Cherwell District Council

Accounts, Audit and Risk Committee

18 November 2020

Redmond Review into Local Government Audit

Report of the Director of Finance

This report is public

Purpose of report

To update the Accounts, Audit and Risk Committee on the outcome of the Redmond Review into Local Government Audit.

1.0 Recommendations

The meeting is recommended:

1.1 To note the findings of the Redmond Review

2.0 Introduction

2.1 In July 2019, the then Secretary of State for the Ministry of Communities, Housing and Local Government, James Brokenshire commissioned a review of the arrangements in place to support the transparency and quality of local authority financial reporting and external audit including those introduced by the Local Audit and Accountability Act 2014. Sir Tony Redmond was appointed to undertake the review due to his experience in the Local Government sector and fromer role as President of the Chartered Institute of Public Finance and Accountancy (CIPFA).

2.2 A Call for Views was launched in September 2019 and received 156 responses and more than 100 interviews were carried out. The report arising from the review was published on 8th September 2020. The full report is published at GOV.UK

2.3 The Review was carried out in the context that Local Government in England is responsible for 22% of total UK public sector expenditure making it essential that local authority financial reporting is of the highest level of transparency to allow taxpayers to understand how their money is being spent. The Review examined the effectiveness of local audit and its ability to demonstrate accountability for audit performance to the public. It also considered whether the current means of reporting the Authority's annual accounts enables the

public to understand this financial information and receive the appropriate assurance that the finances of the authority are sound.

2.4 The key findings of the Review, summary of recommendations, and potential implications for the Council are set in this report.

3.0 Report Details

3.1 The key findings of the Review can be summarised into four themes:

(i) **Local Audit arrangements** – The most significant finding is the lack of coherence in local audit arrangements including in the approach to procuring audit services. There were serious concerns regarding effectiveness of local audit which is in part due to the current fee structure.

(ii) **Current Fee Structure –** The Review estimated that the cost of External Audit is 25% less than it should be and as a result the quality of auditors has reduced. There is also concern auditors do not have the experience or knowledge of local authorities. Evidence was considered that 40% of local authority audits were not completed by the 31 July deadline for 2018/19.

(iii) **Governance arrangements** – The Review questioned whether Audit Committees understand the issues to question and challenge in an effective way and noted that there are relatively low number of independent Audit Committee members and little communication between Audit Committee and inspectors with no formal exchange of views. There seems to be no real relationship between Audit Committee and Full Council with very few audit reports going to Council. The Review questions the role of three statutory officers (Head of Paid Service, Monitoring Officer and Section 151 Officer) in relationship to Audit and in particular whether they engage with auditor together on an informal or formal basis. The Review noted that Internal Audit is not currently utilised effectively by External Audit as the Audit code of practice does not require them to liaise with the Internal Audit function. The Review also noted that there is not always sufficient expertise amongst staff involved in completing the year end accounts process.

(iv) **Transparency and reporting** – The Review concluded that the current arrangements do not enable the general public to understand the statement of accounts and found that more can be done to improve the transparency of what local authorities do. Consideration was given to simplifying the accounting framework for local government accounts, however this was not considered appropriate in the context of local authorities becoming more commercial in their operations.

Review Recommendations

3.2 The Review Recommendations are set out in full at Annex 1. The Review contains 23 recommendations across four categories of which three categories and 19 recommendations apply to the production of the Council's accounts and external audit. The remaining category, containing three recommendations applies only to smaller authorities with an annual turnover of under £6.5m. Recommendation 23 also applies only to smaller authorities.

External Audit Regulation

3.3 The central recommendation of the Review is for the creation of a new body, the Office of Local Audit and Regulation (OLAR), to manage, oversee and regulate local audit with the following key responsibilities:

- procurement of local audit contracts;
- producing annual reports summarising the state of local audit;
- management of local audit contracts;
- monitoring and review of local audit performance;
- determining the code of local audit practice; and
- regulating the local audit sector.

3.4 The review also focusses on the sustainability of the external audit market, the skills within the audit team and the level of audit fees. The review sets out recommendations to address these issues.

3.5 Public Sector Audit Appointments (PSAA) was incorporated by the Local Government Association (LGA) in 2014 and has been specified by MHCLG as an 'appointing person' under provisions of the Local Audit and Accountability Act 2014. PSAA appoints external auditors to local authorities and is responsible for the statutory function of setting audit fees, including the current practice of agreeing fee variations for additional audit work. It is recommended that the responsibilities of this body be discharged by the OLAR which will set a fee structure that will 'ensure that adequate resources are deployed to meet the full extent of local audit requirements' and that the quality of the audit will 'be consistent with the highest standard of audit within the revised fee structure.'

3.6 A number of other recommendations are made in this category, including that, where appropriate, external audit should use the work of Internal Audit to support their conclusion. The report recognizes that internal auditors are much closer to the business than external audit, providing a 'rich source of knowledge' and work which focuses on governance and service delivery matters.

3.7 The Review recommends that the deadline for the completion of audits be extended from 31 July to 30 September to enable more time for the audit to take place and to make easier for audits to be resourced. This proposal would require an amendment to the Accounts and Audit Regulations 2015.

3.8 Not all recommendations require a change to statute and some recommendations could be adopted based on local decisions such as:

- Formalising the facility for the Chief Exec, Monitoring Officer and Chief Finance Officer to meet with the Key Audit Partner at least annually, and;
- Appointing at least one suitably qualified independent member to the Audit Committee

3.9 It is also recommended that the external auditors should report to Full Council annually in September in addition to the current practice of reporting to Audit Committees. They should report to all members on risks identified and conclusions reached in a transparent and understandable format to reduce the risk that a majority of elected members may not be sighted on serious governance or financial resilience issues.

Financial Resilience of local authorities

3.10 Under the current regulations there is no specific responsibility for auditors to provide an opinion on whether a local authority is financially sustainable. The Review recommends that MHCLG reviews its current framework for seeking assurance that financial sustainability in each local authority in England is maintained and that key concerns relating to service and financial viability be shared between Local Auditor and Inspectorates including Ofsted, Care Quality Commission and HMICFRS prior to completion of the external auditor's Annual Report.

3.11 The Review considers a number of possible frameworks for assessment including CIPFA's Pillars of Financial Resilience and the Financial Management Code of Practice (FM Code). Although not prescribed in the formal recommendation, the review notes that MHCLG could give the FM Code statutory status and require local authorities to report on compliance with the Code in their Annual Governance Statement with auditors expected to report on material breaches.

Transparency of Financial Reporting

3.12 The Review recommends the development of a new 'Summarised Accounts' or 'Simplified Statements' that are prepared on the budget setting basis and reconcilable to the Council Tax Requirement. These accounts would:

- include a standardised statement of service information and costs, perhaps based on the statutory Service Reporting Code of Practice (SERCoP)
- be reconcilable to the Statutory Accounts
- be subject to audit.

3.13 The objective of creating these additional statements is to increase transparency and, as a short stand-alone document, would be accessible to taxpayers and service users. There may also be an opportunity to remove some of the existing statements and disclosures within the statement of accounts that reconcile the outturn position, funding position and IFRS accounting basis, although it is noted that the work to complete the reconciliation would still need to be undertaken.

3.14 The Primary Legislation for the Local Authority Accounting Framework is the Local Government Act 2003 which allows the Secretary of State to make provision about accounting practices that local authorities must follow. The Secondary Legislation is the Capital Finance and Accounting Regulations 2003 which gives CIPFA the power to produce a statutory accounting code. This means that CIPFA can take forward this recommendation through revisions to the Accounting Code of Practice without amendments to primary or secondary legislation. In practice, this would be done in consultation with the Financial Reporting Advisory Board (FRAB) which advises HM Treasury on public sector accounting.

Recommendations into practice

3.15 If adopted in full, the review recommendations have an impact on the preparation of the annual statement of accounts and the annual audit process which will have resource implications for the Council. The degree to which this applies will depend on how many of the recommendations are taken forward.

External Audit Regulation

3.16 The creation of the OLAR is estimated to cost in the region of £5m per year. Identifying funding for this is outside of the scope of the recommendations. In terms of the proposal to review the audit fee, the PSAA already has the ability to agree fee variations and it is common for additional fees to be agreed. At this stage it is difficult to estimate how significant a fee increase would be for individual authorities after taking account of these additional fees.

3.17 The proposed extension of the audit deadline from 31 July to 30 September could have a detrimental impact on resources in the finance team with staff leave over the summer period needing to be balanced with the audit requirements and impacting on the team's ability to move onto other areas work.

3.18 The recommendation for external audit to place reliance on the work of internal audit may help to decrease the level of audit activity although this could also impact on the internal audit work plan.

Financial Resilience of local authorities

3.19 It is acknowledged in the Review that expanding the scope of the audit will increase audit costs (both in terms of the audit fee and resource to respond to audit queries) but concludes that the expansion of the opinion to encompass financial resilience and sustainability would, potentially, provide comfort to the authority and to council taxpayers that the finances are in good order.

3.20 The impact on resources will not be clear until MHCLG set out a proposed assurance framework. However, if the framework is consistent with the suggestions set out in the Review, this should not create a significant resource requirement. Although the FM Code does not have statutory status, the Council is already planning to self-assess and report on compliance with the code to the Audit & Governance Committee.

Transparency of Financial Reporting

3.21 The introduction of an additional financial statement is likely to create additional work for the finance team. Although the review makes recommendations about extending the audit period there is no recommendation to extend the date for the publication of the draft accounts beyond the 31 May, concentrating further work into an already short period of time.

3.22 The Review does not comment on other external reporting completed by local authorities. The Council already produces an outturn report which is reconciled to the budget set by Council in February and reported to Cabinet in May or June following the 31 March. In addition, all local authorities are required to complete the Revenue Outturn report to MHCLG which is based on the SERCoP. There is a risk that the addition of another reporting format may create duplication and further confusion for residents.

Responses to the publication of the review

3.23 In the press release announcing the publication of the review, the Secretary of State for Communities, Housing and Local Government stated that 'This government remains committed to a locally-led audit regime, alongside robust local scrutiny and local accountability by the press and public.' MHCLG will 'carefully consider the recommendations proposed, which will play an important strategic role in strengthening the overall framework for local accountability.' However, a timeframe for this has not been set out and no formal commitment has been made to implement the recommendations.

3.24 The Chief Executive of CIPFA, Rob Whiteman welcomed the recommendations in the Review, including the creation of the new audit body to 'ensure a stable future for local public audit that is currently at risk.' Whiteman also praised the proposed new financial reporting requirements which 'would support more effective communication of the often-complex financial affairs of local authorities.'

3.25 CIPFA have sought stakeholders' views on the impact of the recommendations and other commentaries of the Review on local authority financial reporting and the strategic plan for the development of the Code in its consultation on the 2021/22 Code of Practice which closed on 23 October.

3.26 The PSAA has issued a response to the Review which is broadly supportive of the report. However, the response also raised concerns that structural reorganisation, including the creation of the OLAR, would take time and would therefore not resolve the current challenges facing the audit sector. It is also unclear where the additional resources will come from to fund investment in external audit.

4.0 Conclusion and Reasons for Recommendations

4.1 It is important that the Accounts, Audit and Risk Committee is aware of the recommendations that have been proposed from the Redmond Review.

5.0 Consultation

None

6.0 Alternative Options and Reasons for Rejection

6.1 None – the report is for information.

7.0 Implications

Financial and Resource Implications

7.1 There are no financial implications associated with this report.

Comments checked by:
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Legal Implications

7.2 There are no legal implications associated with this report.

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Risk Implications

7.3 There are no risk management implications arising directly from this report.

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8.0 Decision Information

Key Decision N/A

Financial Threshold Met: N/A
Community Impact Threshold Met: N/A

Wards Affected

All

Links to Corporate Plan and Policy Framework

All Corporate Plan Themes

Lead Councillor

N/A

Document Information

Appendix number and title

- Appendix 1 – Summary of Review Recommendations

Background papers

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