

AUDIT COMMITTEE

Financial Reporting Council Major Local Audits – Audit Quality Local Inspection 25 November 2020

Report of Chief Finance Officer

PURPOSE OF REPORT

This report seeks to provide Members with information on the recently released Financial Reporting Council (FRC) Major Local Audits – Audit Quality Local Inspection report.

This report is public.

RECOMMENDATIONS

The Audit Committee is recommended

(1) **To note the report**

1.0 INTRODUCTION

1.1 The Financial Reporting Council (FRC) is the independent body responsible for monitoring the quality of Major Local Audits, as defined by the Local Audit (Professional Qualification and Major Local Audit) Regulations 2014.

1.2 The reviews are performed by the FRC's Audit Quality Review (AQR) team contributes to safeguarding and promoting improvement in the overall quality of Local Audit auditing in the UK.

2.0 BACKGROUND

2.1 The report sets out the principal findings arising from the 2019/20 inspection of the audit firms completing major local audits in England carried out by AQR. An audit qualifies as "major" if the Authority has total income or expenditure of more than £500M.

2.2 The report is based on a total of 12 reviews of 2018/19 audits across the whole of local government and three from the NHS, covering each of the appointed audit firms. The sample size is low, but the reviews did cover the firms' overall policies and procedures as they applied at each audit.

2.3 Currently there are seven audit firms contracted to undertake such audits and these are listed below with the corresponding number of reviews undertaken reflecting market share.

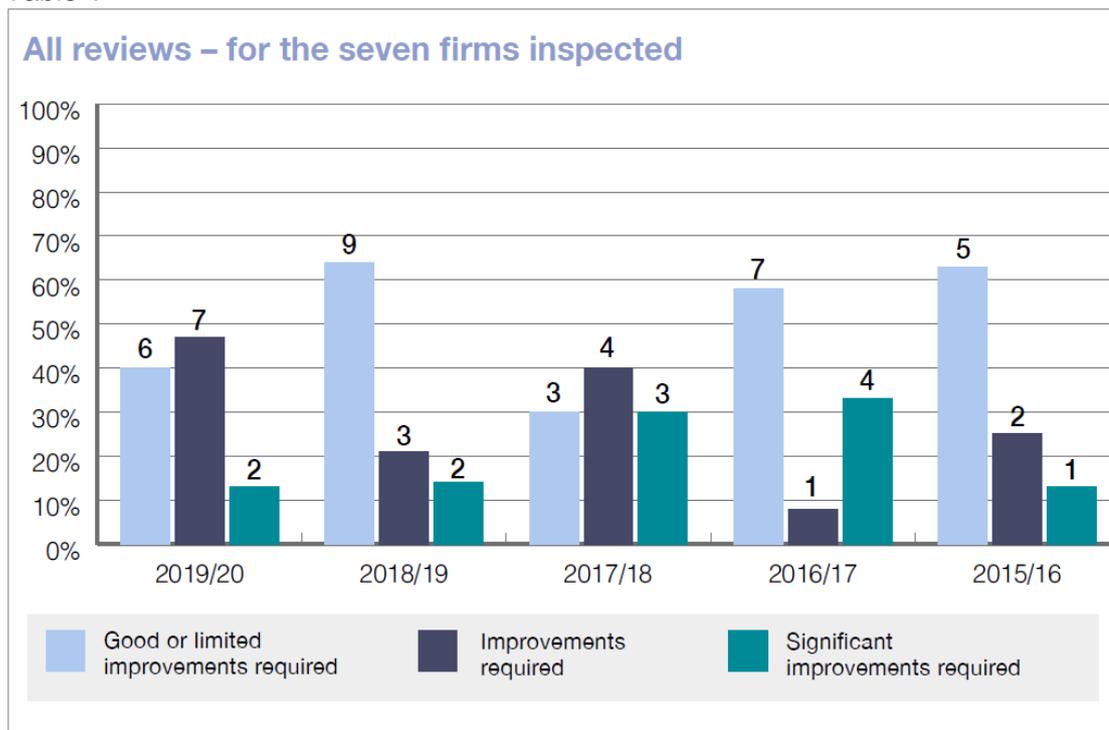
Audit Firms	Number of		Reviewed by
	Local Major	Market Share	
	Audits		AQR
Grant Thornton UK LLP	109	40.2%	6
Ernst & Young LLP	72	26.6%	3
Mazars LLP	42	15.5%	2
KPMG LLP	25	9.2%	1
BDO LLP	12	4.4%	1
Deloitte LLP	10	3.7%	1
PwC LLP	1	0.4%	1
	271	100%	15

3.0 SUMMARY OF FINDINGS

Financial Statements Audit

3.1 Only six of the 15 reviews concluded that the audit was good or required limited improvement with nine failing to reach an acceptable level.

Table 1



3.2 Grant Thornton and Mazars were identified for particular criticism and must now perform a Root Cause Analysis of the issues identified and put in place an audit quality action plan.

3.3 The key areas for attention in the financial statements audit were:

- Valuation of property (including investment property)
- Multi-employer pension deficits
- Occurrence and completeness of expenditure
- First year audit procedures
- The impairment of receivables
- The fraud risk assessment and responses.

3.4 Some of the key findings within the report are:

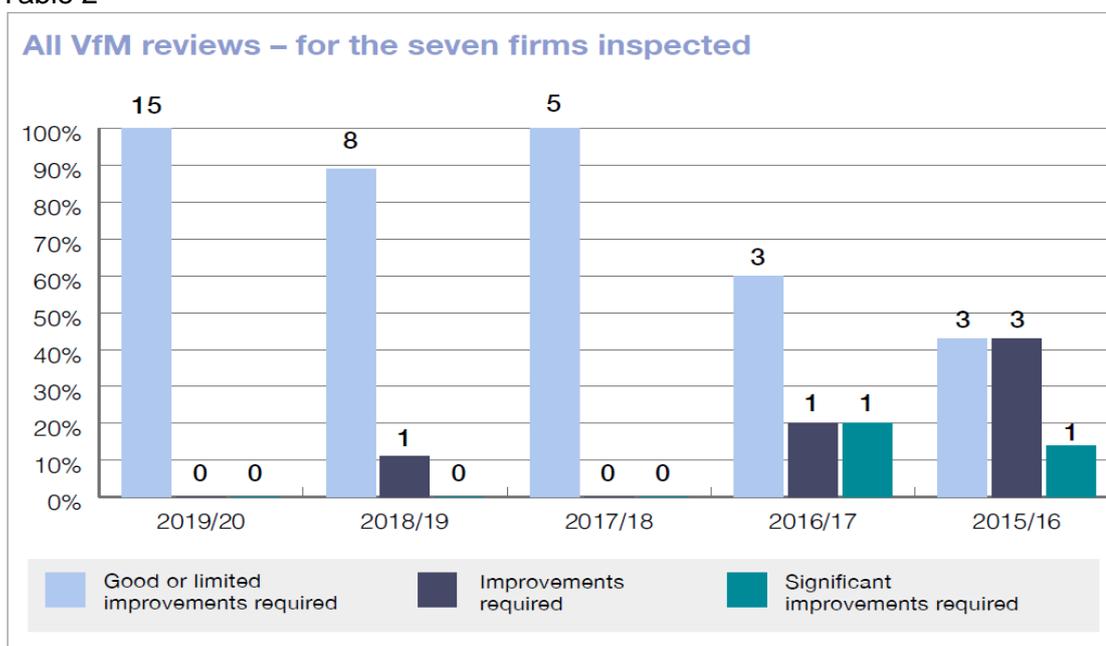
- Significantly strengthen audit procedures and challenge of management and their own valuation experts in the testing of property revalued in the year.
- Improve the level of evidence obtained over amounts receivable, particularly sample sizes and the assumptions used to value expected credit losses for financial receivables.
- Strengthen the audit response to the risk of fraud arising from management override of controls, particularly in relation to journal entry testing.
- Improve consideration of the risk of fraud in expenditure recognition and the extent of testing around the completeness and occurrence of expenditure.
- Design and execute appropriate audit procedures to assess the estimates used to determine liability provisions.
- Enhance the procedures over defined benefit pension arrangements, with improvements in the sufficiency of audit work performed over pension fund assets.
- Improve the evidence of judgements taken in the exercise of special reporting powers (statutory recommendation and public interest reports).

3.5 As the audit of the 2019/20 Financial Statements is currently underway, we expect challenge in these areas.

Value for Money (VFM)

3.6 Work on the VFM conclusion was graded good or requiring limited improvement at all 15 audits.

Table 2



- 3.7 Members will recall from the meeting 19 February 2020 that all audit firms will need to comply with the new National Audit Office (NAO) Code of Practice, which will be applicable for the 2020/21 Financial Statements. The new Code of Practice has changed the scope and auditors' work on VfM arrangements. AQR will continue to monitor VfM arrangements for one further inspection review before monitoring the audit of VfM arrangements under the new Code.
- 3.8 The FRC also undertake thematic inspections to supplement their annual process. Recent reviews have included the use of audit quality indicators, the use of technology in the audit, culture, and materiality. A copy of the Major Audits report is attached at Appendix A with further information on the thematic reviews and individual firms available on the FRC's website <https://www.frc.org.uk/auditors/audit-quality-review>

4.0 OPTIONS AND OPTIONS ANALYSIS

- 4.1 Not applicable – The report is for noting and so no decision is required

5.0 CONCLUSION

- 5.1 High quality audit is essential to maintain confidence by providing an independent, impartial view of the Council's financial statements and arrangements in place to secure value for money. Poor auditing may fail to alert management, the public and other stakeholders to material misstatements (including those arising from fraud) or financial control weaknesses, in those cases where management have not identified or appropriately amended them.

<p>CONCLUSION OF IMPACT ASSESSMENT (including Health & Safety, Equality & Diversity, Human Rights, Community Safety, Sustainability and Rural Proofing):</p>

<p>No implications directly arising.</p>
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<p>LEGAL IMPLICATIONS</p>

<p>There are no direct legal implications arising from this report</p>
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<p>FINANCIAL IMPLICATIONS</p>

<p>There are no direct financial implications arising from this report</p>
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<p>OTHER RESOURCE IMPLICATIONS, such as Human Resources, Information Services, Property, Open Spaces</p>

<p>No implications directly arising.</p>
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<p>SECTION 151 OFFICER'S COMMENTS</p>
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<p>The s151 Officer has authored this report in his capacity as Chief Finance Officer</p>

MONITORING OFFICER'S COMMENTS		
The Monitoring Officer has been consulted and has no further comments		
<table border="1"><tr><td>BACKGROUND PAPERS</td><td>Contact Officer: Paul Thompson Telephone: 01524 582603 Email: pthompson@lancaster.gov.uk Ref:</td></tr></table>	BACKGROUND PAPERS	Contact Officer: Paul Thompson Telephone: 01524 582603 Email: pthompson@lancaster.gov.uk Ref:
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