

**Audit and Risk Committee 21<sup>st</sup> July 2021**

**Report of Leicestershire County Council's Head of Internal  
Audit & Assurance Service**

**Further update on developments in local (external) audit  
arrangements**

**PURPOSE OF REPORT**

1. The purpose of this report is to provide the Audit and Risk Committee (the Committee) with a further update on developments in local (external) audit arrangements, that are associated with the Committee's responsibilities.

**RECOMMENDATIONS**

2. This report is for information only

**SUMMARY**

3. The Committee has previously received three reports following the Ministry of Housing Communities and Local Government's (MHCLG) requirement for an independent review (led by Sir Tony Redmond) of the effectiveness of local (external) audit and the transparency of local authority financial reporting.
4. The first report on 25<sup>th</sup> November 2019 explained there was a formal call for views and that the Council's Director of Finance would respond.
5. At its meeting on 24<sup>th</sup> November 2020, the Committee received a further report and a short presentation summarising the Redmond review's key findings, outlining its 23 recommendations, how the report was being taken forward and communicated to stakeholders and what the next steps were, including awaiting a formal response from MHCLG which had commissioned the review.
6. At its meeting on 17<sup>th</sup> March 2021, the Committee was informed that the MHCLG had formally responded (December 2020) to the review report. The response was mostly positive and the MHCLG agreed to work with a wide range of key stakeholders to deliver the review's recommendations. However, a key area of disagreement was the recommendation to develop and implement a new body, the Office of Local Audit and Regulation (OLAR), to be created to provide systems leadership and manage, oversee, and regulate local audit. This was rejected primarily because creating a new body would

have required new legislation from central government. Nevertheless, MHCLG recognised certain areas needed to be addressed so it proposed further engagement in the Spring.

## **REPORT**

### **Redmond review into local (external) audit – Spring update report**

7. On 19<sup>th</sup> May 2021, the MHCLG wrote to all local authority Chief Executives informing that it had published its update report that was promised in its December 2020 response. The full report is found here: -  
  
<https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-spring-update/local-authority-financial-reporting-and-external-audit-spring-update>
8. The report provided an update on the MHCLG's progress with implementing the Government's response to the Redmond review, including on the delivery of measures to support immediate market stability and towards implementation of the other recommendations.
9. It set out the Government's views on systems leadership for local audit. The Government agrees that a clearly accountable system leader with overarching responsibility is needed to make sure the local audit framework operates in a coherent and joined up manner, however it does not believe a new arm's length body is needed to achieve this. The Government's view is that the new Audit, Reporting and Governance Authority (ARGA), being established to replace the Financial Reporting Council (FRC), as part of the Department for Business, Energy & Industrial Strategy (BEIS) broader corporate audit reforms, would be best placed to take on this role. The FRC already undertakes the core functions relating to the audit quality framework necessary for a single responsible body to have. Establishing ARGA as system leader for the local audit framework would also ensure alignment with, and harness the positive impact of, the broader audit reforms.
10. To ensure the new regulator acquires the necessary focus and expertise on local audit, a standalone unit will be established within ARGA. Development and maintenance of The Code of Audit Practice will transfer from the National Audit Office to ARGA, however the latest Code (introduced in 2020), which includes the new Value for Money commentary, will be retained. ARGA will not conduct procurement or contract management as this could create a conflict of interest. Therefore, the new arrangements will encompass a separate appointing body. MHCLG confirmed that Public Sector Audit Appointments Ltd (PSAA) will continue as the appointing body for local audit, in charge of procurement and contract management for local government external auditors, with commercial support from MHCLG for the next procurement.
11. As the proposed reforms to the local audit framework will take time, MHCLG will take an increased leadership role in the interim, including setting up and chairing a Liaison Committee of key stakeholders, that will oversee the

governance of the new audit arrangements and ensure they are operating effectively, which Redmond recommended be created.

12. The Government intends to launch a public consultation on the proposals ahead of summer recess.
13. Two further MHCLG consultations recently occurred: -
  - a. A consultation proposing changes to the fee setting and fee variation arrangements set out in the Local Audit (Appointing Person) Regulations 2015 to provide additional flexibility to the appointing person for principal bodies (PSAA) to reflect the changing nature of the local audit market, closed on 1<sup>st</sup> June.
  - b. A consultation seeking views on the most appropriate methodology for allocating £15 million additional funds to assist councils to meet the rise in audit fees and new burdens resulting from the implementation of additional requirements closed on 18<sup>th</sup> May.
14. The Government's proposals on local audit have gained a qualified welcome from stakeholders although concerns around audit supply and market instability remain. Additionally there are questions around: -
  - a. Will the standalone unit within ARGA have the specialist skills and capacity it needs?
  - b. To what extent will the standalone unit be able to tailor ARGAs corporate approach to the application of International Auditing Standards, to local authority audits?
  - c. Will the PSAA succeed in securing audit contracts that are both competitively priced and enable audit suppliers to deliver audits that local authorities and the public deserve?

### **Local (external) audit arrangements from 2023 and beyond**

15. Within its Terms of Reference under the section 'External Audit', the Committee has a responsibility, 'To consider, comment upon and note the arrangements chosen by the Council to select and appoint its statutory external auditor'.
16. During Autumn 2021 all local government and police bodies will need to make important decisions about their external audit arrangements for the period commencing from the financial year 2023/24. In relation to appointing auditors local bodies have options to arrange their own procurement and make the appointment themselves or in conjunction with other bodies, or they can join and take advantage of the national collective scheme administered by Public Sector Audit Appointments Limited (PSAA).
17. On 10<sup>th</sup> June PSAA launched its draft prospectus for 2023 and beyond which provides an introduction to the PSAA national scheme and invites views and comments from local bodies and other interested parties in relation to the aims of the scheme and how it needs to develop going forward. Details can be found at: -

<https://www.psa.co.uk/about-us/appointing-person-information/appointing-period-2023-24-2027-28/prospectus-2023-and-beyond/draft-prospectus-for-2023-and-beyond/page/7/>

18. The prospectus explains in some detail how the audit market quickly destabilised starting in 2018 when a series of financial crises and failures in the private sector gave rise to questioning about the role of auditors and the focus and value of their work. In rapid succession there has been the results of four independent reviews commissioned by Government including Redmond's review of local authority financial reporting and external audit. Much of this has been explained to the Committee in previous reports.
19. It is PSAA's view that the audit market will continue to be relatively unstable and difficult to predict for a further period of time as the Government continues to develop and implement its policy response to the four independent reviews; as further regulatory pressure is applied; and as firms respond and adapt. It considers that local government audit will not be immune from these difficulties.
20. The prospectus includes plans to adjust the procurement ratio between quality and costs from an equal 50:50 to 80:20 (i.e. the focus of appointing external auditors will be clearly on quality, not cost). This change in approach would be supported by key performance indicators on audit approach, quality assurance arrangements, resourcing, capacity and capability. There is some nervousness in the local government sector about this proposal, in that whilst quality is clearly important, costs must not get out of hand.
21. Consultation on the prospectus closes on 8<sup>th</sup> July.

### **Timetable for decisions**

22. A further report will be brought to the Committee once the consultations are concluded.

## **FINANCIAL, LEGAL AND OTHER IMPLICATIONS**

### **Financial Implications**

23. None directly, but the Audit and Risk Committee is a key component of the Council's governance framework. It provides those charged with governance independent assurance on the on the adequacy and integrity of the financial reporting and governance processes. By monitoring the quality and effectiveness of both external and internal audit, it makes an important contribution to ensuring that effective assurance arrangements are in place.  
*Colin Sharpe, Deputy Director of Finance, ext. 37 4081*

### **Legal Implications**

24. The Council may need to implement any further statutory requirements arising from the post implementation review of the audit framework and financial reporting elements of the Local Audit and Accountability Act 2014. *Kamal Adatia, City Barrister & Head of Standards, x37 1401*

**Other Implications**

OTHER IMPLICATIONS	YES/NO	Paragraph references within supporting information
Equal Opportunities	No	
Policy	No	
Sustainable and Environmental	No	
Climate Change	No	
Crime and Disorder	No	
Human Rights Act	No	
Elderly/People on Low Income	No	
Corporate Parenting	No	
Health Inequalities	No	
Risk Management	No	

8. BACKGROUND PAPERS – LOCAL GOVERNMENT ACT 1972

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