

To: Audit and Governance Committee

Date: 14 January 2021

Report of: Head of Financial Services

Title of Report: The Redmond Review into Local Audit and Local Authority Financial Reporting

Summary and Recommendations

Purpose of report: To provide a summary of the findings of the Redmond Review into Local Audit and Local Authority Financial Reporting.

Key Decision No

Cabinet lead member Councillor Ed Turner

Policy Framework: n/a

Recommendations:

1) That the Committee consider implementation of the following recommendations from the report:

- a) Require the external auditor to present their annual report to Council
- b) Support an annual meeting of statutory officers with the key audit partner
- c) Support the addition of an independent audit committee member to the audit committee

2) Note the Report including the comments and the summary of the response from MHCLG

Appendices: None

Background

1. The Audit Commission was a statutory corporation established under the Local Government Finance Act 1982 which became operational on 1 April 1983. The

Commission's primary objective was to appoint auditors to a range of local public bodies in England, set the standards for auditors and oversee their work. On 13 August 2010, the Secretary of State for Communities and Local Government, announced that the Commission was to be scrapped and the Commission closed on 31 March 2015, with its functions being split between the voluntary, not-for-profit and private sector.

2. Public Sector Audit Appointments Limited (PSAA) was incorporated by the Local Government Association (LGA) in August 2014. PSAA is a company limited by guarantee without share capital and is a subsidiary of the Improvement and Development Agency (IDeA) which is wholly owned by the LGA. The Secretary of State for Housing Communities and Local Government has specified PSAA as an appointing person under provisions of the Local Audit and Accountability Act 2014. For audits of the accounts from 2018/19, PSAA appoints an auditor to relevant principal local government bodies that opt into its national scheme. Up to and including the financial year 2017/18, PSAA was responsible for publishing an annual report summarising the results of the audits of local authorities and the NHS under a Memorandum of Understanding between PSAA and the Ministry for Housing, Communities and Local Government (MHCLG). When the Memorandum of Understanding lapsed, MHCLG decided not to renew it which means that there is currently no body with responsibility for publishing this annual report.
3. Sir Tony Redmond was commissioned in June 2019 by the MHCLG to produce an independent review of the effectiveness of local audit and the transparency of local authority financial reporting. Sir Tony Redmond is a former Chartered Institute of Public Finance and Accountancy (CIPFA) president. The report was published on 9th September 2020 and can [be accessed online](#)
4. The purpose of the review was to:
 - examine the effectiveness of external audit activity in local government;
 - determine how audit supports public accountability, particularly to service users & council tax payers;
 - consider transparency of financial reporting, particularly whether the published information is understood by the public
5. The response from MHCLG was published on 17 December and can [be accessed online](#)

Summary of findings

6. The report contains 85 pages and so, as would be expected, contains many findings. The key findings are summarised below with the paragraph reference to the Redmond Review Report in brackets and comments underneath where relevant:
 - The Local Audit and Accountability Act 2014 split Audit Commission functions between 6 bodies, none of which has statutory responsibility to ensure that the audit framework operates coherently [2.2.4];

- Following the abolishment of the Audit Commission and MHCLG not commissioning another body after the 2017/18 financial year, no entity has been responsible for collating and reporting on work of public sector external audit work [5.3.12 – 5.3.13];

Comment: Following the abolition of the Audit Commission, responsibilities for external audit have become confusing for practitioners and therefore will be even more confusing to stakeholders

- Onerous audit tendering provisions in 2014 Act resulted in 98% of local authorities accepting PSAA auditor allocation, with market in provision of audit services not expanding as hoped [2.3.1 / 2.3.3];
- Neither the Financial Reporting Council (FRC) or the Institute of Chartered Accountants in England and Wales (ICAEW) are able to sanction auditors whose audit doesn't meet quality standards [2.3.14 / 2.3.19];
- Local authority audit fees fell significantly (42.25% in cash terms since 2015) while audit fees in other sectors have risen significantly [3.2.11 / 4.3.17];
- There has been an increase in the number & size of audit fee variation requests submitted by auditors to PSAA [3.4.2];

Comment: There appears to be two key reasons for this: the contracts did not include costs of the audit of Group Accounts and the reductions in scale fees has resulted in local authority external auditors having no contingencies for any work other than a completely trouble-free or query-free audit which in reality is not realistic.

- There is a view from local authorities that the audit contract doesn't provide complaints mechanism regarding audit services, while PSAA don't accept its role includes contract management [3.4.10 / 3.4.11];

Comment: Since the tendering process was undertaken by PSAA, local authorities have no power to manage contracts meaning that there is not any body fulfilling this role.

- The Accounting Code is long & complex, being highly prescriptive with detailed guidance: an alternative could be principles based Code that requires local authorities to comply with generally accepted accounting practice (GAAP) and only provides detailed guidance for adaptations to GAAP [2.3.24];

Comment: This move could lead to more differences becoming prevalent between the interpretations between different audited bodies and the external auditor.

- CIPFA's sales numbers demonstrate that at least one third of local authorities do not purchase an Accounting Code in any given year [7.2.5];

Comment: The finance team consider it important to obtain the latest Accounting Code in order to ensure compliance with the requirements contained therein. Oxford City Council therefore purchases a copy of the latest code through a CIPFA Publications subscription.

- Concerns have been raised by local authorities about the lack of knowledge, expertise, and continuity in local audit teams [4.3.6];

Comment: There have been changes in the audit team over recent years which can lead to additional pressures on the audit team due to them having to get acquainted with local requirements and differences. This must put an additional strain on already stretched audit resource.

- Audit firms indicate that it is difficult to recruit and retain public sector audit staff: pressures from compressed reporting timetable, and lack of profitability in sector seen as detrimental to career prospects [4.3.12];
- There is significant concern that existing fee structure has contributed to fragility of local audit sector with one of the registered firms deciding not to bid due to the fee levels [4.3.19];

Comment: The fee to this Council for the statement of accounts audit work has reduced from £86k for 2015/16 to £66k planned fee for 2019/20. An additional fee was approved by PSAA for payment for 2018/19 relating to additional work on Group Accounts and pensions.

- Significant audit time is spent on asset and pension valuations; local authorities believe focus should be on the cost of delivering services and financial resilience. Audit firms address valuations in context of FRC quality assurance process; the FRC view is that if audit focus on asset and pension valuations is inappropriate, should be addressed by CIPFA/LASAAC (the Chartered Institute of Public Finance and Local Authority (Scotland) Accounts Advisory Committee Code Board) through modifications to the Accounting Code [4.3.13 / 4.3.14 / 2.3.15];

Comment: Officers believe that too much focus and audit time is spent on assets and pensions when the transactions are reversed out to derive the General Fund balance. These balances and charges to revenue do not have the same impact on the statutory revenue accounts as in the private sector and so the emphasis should reflect this. It should also be noted that pension fund figures are audited within the pension fund accounts and this is in addition to those audits.

- There has been an increase in delayed audit opinions with 40% of the 2018/19 audits not completed by due date. Most common reasons provided by auditors to PSAA are poor quality working papers, potential qualifications, objections to accounts, and insufficient qualified audit staff [4.3.24];

Comment: Although this Council's audit was completed within the revised timeframes, indications are that the national position is the same as 2018/19.

- It is rare for Audit Committee to refer substantive items on to a full Council agenda so that a significant risk majority of elected Council members unaware of serious governance or financial resilience issues [5.3.3 / 5.3.6];

Comment: Although it is the case that at Oxford City Council, matters are not referred, there are not substantive items that would warrant such a referral.

- There has been increasing local authority commercialisation since 2015 which potentially poses risks to financial resilience, with potential lack of transparency on exposure to risk for the reader of financial statements [6.2.9 / 6.2.12];

Comment: Oxford City Council's Group Accounts are material which means that these accounts are included in the audit. Additionally, the Council has prepared Group Accounts since the establishment of the Barton Oxford LLP in

2012 which, although not material at that stage, meant that the Council's group relationships were disclosed in the accounts.

- Sustainability and resilience currently addressed through a 'Going Concern' review, which has been criticised by local authorities because they are unable to face bankruptcy or be wound up by management. The assessment is still valued by auditors [6.3.5];

Comment: A Going Concern assessment is not appropriate in a local authority context unlike in a private sector context due to the statutory nature of local authorities. However it is appropriate that auditors should provide a view on a Council's financial resilience; this should be labelled as such rather than using the private sector terminology so that it is clear to stakeholders what is being assessed.

- Neither financial or Value for Money (VfM) audits include a specific responsibility to provide an opinion on whether a local authority is financially sustainable (the ability to manage budgets over the medium term whilst continuing to deliver high quality and effective services that can be accessed by service users) leading to a potential gap compared to stakeholder expectation [6.1.1 / 4.6.1 / 6.2.8];
- Stakeholder expectation gaps should be partly bridged by the scope of the audit including substantive test of a local authority's financial resilience and sustainability: NAO 2020 Audit Code provides three reporting criteria: Financial sustainability, Governance, Improving economy, efficiency and effectiveness [6.5.2 / 6.5.4];
- There is potential to examine financial resilience in the VfM opinion: the Audit Code effective from 2020-21 requires auditors to provide a narrative statement on arrangements in place, but there is not a requirement to consider local authority systems and performance against specific standards or good practice examples. There is also a lack of guidance on how to assess whether a VfM risk is material [6.3.6 – 6.3.8];

Comment: A test of financial resilience could replace the current Going Concern assessment to be incorporated along with the current VfM assessment into a replacement for the VfM aspects of an audit.

- Local authority accounts are widely considered not to be transparent or easily understandable: to be improved through a new summary statement presented alongside accounts. The review finds that this is preferable to removal of International Financial Reporting Standards (IFRS) as basis for the preparation of accounts, or adjustments to current narrative statement [7.4.1 / 7.5.1 to 7.5.20];

Comment: It is the disparity between IFRS and the statutory basis of local authority finances which directly leads to the lack of transparency and the inclusion of additional statements which reconcile the IFRS accounts back to statute. Additionally the criticism of the level of emphasis placed on asset and pension fund valuations arise through the application of IFRS. The logical response would be to remove the strict application of IFRS where it doesn't align with the local authority legislative basis.

The change to the Comprehensive Income and Expenditure Statement (CIES) led both to the addition of Expenditure and Funding Analysis (EFA) and also

additional supporting notes. It also meant that local authority revenue accounts ceased being directly comparable either between years or between authorities and to additional work being needed on an ongoing basis to revise the CIES and EFA prior year comparatives. This change was intended to provide a direct comparison to the management accounts reporting and to clarify the annual expenditure used and funded by the Council together with the adjustments between the funding and accounting basis to reconcile with the CIES. There are discrepancies between how Councils actually report in-year financial information and the requirements of the CIES and EFA production (for instance in respect of the Housing Revenue Account) and the reformatting of data included in the Movements in Reserves Statement such that the result is that neither aim is achieved.

The production of an additional statement could add more pressures to local authority finance departments which already have very stretched resources. The Council's current narrative report already contains the majority of the content of the proposed summary statement and with a few adjustments could achieve the intended result. If necessary the narrative report could then be extracted into a separate document.

- Statutory guidance would be required to determine the form and content of Summarised Accounts which could include service information and costs, budget setting compared to outturn, and a simplified Balance Sheet 6 [7.5.16].

Comment: As noted above, the Council's narrative report includes the majority of the proposed information and so any statutory guidance should be directed to the format and content of the narrative report to remove the potential additional burden which would be placed on local authority finance teams.

Key Recommendations

7. There were a number of recommendations arising from the review. The main ones are summarised below with comments as appropriate:

- The creation of an Office of Local Audit Regulation to oversee, procure, manage and regulate the external audits of local authorities

Comment: The consistency and clarity this would give is to be welcomed, however it should result in significant additional costs to local government where finances are already under pressure.

- **MHCLG** do not agree that there is enough reason to set up another armslength organisation.
- Annual report from external audit submitted to the first full Council meeting after 30 September each year (enhance public transparency & accountability)

Comment: The Audit and Governance Committee has delegated responsibility to approve the statement of accounts and consider the reports from the external auditors and as things stand, this would continue. A decision would be needed to be taken to change constitutional delegations if it were deemed appropriate to submit the auditor's report to Full Council.

MHCLG strongly agree with the recommendation that the external auditor be required to present an annual audit report to a Full Council meeting,

irrespective of whether the accounts have been certified. Although they note that many local authorities feel existing reporting arrangements to audit committees are sufficient, they believe that presentation to Full Council is an important opportunity for potential risks or concerns to be escalated in a timely way and that this should be best practice. MHCLG will explore options with relevant stakeholders including the LGA and the National Audit Office as to how this can best be achieved, and whether the 30 September milestone is most appropriate. If a legislative opportunity arises, the department will consider enshrining this in statute.

- Local authorities to have at least one independent member on their audit committees

Comment: Any independent members of an audit committee would normally receive payment which would therefore have to be funded by the Council. Additionally there would need to be a recruitment process to identify a suitably skilled and / or qualified individual. There will also be considerations of confidentiality which may have to be addressed if there are any audit reports that have to be on a private part of the agenda. The Council currently has the powers to employ an independent audit committee member although this would need a change to the constitution.

- Formal requirement for statutory officers to meet at least annually with the Key Audit Partner

Comment: It is unclear how the Council itself can make this a formal requirement as suggested by the report, however it is simple to put this in place at officer level.

- All auditors engaged in local audit be provided with the requisite skills and training to audit a local authority revisions in the current fee structure for external audits

Comment: This could result in an increase in fees to Councils of a suggested 25% (£17k for Oxford City Council). Any revision should be after reducing the scope and emphasis for external audit including assets and pensions.

MHCLG have stated that they will make £15 million available to local authorities to meet the anticipated increases in audit fees. How this will be allocated and whether the funding will be sufficient is currently unclear but MHCLG have stated that the allocations will be confirmed once PSAA has set its fee scales for the audit of the 2020/21 accounts.

- New powers to sanction firms for significant audit failures
- External audit teams encouraged to engage more effectively with local authority internal audit functions

Comment: This would be welcomed if it would enable internal audits to be targeted to give assurance on specific areas of systems operation. Currently there is a level of duplication with external audit including walk-through tests in their audit. However it should be noted that although the engagement may be encouraged, it does not mean that it will definitely occur or that it would make any changes to the level of audit.

- Deadlines for audits extended to 30 September extend deadline for publishing audited accounts from 31 July to 30 September

Comment: This would assist audit firms in spreading the pressure of compressed audit periods. Oxford City Council would still wish to complete the accounts and the audit of those accounts prior to any extended deadline although it should be noted that this could only be achieved if external audit resourcing allows this.

MHCLG have stated that, subject to consultation in the new year (2021), they intend to amend regulations to extend the deadline for publishing audited local authority accounts from 31 July to 30 September, for a period of two years (i.e. covering the audit of the 2020/21 and 2021/22 accounting years). At the end of this period there will be a review of whether there is a continued need to have an extended deadline.

- More effective external audit consideration of financial resilience and value for money matters. MHCLG reviews its current framework for seeking assurance that financial sustainability in each local authority in England is maintained.

Comment: Where resilience is to be tested through the external audit, this should be formalised as to exactly what this means so that there is clarity for both auditors and local authorities. The concept of “going concern” applied in private sector audits is not appropriate for local authorities, although financial resilience is and is assessed to some extent at budget setting within the section 151 officer’s section 25 report.

- A simplified standard financial statement of services and costs to be made available to the public and subject to audit enabling comparison to annual budget and council tax. Councils to decide how best to publicise this statement to ensure access for all sections of the communities.

Comment: This statement would be additional to the statement of accounts as the recommendation stands, although the Council’s current narrative report within the statement of accounts includes much of the same information and is in a similar format. Producing something separate could result in additional costs of production and audit and it would be preferable to adapt the narrative report to cover these requirements and, if necessary, produce the report by extracting the Council’s narrative report into a separate publication. It could be argued that since local authority accounts are supposed to report the financial position of the Council to the public, then it should be these that change. The Council currently publishes its accounts on its website. Other approaches, such as posting documents to all householders and potentially translating to other languages could be prohibitively expensive for little if any additional benefit.

MHCLG agree with the recommendations that all local authorities be required to prepare an audited standardised statement of service information and costs which are short and accessible, for example one or two pages. MHCLG hold the view that these should be communicated to all taxpayers and service users, and they will explore how this can be done, for example, alongside or with council tax bills from 2022.

- CIPFA-LASAAC Local Authority Code Board look again at the composition of the statutory accounts to see if improvements can be made to improve their usefulness and understandability.

Comment: This review would be welcomed if it resulted in the removal of time-consuming transactions that both don't add anything to the real position of the Council and also make the accounts confusing and complicated to the reader.

MHCLG agree with this recommendation and state that they will work with CIPFA-LASAAC on simplifications.

Financial Implications

8. These are covered within the main body of the report.

Legal Implications

9. The recommendations have a range of legal bases. Some of the recommendations can be implemented through directions from Government, some will require primary or secondary legislation and others could be voluntarily adopted by the council.

Risk Implications

10. There are no risks associated with the recommendations in this report.

Communication

11. None

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Background papers:

The Redmond Review Report into Local Audit and the Transparency of Local Authority Financial Reporting

<https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-independent-review>

Ministry for Housing, Communities, and Local Government response to the review

<https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-government-response-to-the-redmond-review/local-authority-financial-reporting-and-external-audit-government-response-to-the-independent-review>

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