

DERBYSHIRE COUNTY COUNCIL

AUDIT COMMITTEE

8 December 2020

**Report of the Director of Finance & ICT and Assistant Director of
Finance (Audit)**

REDMOND REVIEW

1 Purpose of the Report

To provide Audit Committee with an overview of the report on the Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting, known as the 'Redmond Review'.

2 Information and Analysis

In June 2019 Sir Tony Redmond was asked by the then Secretary of State for the Ministry of Housing, Communities and Local Government (MHCLG) (Rt Hon. James Brokenshire MP) to undertake an independent review of the effectiveness of local audit and the transparency of local authority financial reporting – The Redmond Review. In April 2020 a new Code of Audit Practice came into force and consultation started shortly afterwards on its application and guidance for 2020-21 external audits. The Redmond Review (Review) was published in early September 2020 and includes reference to the Audit Code, the consultation on which also closed in early September 2020.

The Review also considered how local authorities are accountable to service users and taxpayers, how auditors are 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. It encompassed not only principal local authorities but also Police and Crime Commissioners, Fire and Rescue Authorities and Parish Councils.

The report on the Review followed with a consultation inviting views, information and evidence on, in particular:

- definitions of audit and its users;
- the expectation gap;
- audit and wider assurance;
- the governance framework;
- audit product and quality;

- auditor reporting;
- how local authorities respond to audit findings; and
- the financial reporting framework.

The call for views was aimed at anyone with a direct or indirect interest in local authority audit and financial reporting. A response was submitted by the Derbyshire Finance Officers Association (DFOA). DFOA is comprised of the Chief Finance Officers from the eight district and borough councils, city and county councils and the fire authority of the county of Derbyshire.

The Review received 156 responses to the call for views and carried out more than 100 interviews. Serious concerns were expressed regarding the state of the local audit market and the ultimate effectiveness of the work undertaken by audit firms. The Review report highlights that this is not to say that the audits are carried out unprofessionally but that there remains a question of whether such audit reports deliver full assurance on the financial sustainability and value for money of every authority subject to audit. A particular feature of the evidence submitted related to concern about the balance of price and quality in the structure of audit contracts.

A regular occurrence in the responses to the call for views suggested that the current fee structure does not enable auditors to fulfil the role in an entirely satisfactory way. To address this concern, the Review recommends that an increase in fees is considered. With 40% of audits failing to meet the required deadline for reporting in 2018-19, the Review reports that this signals a serious weakness in the ability of auditors to comply with their contractual obligations and recommends that the current deadline should be reviewed. A revised date of 30 September gathered considerable support amongst respondents who expressed concern about this current problem. However, the Review report concludes that this only in part addresses the perceived quality problem.

The Review report notes that an underlying feature of the existing framework is the absence of a body to coordinate all stages of the audit process and that although there is some scope to effect alterations to the individual roles, appropriately fulfilled within the existing framework, this would not achieve the overriding objective of providing a coherent local audit function which offers assurance to stakeholders and the public, in terms of performance and accountability of the local authority and the auditor.

Consequently, a key recommendation of the Review is to create a new regulatory body responsible for procurement, contract management, regulation and oversight of local audit. It is recognised that the new body will liaise with the Financial Reporting Council (FRC) with regard to its role in setting auditing standards. The engagement of audit firms to perform the local audit role would be accompanied by a new price/quality regime to ensure that audits were performed by auditors who possessed the skills, expertise and

experience necessary to fulfil the audit of local authorities. These auditors would be held accountable for performance by the new regulator, underpinned by the updated code of local audit practice. A further recommendation is to formalise the engagement between local audit and Inspectorates to share findings which might have relevance to the bodies concerned.

The Regulator would be supported by a Liaison Committee comprising key stakeholders and chaired by the Ministry of Housing, Communities and Local Government (MHCLG). The new regulatory body would be small and focused and would not represent a body which has the same or similar features as the Audit Commission.

The Review recognises that local audit is subject to less critical findings in respect of audit procurement and quality relating to smaller authorities. However, the recommendations include a review by Smaller Authorities' Audit Appointments (SAAA) of current arrangements relating to the proportionality of small authority audits, together with the process for managing vexatious complaints, where issues have been raised by those bodies which have experienced such challenges.

Governance in respect of the consideration and management of audit reports by authorities has also been examined in considerable detail. Based on evidence presented, the Review concludes that there is merit in authorities examining the composition of Audit Committees, including the appointment of at least one independent member, in order to ensure that the required knowledge and expertise are always present when considering reports, together with the requirement that at least an annual audit report be submitted to Full Council. This would demonstrate transparency and accountability from a public perspective, which the Review reports is currently lacking in many authorities.

The Review questions whether external audit could make more use of the knowledge and expertise of internal audit in developing sufficient understanding of the local authority. Internal auditors are likely to be closer to the business than external audit and, in many authorities, a proportion of their work focuses on governance and service delivery matters.

The Review notes that the issue of transparency is of equal relevance to the current presentation and publication of the annual accounts. Given that the feedback from practitioners and other key stakeholders revealed that current statutory accounts prepared by local authorities are considered to be impenetrable to the public, the Review recommends that a simplified statement of service information and costs is prepared by each local authority, in such a way as to enable comparison with the annual budget and council tax set for the year. This would enable Council taxpayers and service users to judge the performance of the local authority for each year of account. The new statement would be prepared in addition to the statutory accounts, which

could be simplified. The Review also recommends that all means of communicating such information should be explored to achieve access to all communities.

In summary, the outcome of the Review is designed to deliver a new framework for effective local audit and an annual financial statement, which enables all stakeholders to hold local authorities to account for their performance, together with a robust and effective audit reporting regime. The Review report notes that aside from the additional costs arising from a fee increase, the resource implications of the new regulatory body would amount to approximately £5m per annum after taking into account the amount related to staff subject to transfer under TUPE arrangements.

A complete list of the Recommendations from the Review is included at Appendix One to this report, alongside comments - where relevant - on the Council's position.

Implementation of the Review recommendations would, in part, require regulatory or legislative change but the Review report notes that many of the issues identified require urgent attention, given the current concerns about local audit demonstrated in the Review.

The Council has commenced a dialogue with its external auditors to discuss the findings of the Review.

3 Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal, prevention of crime and disorder, equality and diversity, human resources, environmental, health, property, transport and social value considerations.

4 Background Papers

Papers held electronically by Technical Section, Finance & ICT Division, Room 137.

5 Officers' Recommendation

That Audit Committee notes this overview of the Redmond Review and the recommendations arising from it, as set out in the associated report.

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Assistant Director of Finance (Audit)

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The recommendations of the Redmond Review are as follows, alongside comments - where relevant - on the Council's position:

External Audit Regulation

1. 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:
 - 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.

2. The current roles and responsibilities relating to local audit discharged by the:
 - Public Sector Audit Appointments (PSAA);
 - Institute of Chartered Accountants in England and Wales (ICAEW);
 - FRC/ARGA; and
 - The Comptroller and Auditor General (C&AG)

to be transferred to the OLAR.

3. A Liaison Committee be established comprising key stakeholders and chaired by MHCLG, to receive reports from the new regulator on the development of local audit.

4. The governance arrangements within local authorities be reviewed by local councils with the purpose of:
 - an annual report being submitted to Full Council by the external auditor;
 - consideration being given to the appointment of at least one independent member, suitably qualified, to the Audit Committee; and
 - formalising the facility for the CEO, Monitoring Officer and Chief Financial Officer (CFO) to meet with the Key Audit Partner at least annually.

The results of the annual audit are reported each year to Full Council. It has been agreed with Mazars that in future they will attend that meeting to present their report in person. In the past consideration has been given to the involvement of an independent member on the Audit Committee, perhaps now is the time to consider the option again, perhaps utilising a joint appointment with another public body but without compromising the

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role of elected representatives. At present the auditor meets frequently with the key statutory offices in the council, formalising this process will be a sensible move.

5. All auditors engaged in local audit be provided with the requisite skills and training to audit a local authority irrespective of seniority.
6. 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.

Whilst this may mean an increase in costs it is time to reverse the recent decreases in fee levels as it has resulted in an unstable market for audit services and an audit that has, on occasion, not been fit for purpose across some parts of the local government sector.

7. 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.
8. Statute be revised so that audit firms with the requisite capacity, skills and experience are not excluded from bidding for local audit work.
9. External Audit recognises that Internal Audit work can be a key support in appropriate circumstances where consistent with the Code of Audit Practice.

External Audit reliance on the work of Internal Audit has diminished over the years and now is an appropriate time to rebuild that relationship, to assess whether collaboration can assist External Audit in obtaining the assurance they require in respect of the accuracy and completeness of the statement of accounts. The Council has an established External and Internal Audit Protocol which provides a firm basis for further development of this relationship.

10. The deadline for publishing audited local authority accounts be revisited with a view to extending it to 30 September from 31 July each year.

Whilst such a change is understandable due to the capacity issues in External Audit firms, it is regrettable that such a move is necessary and we would hope that when some element of stability has returned to the market then consideration may be given to a return to a July date.

11. The revised deadline for publication of audited local authority accounts be considered in consultation with NHSI(E) and DHSC, given that audit firms use the same auditors on both Local Government and Health final accounts work.

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12. 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.
13. The changes implemented in the 2020 Audit Code of Practice are 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.

Smaller Authorities Audit Regulation

14. SAAA considers whether the current level of external audit work commissioned for Parish Councils, Parish Meetings and Internal Drainage Boards (IDBs) and Other Smaller Authorities is proportionate to the nature and size of such organisations.
15. SAAA and OLAR examine the current arrangements for increasing audit activities and fees if a body's turnover exceeds £6.5m.
16. SAAA reviews the current arrangements, with auditors, for managing the resource implications for persistent and vexatious complaints against Parish Councils.

Financial Resilience of local authorities

17. MHCLG reviews its current framework for seeking assurance that financial sustainability in each local authority in England is maintained.

This is welcomed in view of the recent financial failures in local authorities.

18. Key concerns relating to service and financial viability be shared between Local Auditors and Inspectorates including Ofsted, Care Quality Commission and HMICFRS prior to completion of the external auditor's Annual Report.

Transparency of Financial Reporting

19. A standardised statement of service information and costs 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.

If such a statement can be made to simplify reporting into an easily understandable explanation of the Council's financial position, then it is to be welcomed.

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20. The standardised statement should be subject to external audit.
21. 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.
22. CIPFA/LASAAC 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 by removing disclosures that may no longer be considered to be necessary.

Such a move has been required for a long time and it is hoped real simplification can be achieved.

23. JPAG be required to review the Annual Governance and Accountability Return (AGAR) prepared by smaller authorities to see if it can be made more transparent to readers. In doing so the following principles should be considered:
 - Whether “Section 2 – the Accounting Statements” should be moved to the first page of the AGAR so that it is more prominent to readers;
 - Whether budgetary information along with the variance between outturn and budget should be included in the Accounting Statements; and
 - Whether the explanation of variances provided by the authority to the auditor should be disclosed in the AGAR as part of the Accounting Statements.