

READING BOROUGH COUNCIL
EXECUTIVE DIRECTOR OF RESOURCES

TO:	AUDIT & GOVERNANCE COMMITTEE		
DATE:	28 January 2021		
TITLE:	INDEPENDENT REVIEW INTO THE OVERSIGHT OF LOCAL AUDIT AND THE TRANSPARENCY OF LOCAL AUTHORITY FINANCIAL REPORTING ("REDMOND REVIEW")		
LEAD COUNCILLOR:	COUNCILLOR EMBERSON	PORTFOLIO:	CORPORATE AND CONSUMER SERVICES
SERVICE:	AUDIT & INVESTIGATIONS	WARDS:	N/A
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1. PURPOSE OF REPORT

- 1.1 In June 2019, the Secretary of State for Housing, Communities and Local Government (MHCLG) asked Sir Tony Redmond to undertake an independent review (Redmond Review) of the effectiveness of local audit and the transparency of local authority financial reporting.
- 1.2 The Redmond 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 a Local 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.
- 1.3 This report seeks to provide the Audit and Governance Committee with a summary of the Redmond Review report, the recommendations made to the Government, along with the Government's response.
- 1.4 The findings and recommendations of the review were published on 8 September 2020 and the response of the Ministry of Housing, Communities and Local Government was published on the 17 December 2020. Whilst some recommendations have been agreed, others are being considered further with a full response to be made by spring 2021.
- 1.5 The full report and associated annexes are available on the Government's website: <https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-independent-review>.
- 1.6 The Government's response to the independent review can be found [here](#).

- 1.7 Appendix A to this report lists the recommendations made by the Redmond review and a summary of MHCLG's response.

2. RECOMMENDATIONS

- 2.1 That the Audit & Governance committee note the update on the Redmond Review.

3. SUMMARY

- 3.1 The Local Audit and Accountability Act 2014 (the 2014 Act) abolished the Audit Commission and introduced a new audit regime for local government to replace the previous arrangements.
- 3.2 In June 2019, The Secretary of State for Housing, Communities and Local Government asked Sir Tony Redmond to undertake an independent review of the effectiveness of local audit as now practised.
- 3.3 The purpose of the Review was to test not only the impact of external audit activity in local government but also to look, critically, at how this helps to demonstrate public accountability, particularly to service users and council taxpayers. The review also considered the issue of transparency in financial reporting and whether the annual accounts and associated published financial information can be readily understood by the public.
- 3.4 The framework for local audit encompasses its procurement, contract management and delivery, the Code of Audit Practice and Regulation and accountability for performance. All these aspects were examined in depth. Whilst the focus of the review was on local audit and public accountability there are several related factors which contributed to the shape and nature of the findings, including: the breadth and complexity of International Financial Reporting Standards (IFRS); the role of the sponsoring department (MHCLG); and the current state of the local audit market.
- 3.5 Attention was also directed towards the governance arrangements and the way in which audit reports are managed and reported. The focus was on the level of public awareness of audit findings. Current practices relating to the annual publication of financial information were also reviewed with an emphasis on the transparency, access and intelligibility of reports.
- 3.6 The findings of the Redmond Review fall into three main topics:
- Local audit arrangements
 - Governance arrangements
 - Financial reporting
- 3.7 The key elements of each are summarised below.

Local Audit Arrangements

- 3.8 Sir Tony Redmond's report concluded that the local audit market is very fragile and that the current fee structure does not enable auditors to fulfil the role in an entirely satisfactory way. With 40% of audits failing to meet the required deadline for report in 2018/19, there is a serious weakness in the ability of auditors to comply with their contractual obligations. The report therefore recommends that an increase in fees is considered and the 30 September deadline for audit completion reinstated, rather than 31 July.
- 3.9 The Government have accepted the recommendation to review the current fee structures in local audit, to provide greater flexibility to meet audit firms' costs. An additional £15m will be allocated to local authorities to help fund additional costs arising from the change in audit fees next year.
- 3.10 The Government has also recognised that next year will be particularly challenging as audit firms seek to catch-up after the significant Covid-19 related delays this year and trying to return to a 31 July deadline to audit the 2020/21 accounting period would be unrealistic. Hence, they have agreed in the moving of the audit deadline to 30 September for local authorities for the next two years and to keep this under review, but without committing to a permanent change.
- 3.11 The underlying feature of the existing framework is the absence of a body to coordinate all stages of the audit process. Consequently, the report made detailed proposals for a new regulatory body responsible for procurement, contract management, regulation, and oversight of local audit. The recommendation was that the proposed new body, 'The Office of Local Audit and Regulation' (OLAR) would take on 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);
 - Financial Reporting Council (FRC) or its planned replacement: Audit, Reporting and Governance Authority (ARGA);
 - The Comptroller and Auditor General (C&AG).
- 3.12 It was further recommended that the Regulator would be supported by a Liaison Committee comprising key stakeholders and chaired by the Ministry of Housing, Communities and Local Government (MHCLG) which would provide a facility for feedback and commentary of how the local audits are carried out. The OLAR could impose sanctions where there are significant issues in a local authority e.g. financial resilience issues where MHCLG are needed to intervene.

- 3.13 However, in its response, published on the 17 December 2020, the MHCLG said it is not currently persuaded that a new arms-length body is required. It added that unless there is an exceptional reason for a new body, the Government will look to explore new options. The response said: *“The creation of a strong system leader for local audit, especially in the form of a new body, would entail significant structural reform”*.

Governance Arrangements

- 3.14 The effectiveness of audit must, in part, be determined by the arrangements in place within each audited body for considering and acting upon external audit reports. All local authorities are required to set up Audit Committees or the equivalent with responsibility for considering the annual accounts and receiving internal and external audit plans and reports. The specific arrangements vary between different tiers of authorities. However, the purpose of an Audit Committee is to provide independent challenge on behalf of the authority in respect of accountability, governance, internal control and risk management arrangements.
- 3.15 Local authority accounts are complex and there appears to be a significant difference between the assurance that external auditors provide and public expectations. The Review questions whether Audit Committees understand the issues to question and challenge in an effective way. There are relatively low numbers of independent Audit Committee members (approximately 40% of Local Authority Audit Committees have independent members) and little communication between Audit Committee Members, external auditors and other inspectors and no formal exchange of views. The Report comments that there seems to be no real relationship between the Audit Committee and Full Council as very few reports go to Council.
- 3.16 The Report consequently recommends:
- 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;
 - formalising the facility for the CEO, Monitoring Officer and Chief Financial Officer (CFO) to meet with the Key Audit Partner at least annually;
 - that Key concerns relating to service and financial viability be shared between external auditors and inspectorates including Ofsted, Care Quality Commission and Her Majesty's Inspectorate of Constabulary and Fire & Rescue Services (HMICFRS) prior to completion of the external auditor's Annual Report.

- 3.17 In their response the Government agreed 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. The Government response noted that many local authorities feel existing reporting arrangements to audit committees are sufficient, however they felt 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.
- 3.18 The Government have agreed to work with key stakeholders such as CIPFA, the NAO and the LGA to ensure that, where appropriate, new guidance is issued which addresses the recommendations relating to meetings between chief officers and the external auditor and the appointment of an independent member(s) to audit committees. The Government responded that they will also work with the DHSC, the Department for Education, the Home Office and the NAO to support the sharing of key information between inspectorates and external auditors, and with CIPFA, the NAO and the LGA on strengthening engagement between external and internal audit.

Financial Reporting

- 3.19 The report concludes that current statutory accounts prepared by local authorities are impenetrable to the public. It is recommended that a simplified Statement of Service Information and Costs is prepared by each local authority 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. All means of communicating such information should be explored to achieve access to all communities.
- 3.20 The proposed new statement would be prepared in addition to the statutory accounts and would be audited to give it credibility. An example statement is contained in an annex to the Redmond Report. The Chartered Institute of Public Finance and Accountancy (CIPFA) and The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) are also recommended to review and simplify the current accounting requirements. For example, the technical accounting adjustments for Property, Plant & Equipment and Pension Fund issues.
- 3.21 The MHCLG has agreed with the need for a new standardised statement summarising council accounts and said it would work closely with CIPFA to consult on the content of this.

Implications flowing from the Redmond Review

3.22 The Review's recommendations and MHCLG's response to them are set out in detail in Appendix A. However, it should be noted that the Council is not considered a smaller authority for audit and accounts purposes, so recommendations in this area do not apply to this Council (recommendations 14, 15, 16 and 23) and have therefore not been included.

3.23 The recommendations are likely to directly impact the Council in the following ways:

- Increased external audit fees; (an additional £15m will be allocated to local authorities to help fund additional costs arising from the change in audit fees next year).
- an annual report being submitted to Full Council by the external auditor;
- The need to appoint an independent member onto the Audit Committee;
- The production of additional statutory financial information (although this may be offset by a removal of other disclosures following a review by the Local Authority Code Board); and,
- An extension to audit deadlines.
- Introduction of a governing body to manage, oversee and regulate
- A review of governance arrangements and accounting codes;
- Ensuring local auditors are provided with the requisite skills and training and statute be amended to ensure audit firms with these skills are not excluded from bidding from local authority work; and,
- That External Audit recognises that Internal Audit work in appropriate circumstances.

4. CONTRIBUTION TO STRATEGIC AIMS

4.1 The proposals contained in the report support the Council's Corporate Plan priority to remain financially sustainable to deliver its service priorities.

5. ENVIRONMENTAL AND CLIMATE IMPLICATIONS

5.1 None arising from this report.

6. COMMUNITY ENGAGEMENT AND INFORMATION

6.1 None arising from this report.

7. EQUALITY IMPACT ASSESSMENT

7.1 Not applicable

8. LEGAL IMPLICATIONS

8.1 At this stage, the report only sets out recommendations to the Government and has no legal standing. Some of the recommendations will require amendments to primary legislation if adopted.

8.2 The council will need to ensure it complies with any changes to the codes of practice and legislation as these arise.

9. FINANCIAL IMPLICATIONS

9.1 Whilst it is not clear how these recommendations may impact on audit fees, detail within the report highlights that four large firms have suggested increases of between 15% and 25% would be required.

9.2 The additional work recommended on reporting is not anticipated to require additional resourcing as it is expected this could be managed within existing resources.

9.3 It has been flagged that sourcing a professionally skilled individual to sit as an independent person on the Audit Committee may be difficult to source, and it is recognised that financial incentives may be required to attract suitable candidates.

9.4 It should be noted that representations were made by councils that extending audit deadlines may take resources away from budget setting and planning for future financial challenges, and if the recommendations are accepted careful planning for the timing of audit work will be required.

10. BACKGROUND PAPERS

10.1 Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting - Sir Tony Redmond. Published 20 September 2020

10.2 Local authority financial reporting and external audit: government response to the independent review. Published 17 December 2020

APPENDIX A: Summary of MHCLG’s response to the recommendations made by the Redmond Review

Action to support immediate market stability (recommendations 5, 6, 8, 10, 11)

	Recommendation	MHCLG Response
5.	All auditors engaged in local audit be provided with the requisite skills and training to audit a local authority irrespective of seniority.	Agree ; we will work with key stakeholders to deliver this recommendation
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.	Agree ; we will look to revise regulations to enable PSAA to set fees that better reflect the cost to audit firms of undertaking additional work
8.	Statute be revised so that audit firms with the requisite capacity, skills and experience are not excluded from bidding for local audit work.	Part agree ; we will work with the FRC and ICAEW to deliver this recommendation, including whether changes to statute are required
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.	Part agree ; we will look to extend the deadline to 30 September for publishing audited local authority accounts for two years, and then review
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.	Agree

Consideration of system leadership options (recommendations 1, 2, 3, 7, 13, 17)

	Recommendation	MHCLG Response
1.	<p>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:</p> <ul style="list-style-type: none"> - 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 - regulating the local audit sector 	<p>We are considering these recommendations further and will make a full response by spring 2021.</p>
2.	<p>The current roles and responsibilities relating to local audit discharged by the:</p> <ul style="list-style-type: none"> - Public Sector Audit Appointments (PSAA) - Institute of Chartered Accountants in England and Wales (ICAEW) - FRC/ARGA - The Comptroller and Auditor General (C&AG) <p>to be transferred to the OLAR</p>	<p>We are considering these recommendations further and will make a full response by spring 2021.</p>
3.	<p>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.</p>	<p>We are considering these recommendations further and will make a full response by spring 2021.</p>
7.	<p>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.</p>	<p>We are considering these recommendations further and will make a full response by spring 2021.</p>

13.	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.	We are considering these recommendations further and will make a full response by spring 2021.
17.	17. MHCLG reviews its current framework for seeking assurance that financial sustainability in each local authority in England is maintained.	We are considering these recommendations further and will make a full response by spring 2021.

Enhancing the functioning of local audit, and the governance for responding to its findings (recommendations 4, 9, 12, 18)

4.	<p>The governance arrangements within local authorities be reviewed by local councils with the purpose of:</p> <ul style="list-style-type: none"> - 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 - formalising the facility for the CEO, Monitoring Officer - Chief Financial Officer (CFO) to meet with the Key Audit Partner at least annually. 	Agree; we will work with the LGA, NAO and CIPFA to deliver this recommendation
9.	External Audit recognises that Internal Audit work can be a key support in appropriate circumstances where consistent with the Code of Audit Practice.	Agree; we will work with the NAO and CIPFA to deliver this recommendation
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.	Agree; we will work with the LGA, NAO and CIPFA and other key stakeholders to deliver this recommendation, including whether changes to statute are required

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.	Agree; we will work with other departments and the NAO to deliver this recommendation
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Improving transparency of local authorities' accounts to the public (recommendations 19, 20, 21, 22)

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.	Agree; we will look to CIPFA to develop a product through consultation with local government. We will work with CIPFA to deliver this recommendation
20.	The standardised statement should be subject to external audit	Agree; we will work with CIPFA, the LGA and the NAO to deliver this recommendation
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.	Agree; we will work with the LGA and CIPFA to deliver this recommendation
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.	Agree; we will look to CIPFA to deliver this recommendation