

Audit Committee

25 September 2020

Independent Review of Local Authority Financial Reporting and Audit

Ordinary Decision



Report of John Hewitt, Corporate Director of Resources

Electoral division(s) affected:

Countywide

Purpose of the Report

- 1 To provide Members with information on the outcome of the Redmond Review (the Review) into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting.

Executive Summary

- 2 In June 2019, Sir Tony Redmond was asked to undertake an independent review of the effectiveness of local audit and the transparency of local authority financial reporting.
- 3 His report makes detailed proposals for a new organisation, the Office of Local Audit and Regulation (OLAR), to be created to manage, oversee and regulate local audit.
- 4 He concluded that current arrangements do not allow for the public to understand the accounts and more can be done to improve transparency of what local authorities do. Therefore, authorities will be required to produce a new standardised statement of service information and costs, compared to the annual budget, that is aimed at taxpayers and service users. This will be presented alongside the statutory accounts.
- 5 In addition it was felt that generally there seems to be no real relationship between a local authority's Audit Committees and full Council, with very few reports going to full Council from Audit Committee. In future the external auditor will be required to present an Annual Audit Report to the first Full Council meeting after 30

September, irrespective of whether the accounts have been certified.

- 6 It is considered that the current audit fee structure does not enable auditors to fulfil their role in an entirely satisfactory way and that the cost is 25% lower than it should be; and as such the quality of auditors has reduced. There is concern that auditors do not have the experience or knowledge of local authorities with 40% of audits not being complete by the deadline for 2018/19. The current fee structure for local audit will thus be revised to ensure that adequate resources are deployed to meet the full extent of local audit requirements.
- 7 The deadline for publishing audited local authority accounts be revisited with a view to extending it from 31 July to 30 September.
- 8 CIPFA/LASAAC will be required to review the statutory accounts to determine whether there is scope to simplify the presentation of local authority accounts.

Recommendation

- 9 It is recommended that Members note the contents of this report.

Background

- 10 In June 2019, Sir Tony Redmond was asked to undertake an independent review of the effectiveness of local audit and the transparency of local authority financial reporting. Whilst conducting the Review his guiding principles were accountability and transparency. How are local authorities accountable to service users and taxpayers, and how are auditors accountable for the quality of their work; and how easy is it for those same individuals to understand how their local authority has performed and what assurance they can take from external audit work.
- 11 His report makes detailed proposals for a new organisation with the clarity of mission and purpose to act as the system leader for the local audit framework; and for a standardised statement of service information and costs, compared to the annual budget, that is aimed at taxpayers and service users. He concluded that current arrangements do not allow for the public to understand the accounts and more can be done to improve transparency of what local authorities do.
- 12 The Review questioned whether the Audit Committees understand the issues to query and challenge in an effective way. Generally, there is a relatively low number of independent Audit Committee members and little communication between Audit Committee and inspectors. There seems to be no real relationship between Audit Committee and Full Council with very few reports going to Council. The Review questioned the role of the three statutory officers in relation to Audit i.e. do they engage with the auditor together on an informal or formal basis. Internal Audit are not used much by External Audit as the code of practice does not require them to, however they could assist.
- 13 He reports that it became clear that the local audit market is very fragile. The current fee structure does not enable auditors to fulfil the role in an entirely satisfactory way. A view that the cost is 25% less than it should be and as a result the quality of auditors has reduced. With 40% of audits failing to meet the required deadline for reporting in 2018/19, this signals a serious weakness in the ability of auditors to comply with their contractual obligations. There is concern they do not have the experience or knowledge of local authorities. In addition, the ambition of attracting new audit firms to the local authority market has not been realised. Without prompt action to implement his recommendations, he reports that there is a significant risk that the firms currently holding local audit contracts will withdraw from the market.

- 14 It will be possible to achieve part of what needs to be done without legislation. However, to fully achieve the vision set out in the Review, changes to primary legislation will be essential. Only then does he feel the new organisation be able to do its job and to rebuild the sustainability of the local audit market.

Recommendations of the Review

External Audit Regulation

- 15 A new body, the Office of Local Audit and Regulation (OLAR), be created to manage, oversee and regulate local audit with the following key responsibilities:

- (a) procurement of local audit contracts;
- (b) producing annual reports summarising the state of local audit;
- (c) management of local audit contracts;
- (d) monitoring and review of local audit performance;
- (e) determining the code of local audit practice; and
- (f) regulating the local audit sector.

- 16 The current roles and responsibilities relating to local audit discharged by the:

- (a) Public Sector Audit Appointments (PSAA);
- (b) Institute of Chartered Accountants in England and Wales (ICAEW);
- (c) Financial Reporting Council (FRC)/ Audit, Reporting and Governance Authority (ARGA); and
- (d) The Comptroller and Auditor General (C&AG)

to be transferred to the OLAR. These staff will be TUPED to the new body.

- 17 There will be a Liaison Committee established, chaired by the Ministry of Housing, Communities and Local Government (MHCLG) and comprising FRC, ICAEW, National Audit Office (NAO), CIPFA, Local Government Association (LGA) and authority representatives, as well as Probation, Home Office and Audit Partners. They would meet quarterly and provide a link to the regulator. They would provide a facility for feedback and commentary in how the local audits are done. (This is not a recreation of the Audit Commission). It will consist of between 30 to 35 staff. OLAR could impose sanctions where there are significant

issues in a local authority e.g. If there were financial resilience issues where MHCLG are needed to intervene.

- 18 The governance arrangements within local authorities be reviewed by local councils with the purpose of:
 - (a) an annual report being submitted to Full Council by the external auditor;
 - (b) consideration being given to the appointment of at least one independent member, suitably qualified, to the Audit Committee; and
 - (c) formalising the facility for the 3 statutory officers: Chief Executive Officer, Chief Financial Officer and Monitoring Officer to meet with the External Auditor at least annually.
- 19 All auditors engaged in local audit be provided with the requisite skills and training to audit a local authority irrespective of seniority. There is a requirement for new s151 officers to receive induction/training on final accounts.
- 20 The current fee structure for local audit be revised to ensure that adequate resources are deployed to meet the full extent of local audit requirements.
- 21 That quality be consistent with the highest standards of audit within the revised fee structure. In cases where there are serious or persistent breaches of expected quality standards, OLAR has the scope to apply proportionate sanctions.
- 22 Statute be revised so that audit firms with the requisite capacity, skills and experience are not excluded from bidding for local audit work.
- 23 External Audit recognises that Internal Audit work can be a key support in appropriate circumstances where consistent with the Code of Audit Practice.
- 24 The deadline for publishing audited local authority accounts be revisited with a view to extending it to 30 September from 31 July each year.
- 25 The revised deadline for publication of audited local authority accounts be considered in consultation with NHS England and the Department for Health and Social Care, given that audit firms use the same auditors on both Local Government and Health final accounts work.

- 26 The external auditor be required to present an Annual Audit Report to the first Full Council meeting after 30 September each year, irrespective of whether the accounts have been certified; OLAR to decide the framework for this report.
- 27 NAO has issued a new Code of Practice on VFM and these will be endorsed. OLAR to undertake a post implementation review to assess whether these changes have led to more effective external audit consideration of financial resilience and value for money matters.

Financial Resilience of Local Authorities

- 28 MHCLG reviews its current framework for seeking assurance that financial sustainability in each local authority is maintained.
- 29 Key concerns relating to service and financial viability be shared between Local Auditors and Inspectorates including Ofsted, Care Quality Commission and Her Majesty's Inspectorate of Constabulary and Fire & Rescue Services, prior to completion of the external auditor's Annual Report.

Transparency of Financial Reporting

- 30 A new standardised statement of service information and costs to be prepared by each authority and be compared with the budget agreed to support the council tax/ precept/ levy and presented alongside the statutory accounts. The standardised statement will be used as a trial basis for the 2020/21 year end and from 2021/22 will be subject to external audit. The new statement will not need to be published. CIPFA is expected to consult on this between September and December.
- 31 The optimum means of communicating such information to council taxpayers/ service users be considered by each local authority to ensure access for all sections of the communities.
- 32 CIPFA/LASAAC will be required to review the statutory accounts, in the light of the new requirement to prepare the standardised statement, to determine whether there is scope to simplify the presentation of local authority accounts, including a review of IFRS as the basis for local authority accounts preparation.

Next Steps

- 33 As part of the final accounts preparations for 2020/21 financial year end, officers will consider any new requirements resulting from the Redmond Review.
- 34 Members to be kept informed of further developments following this Review.

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Appendix 1: Implications

Legal Implications

Preparation of annual accounts in compliance with the Accounts and Audit Regulations 2015 and the latest CIPFA Code of Practice on Local Authority Accounting which is based upon approved accounting standards in England and Wales and constitutes proper accounting practice under the terms of section 21(2) of the Local Government Act 2003.

Finance

None

Consultation

None.

Equality and Diversity / Public Sector Equality Duty

None.

Climate Change

None.

Human Rights

None.

Crime and Disorder

None.

Staffing

None.

Accommodation

None.

Risk

None.

Procurement

None.