followed the government's own best value guidelines. See section 8.

Questions for a future inquiry

We encourage stakeholders and any future public inquiry to ask the following questions:

(1) Why was the extent of the Oracle IT disaster not disclosed to Council Committees until mid-2023, more than 12 months after 'go live'?

(2) Why did central government not conduct the usual best value assessment to properly understand the financial situation prior to statutory intervention in September 2023?

(3) Why did the auditors not make it clear in their statutory recommendations of September 2023 that the equal pay liability was unaudited and that they had not obtained the equal pay model upon which the £760m liability value was based?

(4) If the auditors had not audited or confirmed the £760m equal pay figure, as they claim, then why did Michael Gove assure parliament that it was "the independent auditor's assessment that the revised estimated equal pay liability is likely to be more than £760 million"?

(5) How does the Council intend to improve outcomes, as per the Improvement and Recovery Plan, when making deep cuts to the services in need of investment?

(6) Will the Council be transparent with residents if the cuts in the 2024/25 budget lead to a failure to deliver statutory services or a failure to comply with statutory duties?

(7) How will the Council avoid a further section 114 in April 2026 if it has not yet fully implemented the new Oracle system and is still running significant deficits?

(8) Why are the Council pressing ahead with asset sales to pay for an equal pay liability that the lead Commissioner is on the record as saying is overstated?

Contents

1. Introduction

This report has been commissioned to investigate the accountability and value for money arrangements at Birmingham City Council leading up to, and immediately following the Council's section 114 ('s114') notice, issued in September 2023. The section 114 paved the way for the largest ever cuts to a local authority budget, with £149m cut from the 2024/25 budget, assets sales of £750m, and a capitalisation direction of £1.255 billion. Yet, behind these events lie a number of questions about the basis for Birmingham City Council's section 114 and the subsequent 2024/25 budget, and the speed with which these interventions were pushed through.

The background to the section 114 notice begins with the Council's recognition of a £760m equal pay liability that was immediately identified as the primary cause of the city's financial problems. That liability appeared in the council's own explanation of the section 114, which identified the equal pay liability as the primary cause of the Councils problems; a claim recycled widely in the press.

Shortly after the s114 was issued, Central Government moved swiftly to impose the most severe form of intervention, a Commissioner-led statutory intervention. They did not provide the Commissioners with the usual three-month period to assess the notice, nor was there a robust best value assessment prior to the appointment of the Commissioners. Instead, the budget cuts and asset sales were introduced with very little public consultation; and progressed with limited consideration of the cause of the City's budget deficits – whether they were structural deficits resulting from historical overspends or temporary deficits resulting from one-off problems.

Worryingly, these cuts and asset sales were progressed in a context of uncertainty around the quality of financial information used to justify these interventions. The council's annual reports had not been signed off by the auditor; neither had the £760m equal pay liability. Remarkably, the external auditors concluded in January 2024 that "reliance could not be placed on the most basic of financial information[1]" produced by the council. This suggests deeper problems around internal controls and audit failure. That these cuts and asset sales were sanctioned with little reliable financial data raises important public interest questions.

Cuts and sales on this scale unavoidably create disruption and social harms. In this case, the cuts have the potential to create far-reaching disruption to services and strategic level outcomes[2]. At the same time, the scale and immediacy of the asset sales may result in the fire sale of revenue generating assets, providing poor value for money for the council and its public users. Cuts and asset sales can also pose longer-lasting risks if they

[1] Cited in the external audit reports to the Audit Committee, and in the section 151 officer's section 25 report;

[2] https://auditreformlab.group.shef.ac.uk/financial-crisis-in-birmingham-city-council/

decrease the council's ability to run balanced budgets in the future, creating 'cost spirals'[3]; for example, when cuts to revenue generating activities or business critical operations mean less income is available in the future to service a growing level of demand. Similarly, cuts to prevention and early intervention, or statutory services such as SEND services, home school transport, homelessness and adult social care may simply create new, larger costs in different parts of the Council budget down the line.

In this context it is important to identify the proper cause of the city's difficult financial position because it guides perceptions about the nature of the problem and what needs to be done to resolve it. This is important because there is an emerging counter-narrative about the causes of the council's problems – one rooted in the introduction and implementation of a new Oracle IT system, which generated significant in-year costs that ate into revenue budgets. This, combined with ongoing challenges around austerity budgets promote a quite different story about the causes of the council's financial position which demand different policy responses; not least because if the problem is in part austerity, then more austerity is unlikely to solve anything. Similarly, if the problem is temporary cash overspends due to the poor and costly implementation of an IT system (rather than speculative, prospective future liabilities), then a financial package that capitalises against the cost of Oracle going forward may be more workable and less damaging.

Finally, if the problems were amplified by poor transparency and accountability matters, that too requires a policy response – this should include careful consideration of the role played by the external auditor, together with reforms to the audit, reporting, and best value regimes in the local government sector.

To address these questions, this report digs deeper into a variety of publicly available sources: the accounts of Birmingham City Council, various Audit Committee and Cabinet papers, the 24/25 budget proposals, the section 151 officer's section 114 notice and section 25 report, as well as various audit reports, annual accounts, and other relevant public documentation. To gain more insight, we have also attended public meetings and spoken to a range of stakeholders as background to our analysis. We note that the figures presented in this report rely on publicly available information, which is reflected in our analysis. Data not currently in the public realm may show other financial black holes. In that scenario, further work would need to be conducted before finalizing any revised capitalization direction.

The remainder of the report is structured as follows. Section 2 outlines the context of austerity and rising service demand in many UK local authorities. Section 3 locates the Birmingham case within this context of local authority austerity. Section 4 introduces the problems of the Oracle IT system which compounded those issues, creating larger

[3] https://auditreformlab.group.shef.ac.uk/accountability-crisis-at-bcc/

problems and costs. Section 5 looks more deeply at the role of the auditor in the Birmingham case. Section 6 presents our proposals for redrawing the Council's 'capitalisation direction'. Section 7 reviews the value for money and public accountability arrangements at Birmingham, before briefly summarising recent calls for an independent inquiry in section 8.

Finally, in writing this report we note the considerable financial crisis that is developing across the local government sector. Birmingham finds itself in a position similar to that faced by many other city and metropolitan authorities. This report is therefore an important case study on the current inadequacy of the funding, auditing and best value system in Local Government, and the need to properly support failing authorities on their journey to recovery.

2. The crisis in local government finances and the need for sector-wide funding reform

It is well documented that local government finances are in crisis. A SIGOMA survey[4] last year found that one in ten Councils were close to issuing section 114 bankruptcy notices, while the number of Councils receiving 'exceptional financial support' via 'capitalisation directions' has grown to 19[5]. The Local Government Association (LGA) recently reported that the sector is facing a £4 billion funding gap through 2024/25 and 2025/26[6], with a subsequent report from the Levelling Up, Housing and Communities Committee[7] outlining the reasons – a chronic underfunding of services; the failure to implement the Fair Funding review; inflationary pressures; and the spike in demand across Adult Social Care and Children's Services.

In February 2024, shortly after that report, the Department for Levelling Up, Housing and Communities ('DLUHC') announced an additional £600m for the sector. However, the LGA found that even with this extra funding, three-quarters of Councils would still need to cut Adult Social Care budgets and seven in ten would need to cut Children's Services[8], whilst increasing council tax[9]. These financial problems are compounded by a crisis in the external audit market, with only 5 out of 467 Councils in England receiving the audits of their 22/23 financial statements on time[10].

This crisis is likely to become more severe as Councils implement new budget cuts that may prevent them from meeting their principles of prevention and early intervention, and delivering their statutory duties.

The legacy of austerity and the need for funding reform

It is important to highlight that the above deficits and resultant cuts follow more than a decade of austerity in the sector. The National Audit Office dashboard[11] shows that between 2010/11 and 2020/21 local authorities lost 26% of their spending power, with more deprived authorities with greater population-level-need losing considerably more. Birmingham City Council are listed by the NAO as losing 36% in this same period, more than £1.2 billion in real terms (at 2019/20 prices). This means that any cuts made now, either to fund the £4 billion sector wide funding gap in general or the £300m funding gap

4 https://www.sigoma.gov.uk/news/2023/one-in-ten-sigoma-councils-facing-section-114-notice
5 https://www.gov.uk/guidance/exceptional-financial-support-for-local-authorities-for-2024-25
6 https://www.local.gov.uk/parliament/briefings-and-responses/lga-submission-202425-provisional-local-government-finance
7 https://committees.parliament.uk/publications/43165/documents/214689/default/
8 https://www.local.gov.uk/about/news/councils-warn-cuts-neighbourhood-services-lga-survey
9 By way of example, the reported £300m deficit in Birmingham across 2024/25 and 2025/26, for example, (which was not included in the LGA estimates) would alone account for half of that additional £600m outlay announced for the entire sector.
10 https://www.psaa.co.uk/2023/10/october-2023-update/
11 https://www.nao.org.uk/reports/financial-sustainability-of-local-authorities-visualisation-update/

at Birmingham in particular, follow on from already acute cost pressures. Budgets have already been squeezed and there are now very few genuine efficiencies to be found in the sector, so that savings can only be made by either rises in council tax or other fees and charges, or cuts to front line (and often statutory) services.

Despite promises, funding reform has not materialised. The Fair Funding Review recommended that local authority grants should fairly adjust for population, deprivation and location, albeit with the contradictory aim of increasing (rather than decreasing) reliance on local taxation[12]. Similarly, proposals to narrow the funding gap in the Public Health grant were delayed[13], leaving the sector with year on year cuts to already regressive central government block grants, with this loss only partially made up for by similarly regressive rises in council tax. The net effect of this has been a 'levelling down' in funding – with the most deprived areas with the greatest population need taking the most significant hits to their budgets.

The latest crisis (2022-24) compounds these inequalities because the authorities with the greatest level of need are also experiencing a spike in service level demand, particularly in adult and children's social care, home to school transport and homelessness. This will push costs up, just as income falls, leaving those authorities more exposed to s114s. Those most-deprived authorities may then get caught in a downward spiral: the cuts create new social problems which increase demand for services; this leads to an s114 and enforced cuts and asset sales under punitive capitalisation directions. The asset sales may create future revenue budget deficits due to the lost income generated by them and larger future costs because of the deterioration of service. Conversely, more affluent authorities with larger council tax bases are better placed to invest their reserves in revenue generating assets to protect their revenue budgets, whilst more deprived authorities face this self-reinforcing cycle of decline.

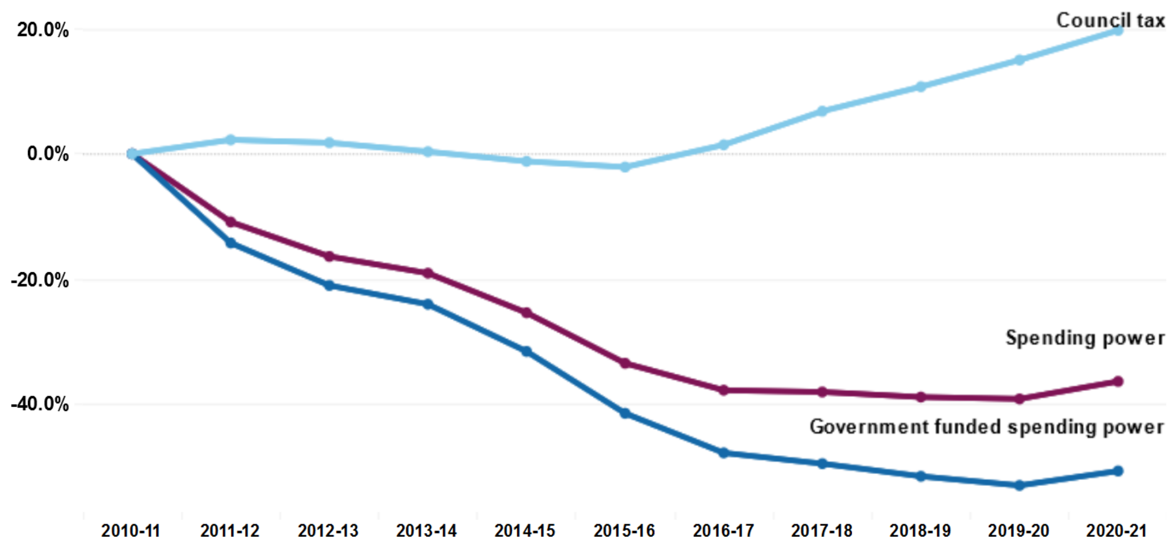
This report should therefore be read as a case study in why sector-wide funding reform, that moves away from reliance on regressive local taxation and provides a fairer distribution of sector-wide resources, is urgently needed.

[12] https://www.local.gov.uk/sites/default/files/documents/call-evidence-fair-fundin-599.pdf
[13] https://publications.parliament.uk/pa/cm201617/cmselect/cmhealth/140/140.pdf

3. Background to the Birmingham City Council case

Birmingham City Council is a case in point. It is the largest local authority in Europe. It serves a population of more than 1.1 million people across ten parliamentary constituencies[14]. In terms of funding, as a large, deprived metropolitan authority, Birmingham City Council has lost disproportionately more of their spending power: they lost 36.3% of their spending in real terms between 2010/11 and 2020/21 (at 2019/20 prices) against a sector average of 26%, despite the increased funding received during the Covid-19 pandemic in 2020/21:

Figure 1: Spending power and its components, 2010-11 to 2020-21 | Birmingham

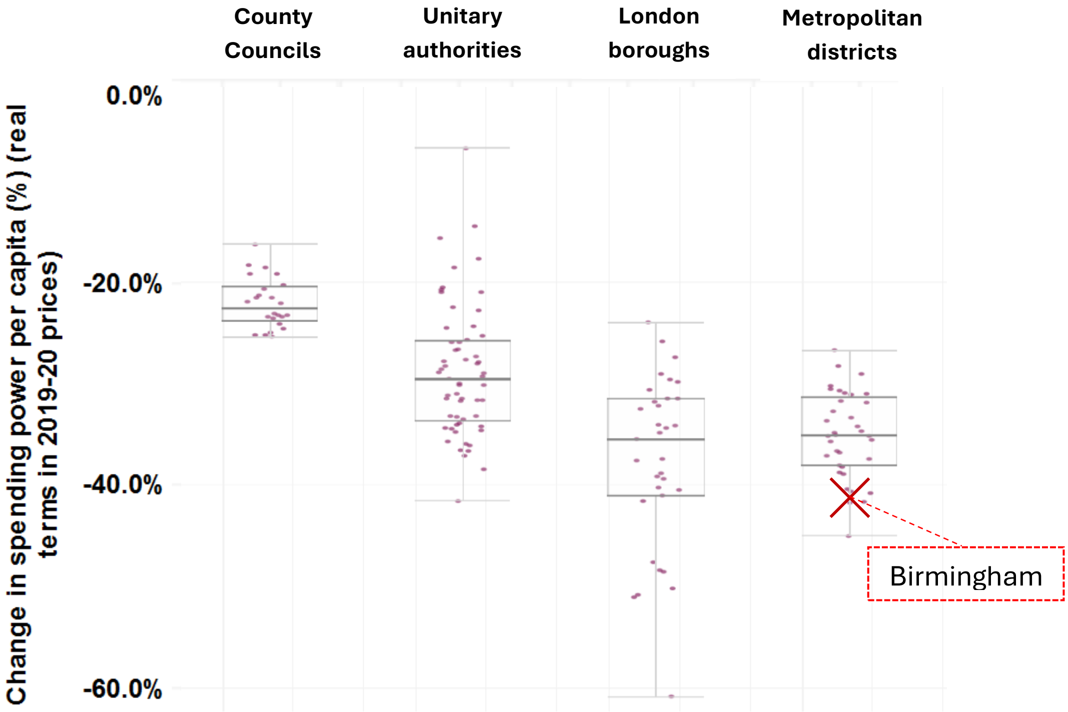


Source: NAO financial sustainability data visualisation

In this time, the local population increased by 7.5%, resulting in a fall in spending power *per head of population* of **<u>40.8%</u>**. This was amongst the very worst of any large City, County, or Borough Council (Figure 2):

[14] Leach and Copus (2023) *The Strange Demise of the Local in Local Government: Bigger is Not Better*, Palgrave Macmillan: Gewerbestrasse.

Figure 2: Change in spending power per capita by local authority type in England, 2010-11 to 2020-21



Source: NAO financial sustainability data visualisation

Birmingham has therefore experienced a significant drop in spending power while serving a growing population. On top of this, there has been a rising 'population need'. A decade of low economic growth, an aging population, high inflation and the legacy of the Covid-19 pandemic have all increased cost pressures specific to the local authority.

Economic activity in the Birmingham and West Midlands metropolitan area grew just 6.4% in the ten years to 2021, and remains below 2007 levels[15]. The population of those aged 85 years or older increased by 16.1% in the decade to 2020/21, an increase of over 3,000 residents. In the latter half of that decade child poverty rates increased from 35.5% in 2014/15 to 46.4% in 2021/22[16], and the city now has more than 2,000 looked-after children in the care system.

The cuts to services over the last decade removed crucial support services for homeless families, disabled people, elderly people, refugees and asylum seekers (including more than 200 children) and many others, and likely led directly to the spike in cost pressures experienced in 2022-24.

'Sound financial management' up to March 2022?

Despite this difficult context, Birmingham City Council managed to report a balanced budget up to March 2022, with only a relatively modest draw down on reserves. At March

[15] https://www.statista.com/statistics/1404955/gdp-per-capita-birmingham/
[16] https://www.jrf.org.uk/uk-poverty-2024-the-essential-guide-to-understanding-poverty-in-the-uk

2022 they began the year with a General Fund reserve of £596.8m having delivered on average 78% of identified savings on time per year across the previous 5 years, delivering a reported 98.3% of these savings by March 2022. Missed savings targets meant that the reserves position had weakened by only £49.5m (less than 8% of available useable reserves) and left them with an outstanding revenue budget deficit at the end of this period of just £3.2m. These would not normally be considered terrible results.

Figure 3: delivery of savings 2017/18 to 2021/22

Year	Planned savings £m	Savings delivered £m	Delivery %
2017/18	70.9	48.3	68%
2018/19	52.9	42.8	81%
2019/20	46.2	38.7	84%
2020/21	22.1	16.0	73%
2021/22	33.1	29.9	91%

Source: Birmingham City Council Financial Plan 2023-2027

These figures may now come under greater scrutiny and new evidence may arise that questions these outputs and the auditing of them, but at the time CIPFA supported this positive view, giving the Council a 3* rating in the Summer of 2021, commending the Council in their press release on the 'inspirational' journey they had taken towards 'sound financial management'[17]. The annual accounts for the year ending 31st March 2022 similarly showed, on a full IFRS accruals basis, a surplus of £85.1m on the provision of services; that the General Fund sat within a total useable reserves figure of £1.5 billion; and that the Council had a positive net cash flow of £3.1m, while making £283.8m of net investments and considerably reducing their debt in the same year.

From these publicly available sources, there is little evidence in the reported figures that the section 114 'bankruptcy' notice issued in September 2023 was the result of 'many years' of poor financial management, as was claimed by Michael Gove when he appointed the Commissioners in September 2023[18]. The audited financial information prepared under the pre-Oracle IT system (SAP) - which would have to be traced back to cash - suggests the Council had managed their financial position satisfactorily, despite some of the most severe cuts and service level pressures faced by any authority[19].

[17] https://www.cipfa.org/members/membership-benefits/cipfa-membership-matters/features/birmingham-city-council%E2%80%99s-inspirational-journey-to-a-three-star-finance-function

[18] https://hansard.parliament.uk/commons/2023-09-19/debates/6ED1706F-3B05-464C-AA7B-7D28AFEF149D/BirminghamCityCouncil

[19] It is possible that observers may question the above figures given the subsequent issues with financial control at the Council. However, there is as yet no evidence of historic issues with the accounts under the old accounting system, prior to April 2022. Auditors would have had to test those accounting transactions back to cash records or other substantive evidence under this system.

2022-24: cost pressures and growth in demand

As with many other Councils across the sector, the cost of living crisis and the legacy of Covid-19 led to an unprecedented spike in demand for crucial statutory services through 2021 and 2022 so that by 2022/23 services were becoming costlier to run. As outlined above, these pressures followed years of cuts to preventative services and the removal of many of the support mechanisms in place previously designed to keep families from becoming homeless, help young people into employment, and to improve population health and wellbeing.

Cabinet papers produced by the Council show that, due to increasing complexity and severity of cases, the average unit cost of care in Children's services increased by 8.5% in 2016-2020 and then by 11.6% in 2020-2022. Meanwhile, the unit cost of residential care increased 18% in 2020-22 while the unit cost of supported accommodation rose by 72% in 2020-22. On top of these unit cost increases, the number of Children in care rose from 1,817 at March 2018 to 2,221 at March 2023, while the number of both older people and young adults with complex needs saw average increases in demand of 5% per year through the same period.

An £11m overspend was cited in 2023/24 against the budget for temporary accommodation as the number of bed and breakfast placements increased from 496 per week in 2020/21 to 1,018 per week in 2023/24, with further increases forecast for 2024/25. Meanwhile, referrals to the Early Help rose to over 20,000 families receiving help in 2021/22.

In addition to these specific service level pressures, there was also a significant impact arising from general price inflation, with CPI peaking at 9.6% and RPI at 14.2% in October 2022. This affected buildings maintenance, transport costs and pay settlements with staff.

Meanwhile, the effects of previous cuts to services began to materialise, leading to higher costs. In addition to the £11m overspend in temporary accommodation, a report by the National Children's Bureau[20] showed that by 2020 Birmingham City Council faced 261 disability appeal tribunal cases per year, costing more than £10m since 2014 and rising to an estimated £1.6m per year by 2020. The costs to the Council of historic cuts to public health, advisory services, homelessness prevention, drug and alcohol prevention, domestic violence services, as well as lost income following cuts to arts and culture are difficult to measure, but likely created new demands elsewhere in the budget just as new claims arose due to the cost of living crisis[21].

---

[20] https://birmingham.cmis.uk.com/birmingham/Meetings/tabid/70/ctl/ViewMeetingPublic/mid/397/Meeting/13205/Committee/413/Default.aspx

[21] See Brackley et al. (2021) https://www.emerald.com/insight/content/doi/10.1108/AAAJ-11-2019-4278/full/html

Against this backdrop, the Birmingham City Council Financial Plan for 2022 showed that total external income was expected to rise just 0.8% in 2022/23 (to £2.98 billion) and 1.7% in 2023/24 (to 3.03 billion)[22]. Birmingham, like many other deprived authorities with greater levels of population-need, faced serious financial challenges in the 2022-24 period.

2022-24: the botched Oracle IT implementation

As Birmingham prepared for a renewed round of austerity, senior executives took the decision to 'go live' in April 2022 with a new Enterprise Resource Planning (ERP) IT system - 'Oracle Cloud Fusion' ('Oracle'). This IT system was a single platform, integrating finance, payroll, HR, procurement, supply chain management, and customer relationship management. Oracle replaced the previous SAP system, that had been in place since 1997. Importantly, the system would integrate the Council's accounting ledger with purchase and payment systems via a 'bank reconciliation system' (BRS). This was later to produce significant problems.

The system was expected to generate significant savings. It was initially budgeted at £19m in July 2019, with estimated savings of £26.9m identified. By final Cabinet approval in March 2021 this cost estimate had risen to £39m, with the savings estimate falling to £10.9m. The system was eventually launched a year later, on the 11th April 2022, with no dummy run or parallel testing, and, initially, without any of the associated audit trail functionality according to reports to the Audit Committee.

As has been documented by the external auditors[23], the hand-over between the old SAP system and Oracle was a disaster. The Oracle system began generating large numbers of transaction errors as tens of thousands of cash transactions could not be traced to the accounting system across council tax and business rates receivable, supplier payments, and schools budgets. According to the Auditor's post implementation review, this made it impossible to effectively monitor budgets or collect overdue debt throughout 2022/23 and into 2023/24. It also prevented the Council from producing their revenue outturn reports for both 2022/23 and 2023/24.

The auditors stated on 31st January 2024 that, "no budget monitoring reports have been provided to Directorates during 2022-23 or 2023-24" and on the 27th February 2024 the chief financial officer, referencing the External Auditors, stated that, "reliance could not be placed on the most basic of financial information from the system, with Directorates unable to receive monitoring reports which reflected the true in-year financial position". This not only prevented the Council from assessing their financial position reliably, but also exposed it to fraud risk because the new system had been set up without a

[22] Including grants, council tax, business rate retention, and ring fenced schools grants.
[23] Auditor report to the Audit Committee, 31st January 2024

segregation of duties and lacked necessary checks and balances when posting accounting entries.

This had a number of very serious consequences. It meant large numbers of temporary staff were needed to manually investigate and adjust the more than 70,000 transaction errors produced by Oracle. It also meant significant costs were incurred to pay for software specialists to perform temporary and long-term fixes to the system. By January 2024, the direct costs of implementation had risen from **£39m** to an estimated **£100m**, and by February the section 151 officer put the figure at **£131m**. In a cash-based accounting system, this fell directly on Council budgets.

On top of this, none of the anticipated direct savings were delivered, and, furthermore, due to the inability to monitor budgets, a significant amount of wider savings had to be written-off. In total, £69m of savings in 2023/24 were written-off, along with unspecified further savings in future years. Many of the internal processes and tacit knowledges that had previously been used to produce financial outputs broke down, providing no simple workarounds that would enable problems of this kind to be resolved.

Finally, the cash impact of these expenditures on Council budgets meant they had to increase short-term borrowing, which became significantly more expensive after the section 114 notice. The full extent of these problems are not yet known, but council tax and business rates receivables increased significantly through 2022/23 and 2023/24, to more than £263.4m by March 2023, after the removal of significant bad debt write-offs. Other costs, such as fines for late payment of suppliers, are unknown. The full direct and indirect costs of the failed Oracle implementation may run to hundreds of millions. In Figure 3, below, we summarise the Oracle related costs identified to date as they were presented to Cabinet on the 27th February 2024.

Figure 4: Direct and indirect costs of Oracle IT system charged to the General Fund

Original budget 2019	£19m	
Revised budget 2021	£39m	
Oracle costs incurred by Feb 2024	**£86m**	(direct)
Business rates bad debt deterioration 23/24	£12.5m	(indirect)
Council tax deficit 23/24	£4m	(indirect)
Savings write-offs 23/24	£69m	(indirect)
Total impact on the General Fund at Mar 2024	**£171.5m**	
Oracle budget to Apr 2026	**£45m**	(direct)
Total impact on the General Fund to April 2026	**£216.5m**	

Source: Cabinet papers: July 2019, March 2021, February 2024

Worryingly, from a transparency and accountability perspective, these problems were largely not disclosed to elected members and the wider public for more than a year, throughout 2022/23 and into 2023/24. Sections 4 and 5 below will explore how this shaped wider understandings of the Council's problems.

4. The section 114 notice: austerity, equal pay, and the Oracle IT disaster

On the 5th September 2023, the section 151 officer of Birmingham City Council issued the city's first ever section 114 notice[24]. As noted previously[25], this was issued on the basis of an unaudited and hence uncertain equal pay liability, which was put into the public domain – arguably prematurely - in the Summer of 2023. This had the effect of making the section 114 notice appear as an 'equal pay' problem rather than an 'Oracle and Covid plus austerity' problem, which significantly shifted the focus of public accountability. It also had a major impact on the capitalization direction the Council would receive, which recommended cuts and asset sales before the Council's audited financial position was known.

The section 114 notice issued in September identified the following factors as contributing to the financial crisis at the council[25]. No mention was made of the Oracle IT failure in the notice, instead placing the emphasis on the equal pay liability and on correspondence from the external auditors Grant Thornton:

a) *Correspondence from External Audit on 1st September 2023 that raised concerns around the provisions for Equal Pay being materially understated, which means the Council would have exhausted its General Fund balance on an accounting basis.*
b) *Further confirmation of the historic value of the potential Equal Pay liability impacting prior years, which is becoming more evident that it is unaffordable for the Council based on existing available reserves.*
c) *Correspondence from External Audit on 1st September 2023 also enquires around the likelihood of the Council being able to generate savings, additional revenue income, and/or capital receipts to mitigate the financial challenges.*
d) *A projected deficit of £87m for the 2023/24 financial year, for which the Council does not have sufficient reserves based on the Equal Pay liability above, which is forecast to grow in the 2024/25 financial year.*
e) *Concerns over the speed and effectiveness of the mitigations which have been put in place to address the in-year budget challenges, and the ability of the Council to address our financial position.*
f) *Extensive discussions with External Auditors, regulatory stakeholders, and leading Kings Counsel who have confirmed our assessment of our financial position.*

Source: https://www.birmingham.gov.uk/downloads/file/27684/section_114_notice

The s114 report noted that the £760m figure was, 'material enough to warrant disclosure' (p.4), despite it being unaudited. Media coverage from September put forward the view

[24] https://www.birmingham.gov.uk/downloads/file/27684/section_114_notice
[25] https://theconversation.com/how-birmingham-city-councils-equal-pay-bankruptcy-provided-cover-for-ongoing-oracle-it-disaster-224416

that the equal pay liability had 'effectively bankrupted' the Council[26] [27]. Neither the section 114 notice nor the media coverage from that time recognized that the equal pay liability had not been audited and that auditors had not received the model on which it was based. In the sections below, we briefly outline the accounting basis for the section 114 notice, then introduce what we know about the equal pay figure and Oracle IT failure. We then conclude on how the publication of the equal pay figure appears to have initiated a section 114 notice, but that its contribution to Birmingham's problems are contestable.

The 'section 114' notice and the cash basis of the revenue budget

Before exploring the issues cited in Birmingham's section 114 notice, we will briefly introduce the statutory basis for such a notice and, linked to this, an important principle of local authority accounting. As we will see in the remainder of this report, the judgments of the section 114 notice and the cash-based accounting underpinning the deficits in the revenue budget will play a significant part in the budget cuts that are imposed on the Council.

Starting with the statutory basis, a section 114 notice, under the Local Government Finance Act 1988, is issued when the 'section 151 officer' (usually the Director of Finance) of the Council judges that one of two financial tests cannot be met. These tests amount to: first, can the Council balance its revenue budget in year; and, second, does the Council have sufficient reserves in their General Fund to cover future costs[28]. Failure of either or both of these tests leads to a section 114 notice. Such a notice is widely referred to as being an 'effective bankruptcy'.

In the case of Birmingham City Council a s114(3) notice was issued on 5th September 2023. However, in practice such a notice bears little resemblance to a technical corporate bankruptcy – it does not, for example, arise due to any inability to pay creditors, nor does it provide the Council with any road map out of trouble, such as a debt consolidation or access to new long-term funding.

Once the notice is submitted, the Council is restricted such that they cannot approve any new non-statutory expenditure and must meet to formulate a plan to address the issues raised by the s151 officer. In any s114, the Council must continue to honour existing contracts and debt commitments as well as staff wages and salaries, which, together, amount to the vast majority of expenditure. Similarly, the Council must continue to provide the wide range of statutory services that they are also obliged by law to deliver. The section 114 itself therefore does relatively little to address the financial challenges of the Council in question, who must draw up plans to either balance the revenue budget or

[26] https://www.ft.com/content/4ed99112-02ab-4460-9397-dadf97fc6329
[27] https://www.bbc.co.uk/news/uk-england-birmingham-66756555
[28] For the full wording in statute, see: https://www.legislation.gov.uk/ukpga/1988/41/section/114

return the General Fund to a net positive position via capitalisation and asset sales (see section 6).

In terms of the accounting basis, this is a notoriously complex issue in local government accounting due to the conflict between what is referred to as the 'funding basis' and the IFRS based 'accounting basis'. In short, local authorities adopted full IFRS based accounting for the purposes of their annual accounts in 2010/11, while the revenue budget and the associated General Fund, which is the 'useable reserve' that finances the revenue budget, are accounted for under the Local Government Finance Acts (1988, 1992, 2003). These acts pre-date IFRS accounting and require that the Council balance their revenue budget on an annual basis under a largely cash-based system, that excludes accrual based accounting adjustments for depreciation, impairments, and fair value, among others. Meanwhile, a complex set of statutory adjustments dictate what accounting provisions and adjustments impact on the General Fund.

In the case of a Council in deficit, this has the effect of incentivising an increasingly short-term focus in their decision making, as it is only decisions with an immediate cash positive impact on the revenue budget that will balance the budget in the coming year. It also creates a situation in which short-term or temporary deficits, such as those that might arise from a failed IT system, can easily be treated as structural deficits requiring permanent reduction of service level provision. In a Council with strong reserves, these issues might, to some extent, be absorbed by the General Fund until the Council have recovered their position. However, in a Council in a negative General Fund position under statutory intervention, the pressure to balance the budget on a short-term basis can override longer term financial planning.

It is also important to consider the difference between the Oracle costs and the equal pay liability. In a cash-based system, Oracle costs are 'real' costs, with cash leaving the Council's bank accounts within year to pay for temporary staff and consultancy fees, whereas the equal pay liability is a speculative estimate of possible future claims. Oracle may also have affected cash income, because it caused chaos in budgetary monitoring system, impacting their ability to collect council tax debt, etc. In contrast, the equal pay liability had no immediate cash consequences because the Council had not at that point received any claims. In that sense, the Oracle costs were visible, but their cause was withheld from the democratic structures of the Council, whilst the equal pay liability claims were speculative and unaudited and thus, arguably, premature to advance as the basis for a section 114 notice.

In the case of asset sales and capitalisation directions (discussed in section 6.), the capitalisation direction is essentially statutory permission for the Council to temporarily borrow from their own capital budget to bring the General Fund back into the black. The asset sales then allow this cross subsidisation from the capital budget to be reversed out. Such asset sales can, however, lead to the loss of revenue generating assets (for example leased premises) which in turn creates further deficits in the revenue budget and requires further cuts to services.

Overview of the equal pay position

The equal pay claims relate to liabilities that may have accrued under the Equalities Act 2010 on two counts: (1) liabilities arising under 'task and finish', which arose between the ending of flexible Covid working arrangements in 2022 and the ending of 'task and finish' working practices in 2023/24, and (2) liabilities arising due to an unfair 'job evaluation' scheme up to April 2025 (when a new job evaluation scheme is set to be introduced).

The 'task and finish' liability relates to the practice in which predominantly male workers, who were allowed to work on a 'task and finish' basis under Covid regulations to minimise the risk of transmission, continued this practice after the Covid regulations ended in Spring 2022. This meant that some male workers were potentially paid more than some female workers because they were able to leave work early and still get paid for a full shift. It is thought that this practice ended between the Summer and Autumn of 2023. The job evaluation liability is more difficult to calculate because it relates to complex grading practices across the Council and the opportunity to progress within pay grades on a comparable basis within different parts of the work force.

We do not have the information to assess the merits of these claims, but it does appear that 'task and finish' was limited to groups of predominantly male workers. We note that there is no direct precedent in case law for the 'task and finish' element of the liability, and no direct comparator or precedent in law for the job evaluation liability, where practices have changed considerably since the 2012 Supreme Court judgment. We would also note that a percentage of the workforce have already settled equal pay entitlement up to 2022, under the 'Memorandum of Understanding' [29].

As noted in the introduction, the full model on which the Council's initial £760m liability figure was based has not been disclosed. In particular, we do not know the breakdown of how much relates to task and finish and how much to job evaluation, the number of workers affected, and their current grading. We do, however, get some breakdown in the February analysis of the capitalisation direction (see Table 1 below). Dated 27th February 2024, this analysis estimates that the equal pay liability will rise to £867m by April 2025, of which £815m is capitalised under the capitalisation direction:

[29] https://birminghamunison.co.uk/2022/01/20/third-generation-parity-payment/

Figure 5: Summary of the equal pay position under the February 2024 capitalisation direction

Provision by fund and Balance sheet date (showing amounts per annum)	**31 March 2021 (£m)**	**31 March 2022 (£m)**	**31 March 2023 (£m)**	**31 March 2025 (£m)**	**Total (£m)**
General Fund	158.3	91.4	121.1	164.0	534.8
Housing Revenue Account	18.1	9.2	8.7	15.8	51.8
DSG & Schools	130.1	18.1	51.1	81.2	280.5
TOTAL	**306.5**	**118.7**	**180.9**	**261.0**	**867.1**
Of which:					
Total General Fund, DSG & Schools (annual EFS request each year)	***288.4***	***109.5***	***172.2***	***109.5***	***815.3***
Total General Fund, DSG & Schools (cumulative)	*288.4*	*397.9*	*570.1*	*815.3*	

Source: 27th February 2024 Cabinet papers

The February 2024 analysis suggests that the provisions recognised up to 31st March 2022 were revised up to an estimated **£425.4m** (£306.5m + £118.7m), from the previous figure of **£121m**. It also shows that a significant proportion of the provision related to the accrual of future liabilities (£261m) after the 31st March 2023. In this sense, not all of the liability amounted to a 'present obligation arising from a past event' on an accounting basis. It also suggests that the methodology used, due to the dates quoted above, skews the liability heavily towards 'job evaluation' rather than 'task and finish', noting the limited overlap in the accrual of the above liability with the period in which task and finish working practices were taking place.

These figures then form a substantial part of the overall £1.255 billion capitalisation direction, as follows:

Figure 6: Summary of the February 2024 capitalisation direction

EFS Request	2020/21 (£m)	2021/22 (£m)	2022/23 (£m)	2023/24 (£m)	2024/25 (£m)	2025/26 (£m)	Total (£m)
Budget Gap	0.0	0.0	0.0	0.0	239.8	0.0	239.8
Redundancy Costs	0.0	0.0	0.0	0.0	50.0	50.0	100.0
Potential Equal Pay Liability (taken from Table 1)	288.4	109.5	172.2	0.0	245.2	-	815.3
EFS Contingency	0.0	0.0	0.0	0.0	100.0	0.0	100.0
TOTAL	**288.4**	**109.5**	**172.2**	**0.0**	**635.0**	**50.0**	**1,255.1**

Source: 27th February 2024 Cabinet papers

Importantly, the above capitalisation direction included no capitalisation against the ongoing overspend on the Oracle IT system, with these costs entirely absorbed by the £149m cuts to the 2024/25 budget and the outstanding £239.8m budget gap going into 2025/26.

Sources within the Council, which were recently quoted in the Financial Times[30] and include the lead Commissioner Max Caller and several of the city's trade unions, now put the best estimate of the equal pay liability closer to £250m, with Caller describing the figures quoted in the section 114 notice as a 'worst-case' scenario due to there being no agreed job evaluation in place at that time. This revelation, in itself, raises issues because section 8 of the CIPFA code and the relevant sections of IAS 37, state that any provision for equal pay settlements should be accounted for on a 'best estimate' *not* 'worst case' basis. Any future inquiry should investigate whether Birmingham City Council have accounted for their equal pay liability on a different basis to every other authority in England, putting a figure into the public domain when there was no clear regulatory justification for doing so.

Did equal pay claims drive the Council's financial difficulties in 2022-24?

On review of the relevant Cabinet documents and the 2024/25 budget, none of the £300m in-year deficit relate to the settlement of new equal pay claims, and none of the £149 million of cuts to services relate to any deficit created by equal pay. Instead, the Council's spiralling deficit, estimated at £300 million across 2024/25 and 2025/26, appears to be

[30] https://www.ft.com/content/753309fd-518b-481b-a542-0f164de1f659

related to the launch of the Oracle IT system, together with the spike in demand documented in section 3. of this report.

The costs of the Oracle implementation had risen to £131m by February 2024, which compounded problems driven by the spike in demand and other cost pressures. Moreover, the tens of thousands of transaction errors produced by the Oracle system led to increased bad debt on both council tax and business rates, penalties incurred due to late payments to suppliers, an inability to monitor budgets leading to a £69m savings write-off in 2023/24, and increased borrowing costs. The full costs of the Oracle disaster may become more apparent with the publication of the Council's 2022/23 draft accounts. However, with these accounts likely to receive a disclaimer audit opinion it may take several years and an independent inquiry for the costs to be fully known.

Based on this analysis, it is therefore likely that the financial difficulties in 2023 were due to demand and price led pressures, the failed implementation of Oracle, or other explanations not currently in the public domain. This is because, in a cash based accounting system, the new equal pay claims do not appear because they relate to potential *future* claims rather than in-year claims. Furthermore, the associated equal pay analysis showed that a large part of the liability had not yet accrued at the date of the section 114 notice (with the liability continuing to accrue up to April 2025), where the value of the equal pay liability remains moot.

There is therefore no evidence that the financial difficulties of the Council were driven by new equal pay claims, and very considerable evidence that they were driven by the Oracle failure, demand pressures, and price inflation.

Who knew what and when: did equal pay concerns displace the ongoing Oracle IT disaster?

As documented above, the spiralling budget deficits cited in the section 114 notice cannot be wholly explained by the equal pay issue. A more significant contributory factor was the costs of the new Oracle IT system and the legacy of a decade of austerity cuts during a cost of living crisis.

Based on our review of reserves and the budgetary monitoring updates, the Council had reached a point by July 2023 at which the prospect of issuing a section 114 notice had become highly likely, if not inevitable, irrespective of the equal pay liability. The overspend on Oracle had become impossible to ignore. As had major write-offs of planned savings, due in large part to an inability to monitor budgets following the failed Oracle implementation. Similarly, major collection fund deficits and write-offs of council tax and business rate income were charged to the General Fund, again potentially due to an inability to effectively monitor or collect debt between April 2022 and January 2023. In December 2023, the section 151 officer gave the following update on reserves:

Figure 7: Summary of useable reserves 31st March 2022 to 31st march 2024

Useable Reserves	Value (£m)
Balance at 31st March 2022	**£596.8m**
Reserves used in 2022/23	(£336.2m)
Latest forecast 31st March 2023	**£260.6m**
Estimated reserves usage in 2023/24	(£25.6m)
Latest forecast 31st March 2024	**£235.0m**

Of the £235.02m, £172.2m is available for use.

*There are **additional draw-downs** which need to be addressed.*

Reserves available for Overspend and Other Items	£172.2m
Overspend for 2023/24	(£87.4m)
Oracle Costs (multi-year)	(£46.5m)
Extra Pay Award Costs 23/24 (assuming 6.5%)	(£11.2m)
Equal Pay Liability, midpoint £650m-£760m future yr	(£705.0m)
Negative Reserves	**(£677.9m)**

Source: 12th December 2023 Cabinet papers

As can be seen from the above, the Council were close to exhausting useable reserves by March 2024, even without accounting for the equal pay liability (with just £705m – £677.9m = **£27.1m** remaining). Add to this the inability to set a balanced budget in 2024/25 and the need to further draw down on reserves in that year, and it was clear that the Council would need to either seek capitalisation support or issue a section 114 notice regardless of the equal pay position. In relation to the table above, we would draw attention, in particular, to the use of reserves used in 2022/23, reported as £336.2m, and contrast that with the deficit reported the year before, in 2021/22, of just £3.1m. This shift in the in-year deficit position is too extreme to be the result of cost pressures alone, and suggests that very significant Oracle costs were hitting the general fund throughout 2022/23. This is consistent with the analysis provided in January 2024 by the external auditor, in which the extent of the Oracle failure became apparent, with major staff costs, procurement costs, and indirect costs relating to debt collection and budget monitoring. Indeed, the extent of the draw down on reserves in 2022/23 suggests that the Oracle cost figures we identify in section 3 of this report may underestimate problems.

Given the extent of these costs and the details of external auditor's post implementation review, it is remarkable to review the minimal disclosure of the Oracle failure via the Council's democratic structures during this time. Questions were asked of senior officers by Labour, Conservative and Liberal Democrat Councillors at Audit Committee, Cabinet, and full Council. We provide an overview of the responses they received below, in which issues with the Oracle implementation appear to have been played down by the executive through 2022/23.

Audit Committee, 18th October 2022

In response to questions raised by members of the committee: *"The [Oracle] system was live and there was a plan to address areas that had not been tackled. It was envisaged this would be addressed over the next few months. Oracle was at the post-implementation period and officers were working through issues. The Committee requested for details on the final expenditure for Oracle Implementation to be provided and to include any additional expenditure; ongoing expenditure; start of project figures; what actual spend was; how late was the delivery and the learnings from the process."*

Audit Committee, 28th March 2023:

In the External Auditor's update to the committee: *"The External Auditors felt the Oracle Implementation and audit around this was not where it needed to be, and constructive engagement was required in the future. The External Auditors requested for details of who was best to engage with from the Council for IT matters."*

"The Chair recognised there were difficulties with engagement between BCC IT department and the External Auditors"

It would not be until May 2023 that any substantive detail on the Oracle implementation was finally provided to the Audit Committee. In the following meeting, in June 2023, the Audit Committee asked that a post-implementation review be commissioned, which would be delivered in January 2024. Too late for the Audit Committee to intervene.

Following this line of questioning at the Audit Committee, questions were asked at full Council on the 18th April 2023. These covered Oracle errors in the monitoring of schools budgets, failures of controls in the Oracle system, non-delivery of savings, and disclosure of Oracle related costs. These were answered as follows:

Full Council, 18th April 2023:

On control failures: *"Officers have provided information to the external auditors on how Oracle handles this specific security issue. They have provided assurance that those specific practices from SAP are not being repeated in the new system".*

On savings: *"Officers have advised that Oracle will begin to deliver savings in this financial year 2023/24".*

On disclosure of Oracle costs: *"The increased funding in the Council's 2023/24 budget has been agreed to support improved Oracle implementation across a range of functions including finance, procurement and people services. In any large and complex organisation there will be uncertainty around the costs of this kind of programme. We have taken appropriate steps to fund these pressures".*

On the failure of functionality: *"Oracle is already delivering a wide range of important functionality including payroll, supplier payments, and accounts payable. We expect the* *system's functionality to continue increasing over the course of 2023/24 and beyond, as we maximise its capability and benefits"*.

On value for money: *"Financial decisions will continue to be made about Oracle on the basis of what is good value for the city as a whole. Any decisions will be made in line with the Council's constitution and financial regulations"*.

In sum, it appears that the widespread failure of the Oracle IT system, and the associated costs running into hundreds of millions of pounds, were not adequately disclosed to the cross-party democratic structures of the Council for around thirteen months, between April 2022 and May 2023. Why Oracle's contribution to the Council's financial distress was all but omitted in the September 2023 section 114 notice is something of a mystery. Any subsequent inquiry should ask serious questions about why the failure of Oracle was downplayed by senior management at that time; and whether this was the result of intransigence and mismanagement, or was part of a deliberate strategy to deflect blame, or some other reason.

5. Questions about the role of the external auditor in the Birmingham case

A lack of transparency and public accountability are key features of the Birmingham case, both in relation to the Oracle disaster through 2022/23 and then in relation to the basis of the equal pay calculation in 2023. External auditors are notionally the key actors to encourage disclosure and transparency in the public interest[31]. However, the external audit function in local government is in a serious state of crisis. A sector wide collapse in the external audit market has seen the proportion of local authorities receiving their audits on time drop from 12% in 2021/22 to just 1% in 2022/23[32]. As covered comprehensively by Research for Action in their recent report[33], since the abolition of the Audit Commission in 2015 and the privatisation of the external audit function, the market for external audit as a timely assurance statement on the accounts has effectively ceased to function at local authority level.

There are questions about the capability of private sector auditors, not specialised in local authority auditing, to conduct effective audits. In their 2023 report[29], Research for Action highlight the relevant sections of the Redmond Review (2020) that report 'significant concerns' among many local authorities 'about the knowledge and expertise of staff working on their audit' such that '83% felt the private firms did not have enough understanding of the local authority regulatory framework'. They also draw attention to recent LGA findings that the audit market is undermined by having 'too few suitably qualified auditors employed by firms'.

In the Birmingham case, the Council are audited by Grant Thornton. Grant Thornton, like many audit firms, have been fined and reprimanded by regulators on several occasions in recent years. The firm was fined by the FRC in 2024 for significant departure from the standards expected in the audit of an unnamed local authority pensions audit, with a finding that material errors existed in the account and that insufficient audit work had been carried out[34]. In 2020 the FRC fined Grant Thornton £3m for firm wide failures in audit ethics in relation to the audit of Conviviality Retail Plc[35] and in 2021 issued a £4m fine in relation to serious breaches in the audit of Patisserie Valerie that included "a pattern of serious lapses in professional judgement, failures to exercise professional scepticism, failures to obtain sufficient and appropriate audit evidence"[36].

---

[31] https://www.nao.org.uk/wp-content/uploads/sites/29/2020/01/Code_of_audit_practice_2020.pdf
[32] https://auditreformlab.group.shef.ac.uk/downloads/financial_crisis_of_bcc_part_1.pdf
[33] https://researchforaction.uk/report-local-audit-why-public-interest-needs-to-count
[34] https://www.frc.org.uk/news-and-events/news/2024/04/sanctions-against-grant-thornton-uk-llp/
[35] https://www.frc.org.uk/news-and-events/news/2020/07/frc-announces-sanctions-against-grant-thornton-uk-llp/
[36] https://www.frc.org.uk/news-and-events/news/2021/09/sanctions-against-grant-thornton-uk-llp-and-david-newstead/

At the time of writing this report, Grant Thornton have still not signed off their audits of Birmingham's 2020/21 or 2021/22 accounts, and it now seems likely that no substantive audit work will be conducted on the crucial 2022/23 accounts prior to the September 2024 backstop date[37]. Their work on the equal pay liability has also been severely delayed, with that work commencing in November 2023 but still outstanding as at June 2024. For context, a similarly sized FTSE listed company would be expected to file a full audited set of accounts within four months of their year-end.

This is not unusual in the sector, however, in respect of the work performed there are further questions in relation to professional scepticism and compliance with ethical standards that need answers.

Before posing these questions, we want to emphasise that our findings in this section of the report are based solely on publicly available information and are framed as 'questions' that require further investigation. We do not draw any firm conclusions. We also want to emphasise that we do not have access to audit working papers or minutes of meetings not taken in public session. In seeking comment from Grant Thornton on these matters, they have asked us to clarify that they had not signed off the accounts for 2020/21 or 2021/22 or given any assurance over the equal pay figures, either in relation to their reports to the audit committee in March 2023 in relation to the £121m liability, or in their statutory recommendations in relation to the £760m liability.

Questions over the audit of equal pay

Auditors: 'No adjustments' to the £121m equal pay liability on the 28th March 2023

There appears to be some ambiguity about the status of the £121m equal pay liability and the extent to which it had been confirmed by the external auditors; and indeed what "confirmed" means in this context. The Audit Findings Report 31st March 2021 raised a series of questions about the valuation and completeness of the equal pay provision, identifying it as a risk requiring special audit consideration, and a key audit matter. A series of events, possibly including the decision by the GMB trade union to advise its members against signing further settlements in 2021, raised, "uncertainties... within the contingent liabilities note in relation to the volume and timing of any future equal pay claims and the determination of any settlements". As a consequence, Grant Thornton requested that management "documents its consideration of whether there is now new information in relation to the position at 31 March 2021 that means an adjustment is required in the provision made in the financial statements". Grant Thornton were explicit that this meant the signing-off of the equal pay liability was incomplete – that they were "in the process of considering and challenging" managements' response to their request.

---

[37] https://www.gov.uk/government/consultations/addressing-the-local-audit-backlog-in-england-consultation/local-audit-delays-joint-statement-on-update-to-proposals-to-clear-the-backlog-and-embed-timely-audit

However, the Audit Findings Report of 31st March 2022 followed up on 2021's figure, noting that they had "gained *sufficient assurance* that these errors did not lead to a material misstatement of the estimate". They went on to note in their "significant risks" section that they had assessed the accuracy and completeness of the information used as the basis of estimating the 2022 liability, reperformed the calculation of the estimate, *confirmed* that the estimate had been determined and recognised in accordance with accounting standards and determined how management had assessed the estimation uncertainty. They concluded that whilst they had identified errors in management's calculations, they considered them, "trivial both individually and in aggregate" and therefore recommended "no adjustments" to the equal pay liability figure (p.15). In this sense, they had "substantively audited" – as defined under ISA500 - the £121m equal pay provision in the accounts as part of the gather evidence phase of the audit[38]. Finally, they noted the need to consider events or conditions that could change the basis of this estimation up to the date of signing of the accounts. However, we would note that this is a standard consideration on any audit through to the sign-off date and does not contradict the fact that the substantive audit work on the £121m liability had been completed.

Figure 8: Findings from the audit of equal pay reported to the 28 March 2023 Audit Committee

2. Financial Statements - Significant risks

Risks identified in our Audit Plan	Commentary
Valuation and completeness of the equal pay liability Under ISA (UK) 540 (Auditing Accounting Estimates, including Fair Value Accounting estimates and Related Disclosures) the auditor is required to make a judgement as to whether any accounting estimate with a high degree of estimation uncertainty gives rise to a significant risk. We identified the valuation and completeness of the equal pay provision as a risk requiring special audit consideration, and a key audit matter.	We have: • updated our understanding of the processes and controls put in place by management to estimate the equal pay provision • reviewed the assumptions on which the estimate is based • assessed the accuracy and completeness of the information used as the bass of estimating the liability, and reperform the calculation of the estimate, on a sample basis where appropriate • confirmed that the estimate has been determined and recognised in accordance with accounting standards • determined how management have assessed the estimation uncertainty Findings Our testing of individual calculations identified a number of errors resulting from manual inputs into the calculations, including: • the use of an estimated interest rate when an actual rate was available • use of an average differential • limitations in the data to determine grade changes in year • formulae error within the calculation working papers • application of a flat 24% tax rate to claims despite HMRC evidence stating that Lunchtime Supervisor roles should have 10%. These issues have been evaluated and are considered to be trivial both individually and in aggregate and therefore no adjustments are proposed. However, we consider that improvements can be made to the preparation of the calculation and have made a recommendation on that basis. Before concluding in respect of this risk we will need to consider events or conditions that could have changed the basis of estimation and the potential impact of any transactions or events after the balance sheet date up to the date of signing of the financial statements.

Both the 2021 and 2022 report were presented to the 28th March 2023 audit committee. Grant Thornton reported that their work on the 31st March 2022 accounts had been largely

[38] By "substantively audited" we mean that the tests auditors use to gather evidence about whether a company's financial statements are free of material misstatements had been competed (see ISA500).

completed, with only minor elements outstanding in relation to property valuations that would not affect the audit opinion. They also confirmed to the Audit Committee that the arrangements in place for calculating the equal pay liability were adequate. That meeting received a management representation letter confirming that the auditors had been provided with all relevant information in relation to the equal pay figure and it was noted in the minutes that the auditors were "very close to issuing opinions [on the 2020/21 and 2021/22 accounts] with items remaining that should not affect the opinion". The Committee was assured that "both audits will be signed off in the near future". No issues were noted in relation to Going Concern.

The £760m liability is 'confirmed' in September 2023, but by who?

Things changed dramatically when in May 2023 Grant Thornton noted that officers sent them a revised figure for the equal pay liability of £760m (Statutory Recommendations, p.1). That figure was to play a huge role in the triggering of the s114 and as justification for bringing in the Commissioners. But to this date that £760m figure remains unaudited and so became, in the public realm at least, something of a Schrödinger's cat – both unaudited and unequivocal, both uncertain and unquestioned.

Much of this ambiguity relates to the status of that figure as being "confirmed". The auditor states that "once the level of the equal pay liability was confirmed we liaised closely with the Council to ensure that it put in place an appropriate job evaluation process" (Statutory recommendations, p1). This could imply that confirmation was *reached with* the officers (an active process which involved some assessment of the accuracy of the figure) or *given by* the officers (a passive process which involved simply noting the figure provided by officers). The view of the auditor, and evident in the context of the statutory recommendations, is that the act of confirmation was given by the officers under this latter meaning. However, this view does not clearly flow from the comments of outsiders.

The s151 officer claimed that "extensive discussions with External Auditors, regulatory stakeholders, and leading Kings Counsel… have confirmed our assessment of our financial position"; whilst even the Secretary of State claimed on the 19th September: "The independent auditor's assessment was that the revised estimated equal pay liability is likely to be more than £760 million and there is a risk it could be much higher". These quotes suggest third parties believed that Grant Thornton played a role that went beyond simply 'passing on' the figure, but rather helped those actors understand – and accept the legitimacy of - the equal pay liability figure of £760m (or more).

There therefore appears to be an element of circularity in the confirmation process: Grant Thornton claims, on the one hand, that it was management who confirmed the existence of the new £760m liability, and that they did not confirm this figure; while the s151 officer – a council official - appears to claim that discussions with External Auditors, amongst others, confirmed her assessment of the council's financial position and the need for an s114. Similarly, the secretary of state's claim that the auditor 'assessed' that the liability was 'likely to be more than £760m' does not appear to support the auditor's claim that they provided no confirmation of that figure. These are self-evident ambiguities and also, therefore, important public interest questions given the significance of that figure and those actors in triggering the s114 and the imposition of commissioners.

Grant Thornton have subsequently stated to both the Council's Audit Committee and to us in their response to this report that no assurance was given over either the £121m figure in March 2023 or the £760m figure in September 2023.

Overstatement or Understatement?

The ambiguity over how the £760m was 'confirmed' aside, Grant Thornton's report to the Audit Committee on 15th September 2023 did not appear to address the possible managerial incentives for *overstating* the £760m figure, to trigger the section 114 notice which distracted from the costly implementation of the Oracle IT system, or indeed other failings[39]. They instead identify the more significant risk as being primarily one of *understatement*. This despite explaining to the committee that they had not obtained the equal pay models and had not yet begun their substantive audit work. This was still the situation at the Audit Committee the following month, in October.

Questions over compliance with ethical standards

The above role and performance of the auditor, Grant Thornton, raises important concerns. First, whether there was, as a result of the above third party perceptions, a potential self-review threat to their independence. Second, a more general question about whether situations like this also pose a management threat to independence. Any future inquiry would have to assess whether Grant Thornton might reasonably be perceived to be acting independently or not in the eyes of stakeholders and the wider public, in a context where compliance with Ethical Standards, particularly in relation to audit independence, is a matter of reasonable perception not of fact[40].

Taking the two issues in order, Grant Thornton did, as we note above, insist at the 24th April 2024 Audit Committee meeting that they had not given any opinion on the higher equal pay estimates in either their advice on the section 114 notice or their statutory recommendations. However, this is not necessarily sufficient to avoid a self-review threat, which is defined by the FRC and the ICAEW as follows:

"The apparent difficulty of maintaining objectivity and conducting what is effectively a self-review, if any product or judgement of a previous audit assignment or a non-audit

[39] This is a statement on audit risk in relation to identification of the audit assertions in the significant risk assessment. It is not an assessment of what took place.

[40] https://media.frc.org.uk/documents/Revised_Ethical_Standard_2024.pdf

assignment needs to be challenged or re-evaluated in reaching audit conclusions" (ICAEW)[41].

"The firm or covered person may be, or may be perceived to be, unable to take an impartial view of relevant aspects of those financial statements or other subject matter information" (FRC)[42].

As noted, the statement in the section 114 notice, dated 5th September 2023, implies independent third parties believed Grant Thornton had some role in helping them confirm the £760m amount: "correspondence from External Audit on 1st September 2023 raised concerns around the provisions for Equal Pay [...] being materially understated" and that there had been "extensive discussions with External Auditors, regulatory stakeholders, and leading Kings Counsel who have confirmed our assessment of our financial position". This perception was also echoed by the secretary of state on the 19th September 2023, that "*the independent auditor's assessment was that the revised estimated equal pay liability is likely to be more than £760 million, and there is a risk it could be much higher*[43]*.*"

Also as noted, at no point in their lengthy statutory recommendations[44] do Grant Thornton make it clear that they had not substantively audited these new equal pay figures, nor obtained the model upon which these figures were based. Grant Thornton, perhaps following Michael Gove's comments above, were widely cited in the media as having confirmed the amount. If that was not the case, it is unclear why they did not set the record straight in their statutory recommendations. Given this, the risk now is that any subsequent opinion on equal pay by Grant Thornton that contradicts the statements in their statutory recommendations, or contradicts the impression those statements may have given (particularly given the Secretary of State's comments in parliament and associated media coverage), could be potentially damaging to the reputation of Grant Thornton. If so, then this could amount to a potential conflict of interests and a "self-review threat" to their independence and objectivity[45].

The revised Ethical standards[46] suggest that this risk arises in any situation where the firm is "or may be perceived to be" unable to take an impartial view. The Audit Committee has already raised questions about whether Grant Thornton are able to provide an

---

[41] https://www.icaew.com/-/media/corporate/files/technical/ethics/professional_ethics/1-201-integrity-objectivity-and-independence.ashx
[42] https://media.frc.org.uk/documents/Revised_Ethical_Standard_2024.pdf
[43] https://www.gov.uk/government/news/government-intention-to-intervene-at-birmingham-city-council
[44] https://www.birmingham.gov.uk/downloads/download/6414/external_audit_2020-21_to_2023-24
[45] The earliest occasion we identified were Grant Thorton clarify that they had not obtained the equal pay models was in the papers presented to the 15th September 2023 Audit Committee. Regulators and stakeholders should consider whether this provides sufficient cover to avoid a self-review threat, in the context of the comments of the secretary of state and the auditor's statutory recommendations.
[46] https://www.frc.org.uk/library/standards-codes-policy/audit-assurance-and-ethics/ethical-standard-for-auditors/

independent opinion in relation to equal pay[47]. The considerable amount of time the equal pay liability audit work is taking, which commenced in November 2023 and remains outstanding as at June 2024, only adds further questions about the audit of equal pay figure.

The guidance on the 'management threat' to independence, is defined as follows:

"A threat to integrity, objectivity and independence also arises where the firm provides non-audit / additional services and, based on that work, management are required to make judgments and take decisions. The persons conducting the service may become closely aligned with the views and interests of management and this may erode the distinction between the entity and the firm, in turn, impairing or calling into question the ability of the persons conducting an engagement to apply a proper degree of professional scepticism." (FRC)[48].

In a context where any audit firm has a relatively long association with a Council and where there is a high turnover of senior staff in that Council, there is always a risk that the firm gets drawn into the wider operations of the Council because of the significant statutory powers an external auditor holds in the local government sector. Particular care should therefore be taken by the audit firm in such a situation to emphasise that they are not interfering with the operations of the Council and are seen to be clearly holding the senior executive to account. By highlighting this risk, we are not implying that it applies to Grant Thornton in this case – but that any future inquiry should consider this general risk, given that statutory powers were exercised in this case, if only just to discount it as a factor in the ensuing events.

[47] https://birmingham.public-i.tv/core/portal/webcast_interactive/872370

[48] https://media.frc.org.uk/documents/Revised_Ethical_Standard_2024.pdf

6. Redrawing the ‘Exceptional Financial Support’ package

If the equal pay liability is found to be lower than the £760m estimate as most now suggest, then the spotlight should return to the problems around Oracle and ‘austerity + increased service demands’. It is feasible, therefore, that the current capitalisation direction and wider support package as agreed in February 2024 are solving the wrong problem. The asset sales, linked to a likely overstated and unaudited equal pay liability, risk delivering poor value for money and may create unnecessary deficits in future revenue budgets. The £300m of budget cuts are also being implemented in a way that don’t engage sufficiently with assessments of future outcomes and longer term financial sustainability.

We therefore recommend a restructure of the capitalisation direction, *capitalising primarily against the cost of the Oracle IT implementation rather than Equal Pay*. Any remaining equal pay provision, calculated on a “best estimate” rather than “worst case” as per section 8 of the CIPFA code, should then only impact upon the General Fund when actual settlement payments are made for the period of the direction[49]. This approach better reflects the issues faced by Birmingham and provides for better outcomes for the city. In particular:

(1) Extending the capitalisation period provides for a more realistic timeline to fully implement Oracle and underwrites the process until the financial position of the Council is properly established. Only then is the city Council in a position to properly assess savings and fulfil its best value duty.
(2) It means that the temporary costs of the Oracle IT failure are not being permanently absorbed in cuts to vital statutory services.
(3) Treating equal pay on a “best estimate” basis allows for the overall capitalisation direction to be reduced. It also complies with the CIPFA code, so that the city is estimating the liability on the same basis as other authorities.
(4) It gives time for the Council to assess their medium-term financial position following any future comprehensive spending review and/or fair funding review.

Below, **Figure 8**, is the current capitalisation direction as approved by the DLUHC. This is based on an unaudited and likely overstated total equal pay liability and ends in April 2026. By February 2024, the equal pay capitalised under the direction had grown to £815m. The overspend on Oracle is entirely absorbed by the General Fund. A significant £100m redundancy cost is included, due to the front-loaded nature of the cuts. The direction also leaves the Council with an estimated £67m deficit at April 2026, which we

[49] As per section 4 the accounting treatment of the capitalisation effectively protects the General Fund from these capitalised costs for equal pay. Due to the cash basis of accounting in the revenue budget, the capitalisation is reversed either as cash settlements are made or via an alternative mechanism such as asset sales.

think is likely to grow due to unaccounted for knock on costs and non-delivery of savings. Overall, the current direction risks delivering the worst of all worlds – doing significant damage to outcomes while at the same time failing to balance the city's budget in the period of the direction.

Figure 8. Current £1.255 bn capitalisation direction, running to April 2026

EFS Request	2020/21 (£m)	2021/22 (£m)	2022/23 (£m)	2023/24 (£m)	2024/25 (£m)	2025/26 (£m)	Total (£m)
Budget Gap	0.0	0.0	0.0	0.0	239.8	0.0	239.8
Redundancy Costs	0.0	0.0	0.0	0.0	50.0	50.0	100.0
Potential Equal Pay Liability (taken from Table 1)	288.4	109.5	172.2	0.0	245.2	-	815.3
EFS Contingency	0.0	0.0	0.0	0.0	100.0	0.0	100.0
TOTAL	**288.4**	**109.5**	**172.2**	**0.0**	**635.0**	**50.0**	**1,255.1**

We therefore propose the alternative capitalisation direction, **Figure 2. (overleaf)**, on the basis of the principles outlined above. Our proposal means capitalising less, both in 2024/25 and overall, while also giving a more realistic roadmap towards a balanced budget in 2027/28. We note this proposal is only a suggested guideline, and that more work needs to be done to assess the direct and indirect costs of the failed Oracle implementation.

Figure 9. the ARL's proposed £1.1bn capitalisation direction

EFS request	20/21 (£m)	21/22 (£m)	22/23 (£m)	23/24 (£m)	24/25 (£m)	25/26 (£m)	26/27 (£m)	27/28 (£m)	Total (£m)
Budget gap	0.0	0.0	0.0	0.0	239.8	75	50	0.0	364.8
Redundancy cost	0.0	0.0	0.0	0.0	50	20	10	0.0	80
Equal pay liability	150	(29)	125	125	0.0	(15)	(15)	(15)	326
EFS contingency	0.0	0.0	0.0	0.0	100	0.0	0.0	0.0	100

Recovery of Oracle	0.0	0.0	0.0	0.0	200	50	(10)	(10)	230
Total	**150**	**(29)**	**125**	**125**	**589.8**	**130**	**35**	**(25)**	**1,100.8**

Proposed revenue budget overspend in 2025/26 and 2026/27

Revised assumptions in relation to equal pay, redundancies, and cost of Oracle

Following the above, we propose an alternative capitalisation direction (above) that capitalises against the direct overspend on the Oracle programme (£131m) and indirect Oracle related savings write-offs (£69m in 2023/24 and £50m in 2024/25). We maintain a more modest equal pay provision, in line with estimates provided by the trade unions, and suggest that these be accounted for on the pre-April 2020 basis, such that only settlements of actual equal pay claims be charged against the General Fund.

*Budget gap: £239.8m figure in the current direction reconciles to the £193.4m in the revised direction as follows:

EFS request	**24/25 (£m)**	**25/26 (£m)**	**26/27 (£m)**	**27/28 (£m)**	**Total (£m)**
Budget gap per original EFP plus overspend in 25/26 and 26/27	239.8	75	50	-	364.8
Non-delivery of savings (24/25)	50	-	-	-	50
Anticipated savings linked to full Oracle implementation	(10.9)	-	-	-	(10.9)
Council tax & business rate write-offs due to Oracle rolled into 24/25	(16.5)	-	-	-	(16.5)
Savings write-offs from 23/24 rolled into 24/25	(69)	-	-	-	(69)
Revised budget gap*	**193.4**	**75**	**50**	**-**	**318.4**

**Recovery of Oracle

	(£m)	

Oracle costs incurred by Feb 2024	86	Direct
Business rates bad debt deterioration 23/24	12.5	Indirect
Council tax deficit 23/24	4	Indirect
Savings write-offs 23/24	69	Direct & Indirect
Total impact on the General Fund by March 2024	**171.5**	Direct & Indirect
Additional Oracle budget to April 2026	45	Direct
Total impact on the General Fund to April 2026	**216.5**	Direct & Indirect

7. Failures in the 2024/25 budgetary consultation

Following the section 114 notice in September 2023, and communication via Council committees of the extent of the Oracle disaster in the Autumn of 2023, the Council entered into a full budgetary 're-basing exercise' in October and November to re-assess their 2024/25 budgetary position. This effectively redrew the budgetary forecasts in the 2023-2027 financial plan, with revised assumptions for savings delivery, service level cost pressures, and inflation. The result of this exercise was disclosed in the 12th December Cabinet papers, which concluded that the Council's deficits were set to rise to £300m by 2025/26. As covered in previous sections of this report, this figure was driven by a combination of direct and indirect Oracle costs together with a steep rise in cost pressures during the difficult austerity funding environment. In the Commissioner's comments on the December Cabinet report, they accepted that the Council would not be able to balance their revenue budget in 2024/25 and set the Council the target of setting a balanced budget in 2025/26. Thus the £300m two-year savings target by 2025/26 was set, with approximately £150m to be found in each year.

For 2024/25, the Council therefore had to deliver the biggest ever single year cuts of any local authority on an accelerated timescale. Not only was the depth of these cuts unprecedented, but the rebasing exercise meant that the normal period of consultation and due diligence was severely curtailed, with cuts that would normally have been identified over the Summer or, at the latest, by September-October were not identified until November-December (with £106m identified by the 24th November and the remaining £43m identified by 12th December 2023). The due diligence and consultation was then condensed into a four-week period from the 12th December to the 10th January. The only public element of this consultation was a survey posted to the Council's website in December asking residents to rank by order of priority various areas of service delivery. No detail of the planned cuts was included in this survey.

Possible breaches of law in relation to public consultations and statutory duties

According to Wyard et al. (2023)[50], there is both a general common law duty of fairness in the local government consultation process and express duties to consult in relation to major best value decisions. There is also a duty to consult where a legitimate expectation has been established by prior custom and practice, and, in the case of Birmingham, where they have themselves committed to consultation. In such cases the consultation should be fair and meaningful and, as a general rule, "the more serious the

[50] https://localgovernmentlawyer.co.uk/governance/314-governance-a-risk-articles/55748-public-sector-consultations

consequences of the decision the more likely there will be an expectation to consult" (Ibid.).

In the Birmingham case, there are serious questions to be asked in relation to whether they complied with these legal duties to consult, both in respect of the 2024/25 budget setting process and also in respect of the £750m of asset sales. According to the LGA's guidance on public consultations, local residents should be given enough information to make an informed response and residents should be given sufficient time to respond. According to the LGA[51], best practice is for the consultation to last from six to twelve weeks, with additional time for more major consultations. The authority should then allocate sufficient time to analyse the results, evaluate the process, and consider views before making any decisions. Additionally, the Government's own guidance documents state that local consultations should provide residents and stakeholders with sufficient information to enable them to make informed decisions[52]. In the Birmingham case, very little information was provided to residents on the detail of the proposed asset sales, and the local survey on the 2024/25 budget was released with no detail on the proposed cuts or links to the relevant documentation. This is in contrast to prior years, in which a full consultation document with a line by line breakdown of the budget proposals was released to residents.

The Council would go on to consult separately on individual cuts where they had specific statutory duties to consult, for example cuts to libraries, home school transport, and adult social care[53]. However, given that the cuts in these subsequent consultations were presented as essential due to the financial constraints of the 2024/25 budget, on which residents were given minimal consultation, it is questionable whether these consultations could be considered meaningful. For example, the home school transport consultation[54] which opened in February incorrectly links the Council's in-year deficits to their equal pay liabilities and outlines how existing provision is not affordable, concluding that:

> "we have to be candid and recognise that this proposal involves a reduction on what is offered. That is not something the Council wishes to do, but rather considers itself driven to by the current financial situation".

This consultation did not close until 22 March, more than two weeks after the Council voted through the proposals to cut the service.

---

[51] https://www.local.gov.uk/our-support/communications-and-community-engagement/resident-communications/understanding-views-2

[52] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/255180/Consultation-Principles-Oct-2013.pdf

[53] https://www.birmingham.gov.uk/info/50306/commissioners_intervention_and_improvement/2903/consultations_to_help_us_reshape

[54] https://www.birminghambeheard.org.uk/bcc/hometoschool-transport-policy-review-consultation/?utm_source=substack&utm_medium=email

The lack of meaningful consultation on the 2024/25 budget, together with limited consideration of equalities, therefore put a number of the cuts at risk of judicial review. In total, the Council's own budgetary task and finish group identifies nine separate savings proposals that were at "high risk" of judicial review (budget reference 15, 19, 89, 90, 146, 147, 148,149, and 193) affecting neighbourhood advisory services, libraries, children and youth services, and early help provision. This list is likely not comprehensive when one considers the Council's wide ranging statutory duties across adult social care, disability services, homelessness services, and housing.

Finally, it is important to note that the Council's legal duties extend well beyond their duty to consult residents. They hold wide ranging statutory duties across children's services, homelessness, adult social care, disabled people's services, environmental health, library provisions, and many others. The National Children's Bureau reported in 2023, for example, that Birmingham had been regularly in breach of the Children's and Families Act 2014 due to an underfunded and inadequate home school transport service for disabled children. This led to 261 disability tribunal cases in 2021 at a cost of around £1.6m. Similarly, in 2018, the Council set up Birmingham Children's Trust after "widespread and serious failures" were found by Ofsted that left children and young people at risk of harm. It is also just two years since the Council accepted findings that there were "serious and sustained breakdown in the services for vulnerable children and their families" in the city[55]. Despite this track record, the 2024/25 budget cut £9m from the Children's Trust budget and more than £8m from the Early Help scheme as part of a wider £55.6m cut to children's services[56]. They also cut a further £2m from the home school transport service.

A summary of the cumulative cuts identified by February 2023 is provided below in **Figure 10**:

[55] https://www.birminghammail.co.uk/news/midlands-news/birmingham-city-council-accept-send-25408459
[56] https://lscpbirmingham.org.uk/working-with-children/early-help/what-is-early-help

Figure 10: Initial savings targets by Directorate for 2024/25 and 2025/26

Directorate	2024/25 £'000	2025/26 £'000
Adult Social Care	23,709	52,861
Children & Families	52,228	63,231
City Housing	6,236	9,536
City Ops	39,268	57,111
PPS	8,365	11,150
SEP	2,447	2,597
Council Management	16,512	24,395
Cross-cutting	1,000	5,207
TOTAL	**149,765**	**226,088**

Source: 27th February 2023 Cabinet papers

Failures of best value

The accelerated timetable on which the Council identified the £149m of savings from the 2024/25 budget severely limited their ability to assess the impact of the cuts. This was brought out in several discussions at Audit Committee, Cabinet, and full Council. Across all of these meetings, and the narrative associated with the 2024/25 budget proposals, the response to such concerns was consistent – regardless of the possible damage to outcomes and service delivery, the cuts were needed to balance the books. This was, in turn, linked to the conditions of the capitalisation direction provided by the DLUHC. In practice, the statutory 'best value' intervention therefore had the effect of shifting the emphasis away from outcomes, prevention, and service delivery and instead towards input reduction. The intervention was therefore consistent with the 'austerity localism' model of governance in UK local government sector since 2010 (Ferry et al., 2022)[57].

The problem with this approach is two-fold: firstly, it not only damages outcomes, which often require stability of resources to deliver, but it has the somewhat dysfunctional effect of deprioritising outcomes in the assessment of best value, which runs counter to

[57] Ferry, L., and Murphy, P. (2018) 'What about Financial Sustainability of Local Government!—A Critical Review of Accountability, Transparency, and Public Assurance Arrangements in England during Austerity', International Journal of Public Administration, 41(8), pp.619-629.

the Government's own definition of best value assessment[58]. Thus, cuts are assessed not on their cost effectiveness or their impact on the strategic objectives of the Council, but, instead, simply on how easy and quickly they can be delivered. The second issue, is that this short term approach to financial planning not only damages outcomes, it also damages financial sustainability where cuts that have not been properly impact assessed develop unintended and unaccounted for knock on costs. Thus, they fail even on the more limited criteria of reducing inputs, potentially leading to cost spirals that undermine the medium term financial position of authorities. As covered in Section 2. this already appears to account for some of the financial challenges in the sector in the 2022-24 period.

These trends of increased focus on input reductions, reduced focus on outcomes, and the fragmentary nature of short-term financial planning in local government have been well documented in academic research [59] [60] [61] [62]. Several studies and reports on sector finances have also demonstrated how austerity cuts can turn out to be cash negative, as they target activities that save Councils money through revenue generation or service level pressure reductions[63] [64]. The LGA, for example, provide a comprehensive overview of how stable investment in children and young people, SEND services, public health, housing and homelessness, debt support, culture and the arts, adult social care, and asset management all provide strong financial returns on 5-year time horizons[65].

As introduced in Section 3., in the Birmingham case we see all of the above areas subject to short-term cuts with a near exclusive focus on input reduction and very minimal consideration on operational or financial consequences for the Council. Experience of more than a decade of austerity provides the evidence base to suggest that such cuts are highly likely damage outcomes and increase cost pressures on the Council, particularly in the areas of homelessness, adult social care, and looked after children. Many of the cuts, particularly the near complete defunding of the arts, also look set to damage the local economy and erode the local tax base, while the steep rises in Council Tax look

---

[58] https://www.gov.uk/government/publications/best-value-standards-and-intervention-a-statutory-guide-for-best-value-authorities/best-value-standards-and-intervention-a-statutory-guide-for-best-value-authorities#defining-best-value

[59] Brackley J., Tuck P. & Exworthy M. (2021) Public health interventions in English local authorities: constructing the facts, (re)imagining the future. *Accounting, Auditing & Accountability Journal*, 34(7), 1664-1691.

[60] Ellwood, S. (2014) 'Autonomy, Governance, Accountability and a New Audit Regime', *Public Money and Management*, 34(2), pp.139-141.

[61] Ferry, L., Midgley, H., Murphie, A., and Sandford, M. (2022) 'Auditing governable space – a study of place-based accountability in England', Financial Accountability and Management, 39, pp.772-789.

[62] Ferry, L., and Murphy, P. (2018) 'What about Financial Sustainability of Local Government!—A Critical Review of Accountability, Transparency, and Public Assurance Arrangements in England during Austerity', International Journal of Public Administration, 41(8), pp.619-629.

[63] https://www.kingsfund.org.uk/insight-and-analysis/data-and-charts/making-case-public-health-interventions

[64] https://www.local.gov.uk/sites/default/files/documents/driving-growth-through-lo-334.pdf

[65] https://www.local.gov.uk/publications/local-government-white-paper#ftn17

likely to drive up bad debt and contribute to child poverty. None of which is assessed in the proposals.

Our line by line review of the 2024/25 budgetary proposals showed that at least £70m of the £149m cuts came from cuts to front line service delivery, noting that these cuts are cumulative in nature and come on the back of some of the most severe cuts any authority had faced in the 2010/11 – 2020/21 period (see section 3.). The proposals include an estimated 600 job losses to a workforce that has already reduced by more than half since 2010, and include a £100m redundancy provision.

The line by line itemisation of the 2024/25 budget can be found in the 27th February Cabinet papers[66].

[66] https://birmingham.cmis.uk.com/birmingham/Committee/Executive/tabid/134/ctl/ViewCMIS_CommitteeDetails/mid/519/id/2/Default.aspx

8. Calls for an independent inquiry

Our report has outlined the current financial context of Birmingham City Council, and has reviewed issues relating to demand, equal pay and Oracle in the issuance of the city's section 114 notice. We highlight the wide-ranging value for money, audit and accountability issues in the Birmingham case, and how the subsequent statutory intervention may do more harm than good. The analysis drew on the financial plans, annual accounts, budget documentation, public notices, and agenda packs of core committee, together with informal discussions with a range of stakeholders and attendance at public meetings.

We were not, however, able to access private minutes, correspondence and other documents not in the public realm, full details of the Oracle costs, the model underlying the equal pay liability, or testimony from key actors. An independent public inquiry would therefore have significantly further scope to establish the facts and learn the lessons of the Birmingham case. We believe that this would be a worthwhile exercise that would have significant implications for the sector in terms of governance, audit reform and funding.

We also note that the citizens of Birmingham have been repeatedly promised a public inquiry, both by the city's elected leadership and by central government. These inquiries have been significantly delayed and now need to be delivered, because they are at risk of being seen as political rhetoric with no real, serious plans to back them up (see for example Jane Haynes piece in the Birmingham Mail on the eve of the West Midlands mayoral elections[67]).

We would therefore suggest a public inquiry should be commissioned to consider, among other issues:

- The appropriateness of the use of the 'best value' system to conduct a statutory intervention in the Birmingham case, including: whether sufficient best value assessment was conducted prior to the appointment of Commissioners, and the lessons for future statutory interventions in the sector.
- The role of the External Auditors in the statutory process, including: whether privately sector External Auditors are sufficiently independent of the local executive to be charged with statutory best value duties, and whether, in the Birmingham case, Grant Thornton acted within the relevant audit and ethical standards.
- Whether sufficient public consultation took place in relation to the 2024/25 budget and £750m of asset sales, and lessons for future engagement with the public in decisions of major public interest.

[67] https://www.birminghammail.co.uk/news/midlands-news/election-eve-leak-inquiry-birmingham-29092264

Based on the issued identified in this report, we would also encourage stakeholders and any future public inquiry to consider the following questions:

(1) Why was the extent of the Oracle IT disaster not disclosed to Council Committees until mid-2023, more than 12 months after 'go live'?
(2) Why did central government not conduct the usual best value assessment to properly understand the financial situation prior to statutory intervention in September 2023?
(3) Why did the auditors not make it clear in their statutory recommendations of September 2023 that the equal pay liability was unaudited and that they had not obtained the equal pay model upon which the £760m liability value was based?
(4) If the auditors had not audited or confirmed the £760m equal pay figure, as they claim, then why did Michael Gove assure parliament that it was "the independent auditor's assessment that the revised estimated equal pay liability is likely to be more than £760 million"?
(5) How does the Council intend to improve outcomes, as per the Improvement and Recovery Plan, when making deep cuts to the services in need of investment?
(6) Will the Council be transparent with residents if the cuts in the 2024/25 budget lead to a failure to deliver statutory services or a failure to comply with statutory duties?
(7) How will the Council avoid a further section 114 in April 2026 if it has not yet fully implemented the new Oracle system and is still running significant deficits?
(8) Why are the Council pressing ahead with asset sales to pay for an equal pay liability that the lead Commissioner is on the record as saying is overstated?