



**Open Report on behalf of Andrew Crookham, Executive Director - Resources**

Report to:	<b>Audit Committee</b>
Date:	<b>19 March 2021</b>
Subject:	<b>External Audit Quality</b>

**Summary:**

This report considers two recent reviews into the external audit of local authority accounts and reports on their key findings.

**Actions Required:**

The Executive Director - Resources recommends that the Audit Committee:

1. Notes the contents of this report.

## **1. Background**

- 1.1 The quality of the work carried out by audit firms of the accounts of public bodies is seen as essential to providing local taxpayers and the wider public with an impartial and independent view of their financial statements and their arrangements for securing value for money (VfM).
- 1.2 The external audit of statutory accounts has been under the spotlight recently with a number of independent reviews\* of audit having taken place.
- 1.3 This report focuses on the findings of the two of these reviews: the Redmond Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting, as well as the Financial Reporting Council Report on Audit Quality Inspection.

### **The Redmond Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting**

- 1.4 The review was commissioned by the government to consider the effectiveness of the legal framework for local audits that was introduced by the Local Audit and Accountability Act 2014.
- 1.5 The Redmond review was led by Sir Tony Redmond, and his consultation was first published in September 2019. Interested parties were invited to

respond to the consultation, which consisted of 43 questions covering areas such as: audit and wider assurance; the governance framework; audit product and quality; the financial reporting framework. Lincolnshire County Council provided a response to this consultation.

1.6 After considering the consultation responses, Sir Tony Redmond published the results of his review in September 2020 and made 23 recommendations. These were grouped under four headings:

- External Audit Regulation
- Smaller Authorities Audit Regulation
- Financial Resilience of Local Authorities
- Transparency of Local Reporting.

1.7 The key recommendations relating to external audit quality were that:

- A new body be created to manage, oversee and regulate local audit to replace the current arrangements;
- All auditors engaged in local audit be provided with the requisite skills and training;
- The current fee structure be revised to ensure that adequate resources can be deployed, and to ensure the stability of the local audit market;
- Internal audit work can be used as a key support to external audit work where appropriate;
- The deadline for publishing audited accounts be revisited with a view to extending it from 31 July to 30 September.

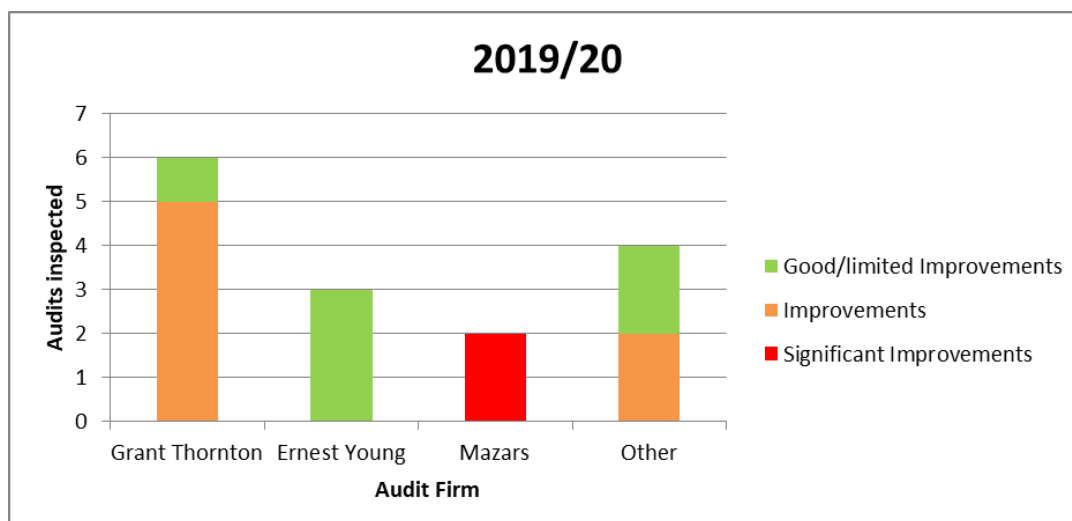
1.8 The government responded to the Redmond review in December 2020. It accepted the recommendation that audit fees be increased, and pledged £15m of additional funding in 2021/22 to cover this. It also accepted the recommendation that the deadline for publication of audited accounts be extended as it would help to mitigate some of the issues reported, however the government's view was that the extension should be for two years only, and should then be reviewed. The government committed to working with accounting bodies and the Financial Reporting Council to consider how the uptake of local audit training can be improved, and agreed to work with the relevant bodies on strengthening engagement between external and internal audit.

1.9 The main area where the government did not support Sir Tony Redmond's recommendations was in the creation of a new body to oversee local audit. The government would prefer to explore other options as it is not of the view that a new arm's length body is required.

- 1.10 Following the publication of its response to the Redmond review, the government made the first moves towards implementing the recommendations it supported. Firstly it published a consultation on the proposed audit fee scale (a summary of the detail of this is shown at Appendix A), and then a consultation on extending the deadlines for publishing draft accounts for inspection (from 31 May to 1 August) and audited accounts (from 31 July to 30 September) for the financial years 2020/21 and 2021/22 only.
- 1.11 There were other recommendations arising from the Redmond review which may be of interest to the Audit Committee. These were all supported by government and are likely to be implemented in due course:
- That an annual report be submitted to full Council by the external auditor.
  - That consideration is given to the appointment of at least one independent member, suitably qualified, to the Audit Committee.
  - That a standardised statement of service information and costs, which compares the financial position to the approved budget, be prepared and presented alongside the accounts.

### **The Financial Reporting Council Report on Audit Quality Inspection**

- 1.12 In October 2020, the Financial Reporting Council (FRC) published their findings into the quality of major local audits in England. The FRC reviewed 15 audits across the seven largest audit firms and covered the Financial Statements opinions and Value for Money conclusions.
- 1.13 The inspection was conducted between December 2019 and September 2020 and covered health bodies, other bodies and local Government authorities. The report focused on key areas requiring action across the firms to safeguard and enhance audit quality, such as property valuations, multi-employer pension deficits, occurrence and completeness of expenditure, first year audit procedures, impairment of receivables and the fraud risk assessment.
- 1.14 The quality of VfM conclusion work across all the firms has continued to improve and all audits reviewed require no more than limited improvements. The report noted that this is a pleasing aspect to the audit firms' work as they are providing high quality assurance to stakeholders around the VfM conclusions.
- 1.15 When inspecting Financial Statements audits it was found that nine of the 15 audits reviewed required improvement, which the FRC deemed as unacceptable. Urgent action is required by some of the firms to ensure swift resolutions are put in place.
- 1.16 Two firms are not consistently achieving the necessary level of audit quality and therefore need to make significant improvement. The FRC has advised these firms to produce a detailed Root Cause Analysis of the issues identified and put in place an audit quality action plan across local audits.



1.17 Mazars is one of the firms that was considered as requiring significant improvement following a trend of poor inspection results. Key areas of focus included the audit of property valuations, group audit oversight, the sufficiency of audit testing over income and receivables and expenditure, and Engagement Quality Control review procedures.

1.18 In response to these findings, Mazars has acted in putting plans in place to improve the quality of their local audit work which also incorporates the emerging changes from the updated National Audit Office Code of Practice. The firm's full response to the FRC's findings can be seen in Appendix B.

1.19 The quality of audit work over property valuations continues to be the biggest area for concern as the FRC. In response to this result, Mazars have mandated their use of a sector-specific audit testing programme for 2020/21 audits onwards.

\* In addition to the two reviews considered in this report, in 2018 Sir John Kingman carried out the Independent Review of the Financial Reporting Council, and the government's Committee of Public Accounts published a report on Auditing Local Government in 2019.

## 2. Conclusion

2.1 This report shows that the two reviews covered have led to a number of recommendations which have been welcomed, and the majority of these recommendations are being either consulted or implemented. This should lead to an improvement in the quality of local audits.

### 3. Consultation

**a) Have Risks and Impact Analysis been carried out?**

No

**b) Risks and Impact Analysis**

N/A

### 4. Appendices

These are listed below and attached at the back of the report	
Appendix A	Public Sector Audit Appointments Ltd Consultation on Audit Fee Scale 2021/22
Appendix B	Mazars' Response to the Financial Reporting Council Report
Link to the Redmond review	<a href="https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-independent-review">https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-independent-review</a>
Link to the FRC report	<a href="https://www.frc.org.uk/news/october-2020/frc-publishes-major-local-audit-inspection-results">https://www.frc.org.uk/news/october-2020/frc-publishes-major-local-audit-inspection-results</a>

### 5. Background Papers

No Background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

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