

Divisions Affected - All

AUDIT & GOVERNANCE COMMITTEE

18 September 2024

Reforms to clear the backlog in local audit

Report by the Executive Director of Resources and Section 151 Officer

RECOMMENDATION

1. The Committee is **RECOMMENDED** to
 - (a) Note the update on the arrangements that the government intends to put in place to address the local audit backlog in England.
 - (b) Note the approach that EY LLP intend to take to the audit and reporting on the council's accounts for 2022/23 onwards.

Executive Summary

2. This report sets out an update on measures being put in place by the government to address the local audit backlog in England and what that will mean locally.

Addressing the local audit backlog in England

3. In early February 2024 DLUHC issued a [consultation](#) with the aim of clearing the backlog of local audits in England. The consultation sought views on amending the Accounts and Audit Regulations 2015 as part of a package of cross-system measures to clear the backlog and put the system on a sustainable footing for the future.
4. On 30 July 2024 the Minister of State responsible for Local Government and English Devolution made [a statement to parliament](#) setting out the Government's policy proposal for addressing the local government audit backlog.
5. This statement outlines immediate actions the Government – together with the Financial Reporting Council (FRC), the National Audit Office (NAO) and organisations in the wider system – is taking, which are designed to address the backlog and put local audit on a sustainable footing.

6. Following the statement a cross system letter set out that secondary legislation will be put in place to amend the Accounts and Audit Regulations (2015) to set a series of backstop dates.
7. The first backstop date would clear the backlog of unaudited accounts up to and including 2022/23. Where auditors have been unable to complete audits, they will issue a 'disclaimed' or 'modified' audit opinion. Auditors are likely to issue hundreds of 'disclaimed' audit opinions and disclaimed opinions will likely continue for some bodies for a number of years.
8. The proposed legislation will include five further backstop dates up to and including financial year 2027/28 to allow full assurance to be rebuilt over several audit cycles. It is the aspiration of the Government and key local audit system partners that, in the public interest, local audit recovers as early in this five-year period as possible. This means disclaimed opinions driven by backstop dates should, in most cases, be limited to the next two years (up to and including the 2024/25 backstop date of 27 February 2026), with only a small number of exceptional cases, due to specific individual circumstances, continuing thereafter. The proposed backstop dates are:
 - Financial years up-to-and-including 2022/23: 13 December 2024
 - Financial year 2023/24: 28 February 2025
 - Financial year 2024/25: 27 February 2026
 - Financial year 2025/26: 31 January 2027
 - Financial year 2026/27: 30 November 2027
 - Financial year 2027/28: 30 November 2028
9. While there will be modified and disclaimed opinions, auditors' other statutory duties – including to report on Value for Money (VfM) arrangements, to make statutory recommendations and issue Public Interest Reports – remain a high priority.
10. For financial years 2024/25 to 2027/28, the date by which Category 1 bodies should publish 'draft' (unaudited) accounts will change from 31 May to 30 June following the financial year to which they relate. This will give those preparing accounts more time to ensure they are high-quality accounts. This in turn will benefit auditors while still ensuring publication shortly after financial year end.
11. The proposed legislation will outline the following scenarios in which bodies may be exempt: where auditors are considering a material objection; where recourse to the court could be required; or from 2023/24, where the auditor is not yet satisfied with the body's Value for Money arrangements. Where such an exemption exists, the legislation would include a requirement to publish the audit opinion as soon as practicable. For transparency, if a body is exempt, they would be required to publish an explanation of their exemption at the time of a backstop date.
12. Bodies that are non-exempt but have failed to comply with a backstop date will be required to publish an explanation, to send a copy of this to the Secretary

of State (to facilitate scrutiny) and publish audited accounts as soon as practicable.

13. The Government also intends to publish a list of bodies and auditors that do not meet the proposed backstop dates, which will make clear where 'draft' (unaudited) accounts have also not been published.

Communications to support local bodies and auditors

14. The statement by the government sets out that there will be extensive communications and engagement on these measures, to make clear the necessity of these steps and emphasise the context for modified or disclaimed opinions.
15. Local bodies should not be unfairly judged based on disclaimed or modified opinions, caused by the introduction of backstop dates that are largely beyond their control. Auditors will be expected to provide clear reasons for the issuing of such opinions to mitigate the potential reputational risk that local bodies may face.
16. Guidance for auditors would be published by the Comptroller and Auditor General and endorsed by the FRC, confirming that there are no contradictions to the requirements or the objectives of International Auditing Standards (UK). A proportionate approach is required and all system partners including the FRC, NAO and auditors, are aware that this is the Government's objective. The FRC's and ICAEW's regulatory activity would consider auditors' adherence to the Code and whether proper regard has been given to the statutory guidance.

Approach by EY LLP

17. In line with the timelines set out nationally EY LLP have confirmed that their intention is to prioritise their resources to:
 - Finalise value for money reporting up to 2022/23 and complete the process of disclaiming audit opinions up to 2022/23 by end of November 2024;
 - Ensure that other priority sectors are protected, including resources for the commencement and planning of 2024/25 local government audits;
 - Deliver 2023/24 audits including continued focus on pension fund audits, where practical, ensuring the value for money responsibilities placed on auditors are completed; and
 - Complete the process of disclaiming audit opinions for 2023/24 by the end of January 2025, to then allow audit teams to begin planning 2024/25 audits with a view to commencing the build back of assurance.
18. Audit of the Statement of Accounts for 2023/24
In respect of the delivery of 2023/24 audits, they are prioritising those audits that they consider meet the following criteria:

- draft unaudited financial statements were published by 31 July 2024;
 - there is evidence that finance teams can effectively and efficiently support the audit process; and
 - have high-quality audit evidence and supporting information that is delivered in accordance with our agreed timetable and in advance of the commencement of the audit.
19. Following publication of the council's Statement of Accounts for 2023/24 at the end of June 2024 the audit of the accounts began in early August and is expected to continue through the autumn with a disclaimed opinion shared in December 2024.
- Audit of the Statement of Accounts for 2022/23
20. While EY LLP will not complete detailed testing of the financial statements for 2022/23 they have requested updates on key areas to be returned by 16 September 2024 to ensure that they are sighted on developments and to form a view on aspects that they report on.
21. That means that in addition to the report including the disclaimed opinion for 2022/23 they will issue a completion report that includes: details of the work undertaken for planning; the results from the work completed for this process; and their value for money commentary. The expectation is that they disclaimed opinion and completion report will be shared with Audit & Governance Committee on 27 November 2024 ahead of the backstop date of 13 December 2024

Financial Implications

22. There are no financial implications arising directly from the report. However, the Council is required to pay its external auditor for conducting the audit of the Statement of Accounts each year.
23. Issuing a disclaimed or modified audit opinion and a subsequent return to being able to fully complete audits will require differing levels of work by auditors. Public Sector Audit Appointments Ltd (PSAA) will set scale fees and determine fee variations where the auditor undertakes substantially more or less work than assumed by the scale fee and will consult with bodies where appropriate. In doing so PSAA will apply the following principles: if auditors have worked in good faith to meet the requirements of the Code of Audit Practice in place at the time the work was conducted (and have reported on work that is no longer required), then they are due the appropriate fee for the work done, and the body is due to pay the applicable fee, including where there is a modified or disclaimed opinion. Conversely, if an auditor has collected audit fees in part or in full, and the backstop date means that the total work done represents less than the fee already collected, then the auditor must return the balance and refund the body the appropriate amount – this ensures that the bodies pay only for work that has been done and reported.

Comments checked by:
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Legal Implications

24. There are no legal implications arising directly from the measures set out. However, the Council will need to ensure that arrangements are put in place to comply with any amendments to the Local Audit and Accountability Act 2014, Accounts and Audit Regulations 2015 and statutory guidance, including the Code of Practice on Local Authority Accounting in England and Wales.

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Background papers: Nil

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