

PUBLIC INTEREST

The recent publication of a review into the quality of local government audit by **Sir Tony Redmond** reveals a lack of understanding of the local authority framework and **highlights “lost” areas**. Can internal audit help to transform the form and focus of public sector audit?

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Most people view professional, independent and objective external audit as a key element of governance and management in local government. However, increasing concerns that current provisions are inadequate, and of a widening expectations gap, prompted the government to set up an independent review under Sir Tony Redmond, a past president of CIPFA. This was recently published and revealed fundamental issues and a lack of coherence and accountability in the existing auditing system, although there was a surprising amount of consensus about what needs to be done among the 150 key stakeholders, who included audit companies, audit stakeholders and local authorities.

Redmond's is the latest in a series

of reviews of audit arrangements, that includes those of Sir John Kingman on the Financial Reporting Council (2018), RAND Europe on assessing the impact of changes to the local audit regime (2018), the Competition and Markets Authority on the statutory audit market (2019) and Sir Donald Brydon on the quality and effectiveness of private sector audit (2019). It responds to widespread and growing concerns about the arrangements for public audit, the implementation of the Local Audit and Accountability Act 2014, and the public assurance regime for local authorities in general.

The scope and conduct of local audit

Redmond's survey reveals a widespread lack of understanding





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among external auditors of the local authority regulatory framework and highlights key areas that currently fall outside the scope of local audit, including some of the riskier and expanding areas of local authority activities, such as new commercial and hybrid organisations. It also tackles the financial resilience and sustainability of local authorities. These have contributed to an expectations gap, which has been accentuated by the coronavirus pandemic.

The review also noted increasing concerns about the sector-specific knowledge of external auditors working on local authority audits. It highlights that reductions in the fees paid by the local authorities in recent years mean that audit firms devote less time to these audits. It suggests that external audit fees are at least 25 per cent too low to meet local audit requirements, and the relatively low contribution of local authority audit to audit firms' profits deters external auditors from specialising in this area. This may explain why audit firms find it hard to attract and retain high quality staff specialising in local authority audit.

Oversight and coordination

Since the demise of the Audit Commission there has been no single regulatory authority responsible for the oversight and co-ordination of public audit. Redmond proposes establishing an Office of Local Audit and Regulation (OLAR) to oversee a new quality regime as well as increasing audit fees.

He is also concerned about the relationship



between internal and external auditors and their engagement with each other at local audit level. This reflects a similar concern in the updated Code of Audit Practice published by the National Audit Office this year: "The [external] auditor should build effective coordination arrangements with internal audit, using the work of internal audit where, in the auditor's judgment and in line with professional standards, this is appropriate."

Redmond argues that internal audit work can be a key support in appropriate circumstances, where this is consistent with the Code of Audit Practice. For example, he suggests that external auditors could make more use of the knowledge and expertise of internal audit to develop their understanding of the local authority. This could make internal audit a "rich source of knowledge, should the external audit team wish to use it".

However, there were also questions about the extent to which external auditors could utilise internal auditors' work, as some external audit firms reported concerns about wide variations in the quality of internal audit work. This suggests that it is important to create, maintain and, in some cases, strengthen positive and mutually helpful relationships between internal and external audit – although this cannot compromise the independence of external audit arrangements.

All key stakeholders said it is essential that both internal and external auditors engaged in local authority audit work should have the requisite skills, training and expertise, and should be held to

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account for their performance by the new regulator. This would strengthen the assurance framework, drive more efficient and effective governance of the local authority, and improve value for money.

Public reporting

Redmond raises serious concerns about the transparency and accountability of local authority accounts to taxpayers and service users. Local authority audit is longer, more complex, and more technical than central government or private sector audit. The accounts are often impossible to understand without technical knowledge and have elements that are counterproductive or redundant. The “going concern” opinion is meaningless in the local government context, according to 87 per cent of respondents, and external auditors spend too much time on fixed assets and pension valuations instead of focusing on major areas of expenditure and non-ringfenced revenue reserves.

Redmond proposes a short, simplified user-friendly financial statement that would be presented alongside the IFRS accounts – and he provides a suggested format. This would strengthen financial transparency and accountability to taxpayers and service users without imposing a significant burden on local authorities. He suggests this would obviate the

need to report, for example, the Expenditure and Funding Analysis, the Movement in Reserves Statement, and supplementary disclosures.

Another change would be a new deadline for publishing audited local authority accounts. Draft accounts should normally be submitted for audit by 31 May, with conclusion of the external audit by 31 July. This timetable puts pressure on staff in the summer, is widely considered unrealistic and, increasingly, is being missed. Redmond proposes a revised deadline of 30 September.

If carried out, the consequences of Redmond’s review could (and should) be a radical transformation of the focus of local audit, the reports that internal and external auditors are required to produce and the objectives that guide and underpin their work. Some of the changes will require primary legislation which will take time. However, the fundamental importance of audit to effective government and the universal view that the current system does not meet anybody’s interests suggest that the changes will not be long in coming. ■

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