PSAA response to the Independent review into the arrangements in place to support the transparency and quality of local authority financial reporting and external audit in England

Chapter 1 – Definitions of audit and users of the accounts	
Q1. Who, in your opinion, are the primary users of/main audience for local authority accounts?	Local authority accounts are an important component of governance and public accountability as they provide vital information to a variety of audiences about how public money has been spent. While there are plenty of potential users, such as taxpayers, residents, service users, electors and elected representatives, and external financial institutions, we recognise that few members of the public are likely to use them in practice. This is mirrored in the profile of the accounts with Members. The budget that drives Council Tax and highlights policy and service priorities is of far more importance to them, along with the subsequent information on delivery of that budget against corporate objectives. Clearly MHCLG has significant interest in the accounts, particularly if there is evidence of an issue emerging or materialising. HM Treasury consolidates the accounts of entities that exercise functions of a public nature to produce Whole Government Accounts (WGA). Local authority accounts are included in the WGA, and authorities have a duty to provide the required information in the format required.
Q2. Who are the other users of local authority accounts? Are any of these other users of accounts particularly important?	We consider that for the majority of the time and in most circumstances there are very low levels of interest in local authority accounts. Indeed local electors are more likely to be interested in local authority budgets and council tax information than they are in the authority's financial statements. Accounts can however develop a higher profile amongst electors when something goes wrong, also attracting interest from other potential users, such as the media and Members of Parliament.

Q3. What level of financial literacy/familiarity with accounts and audit is it reasonable to expect the primary users of accounts to have and what implications does this have for the information presented in accounts and/or the information that should be subject to external audit?	The level of financial literacy will vary between relatively expert users such as financial institutions and lay users, noting that the former needs to interpret the accounts to understand the dual accounting for IFRS and budgeting purposes, and that the latter may be highly informed particularly about as aspect of the accounts such as PFI. It is unrealistic to expect the accounts to answer all of the questions which users might ask particularly where enquiries reflect an interest in a detailed service or local area issue. The rights of electors to inspect the accounts, freedom of information, and the obligations on councils to publish information about payments made to suppliers provide alternative mechanisms for obtaining information to answer questions of this sort. ISA 720 sets out the requirements for the auditor's responsibilities in relation to other information beyond the audited financial statements. Defined in the standard as financial and non-financial information, such information includes entities' annual reports (which can be more than one document). The auditor's opinion on the statements does not cover the other information, and the ISA does not require the auditor to obtain audit evidence beyond that required to form an opinion on the financial statements. Practice Note 10 provides the mechanism for public sector interpretation of the ISAs. Councils are also free to provide further information sources beyond the accounts to assist with these interests. As a general rule, we do not think that it is appropriate to require non-accounts information to be separately audited, though there is scope to clarify what is covered by 'other information' in a local government context and for the auditor to apply the objectives in paragraph 11 of ISA 720 to that information. We understand that Practice Note 10 is being reviewed at present with a revised version due in 2020. We would expect the local authority decision-makers and those charged with governance to have a good level of financial knowledge. They should be involved in the management of the authority's balance sheet and financial risks as well as the budget and council tax setting process.

Q4. Does the external audit process cover the right things given the interests of the primary users of the accounts/is the scope of the opinions wide enough?	In general the ability to meet the needs of primary users has more to do with the relevant accounting and financial statement requirements rather than auditing requirements. For example, distinctively in local public bodies, producing the accounts on a 'going concern' basis is an accounting concept rather than a commentary on financial resilience. Within local audit the Code of Audit Practice adds a dimension with the requirement to provide a VFM arrangements conclusion. There is some pressure for the auditor to provide greater assurance on factors such as financial resilience and sustainability, although in practice this comes more from the preparer community than from users. The proposed new Code of Audit Practice offers a proportionate response to this pressure by proposing a commentary based approach in relation to the adequacy of VFM arrangements which will specifically address financial sustainability, governance and improving economy, efficiency and effectiveness. This review is also an opportunity to consider how the external audit process serves the primary users in terms of sector wide information and assurance. Potentially local audit can collectively inform users by providing overarching insights that are independent and soundly based. The proposed move to a VFM arrangements commentary should provide a useful source of audit views across different types of local government body and as a whole. However, unless there is an exercise to summarise the audit messages then there is a risk that the headline messages about the state of the sector will be missed. A challenge for the current and future framework is to act as one coherent system with a clear system leader (see question 15), providing stewardship, guidance (including dissemination of good practice), and strategic development and direction. This could include the system leader carrying out the analysis of audit messages mentioned above This would help to promote the importance of the local government audit role and reporting in England, which at present in our view lags behind the likes of Scotland, where the auditor's role is more comprehensive.

Q5. Is the going concern opinion meaningful when assessing local authority resilience? If not, what should replace it?	The going concern concept in local government is different to the corporate sector in that it is a requirement of the accounting code that all accounts are prepared on a going concern basis. This is based on the assumption that a local authority's services will continue to operate for the foreseeable future even if the responsible body is to be abolished. Local authorities can only be discontinued by a statutory prescription. The fact that the accounts are prepared on a going concern basis is not a commentary on the financial resilience or sustainability of the responsible body, unlike in the corporate sector where a going concern basis will be used (as opposed to a break up basis) only where there is sufficient assurance that the organisation will continue to operate beyond 12 months of the signing date. There is a debate as to whether auditors should flag going concern issues in their opinions despite signing off accounts prepared on a going concern basis, as it can be argued that they are signing an opinion on the entity, not the services that will continue. However, 'financial resilience' is a wider term that is less well defined than going concern, and in our view the auditor's role is better linked to the VFM arrangements work, proposed to be a commentary rather than a binary conclusion. We note that the NAO will be consulting on the Auditor Guidance Notes (AGNs) that are due to underpin the VFM arrangements commentary itself. The financial health of local authorities is influenced by other factors including the requirement to set a balanced and lawful budget. The local auditor may play a role in ensuring the observance of these requirements. For example, Northamptonshire County Council was issued with an Advisory Notice when its external auditor was concerned that it was about to set an unlawful budget.

<table>
<tr><th colspan="2">Chapter 2 – Expectations Gap</th></tr>
<tr><td>Q6. In your opinion, what should an external audit of a set of local authority financial statements cover?</td><td> The proposed revisions to the Code of Audit Practice as set out in Chapter 2 of the NAO consultation document state that the external audit should be undertaken in accordance with current auditing standards, requiring the auditor to give an opinion on the financial statements and accompanying financial information. This requires the auditor to give an opinion on:

whether the financial statements give a true and fair view of the financial position of the audited body and its expenditure and income for the period in question;
whether the financial statements have been prepared properly in accordance with the relevant accounting and reporting framework as set out in legislation, applicable accounting standards or other direction;
whether other information published together with the audited financial statements is consistent with the financial statements; and
whether the part of the remuneration report to be audited has been properly prepared in accordance with the relevant accounting and reporting framework

These are the appropriate items to cover within the audit of financial statements and are consistent with other sectors.
Please note that in response to question 3 we have highlighted the opportunity to clarify the application of ISA 720 to local government accounts to ensure that there is a common understanding about the auditor’s role on information other than the financial statements, noting that ISA 720 does not require the auditor to obtain additional evidence for this role.
An associated concern is that the wording of the audit opinions can be difficult to understand. For example, statements such that ‘we only report on this matter if we have a concern’ can be confusing, and there is currently inconsistency on reporting on VFM arrangements between local audit sectors. The September 2019 revisions to ISA570 (Going Concern) address this point with respect to going concern and a positive assertion will be required in opinions from the 2020/21 financial statements onwards. </td></tr>
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Q7. In your opinion, what should the scope of the external auditor's value for money opinion be?	The proposed revision to the Code of Audit Practice as set out in Chapter 3 of the NAO consultation document changes the scope and nature of auditor reporting on VFM arrangements to a commentary. There is a focus on reporting on three elements: • **Financial sustainability**: how the body plans and manages its resources to ensure it can continue to deliver its services; • **Governance**: how the body ensures that it makes informed decisions and properly manages its risks; and • **Improving economy, efficiency and effectiveness**: how the body uses information about its costs and performance to improve the way it manages and delivers its services. We note that the proposed move to a VFM arrangements commentary is in the context that the Act (LAAA 2014 s20(1c)) requires the auditor to report '*that the authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.'* We believe that it is important that the commentary is not simply descriptive and that the reader is clear on the auditor's view (this is particularly important as it is key to the new approach adding value.
Q8. What is your view on the scope of an external audit engagement is as described in Chapters 1 and 2 of this Call for Views? If it is different from your expectations, does this have implications for the reliance you place on external audit work?	We believe this question is intended to be answered by the primary users of/main audience for local authority accounts.

Q9. Should the external audit engagement be extended? If so, which additional areas/matters are most important for external auditors to look at? What would be the cost implications of extending the engagement to the areas/matters you consider to be most important be?	It is likely that any extensions to the audit remit will increase costs, although the extent will vary in line with local circumstances. A move to require auditors to consider arrangements against a higher benchmark than ‘adequate’ would be complicated as it would need definitions to be agreed, guidance to be enhanced and potentially significant extra work, and resulting costs. In our view there is an expectations gap in relation to external auditor’s remit for fraud. The current position is that, in compliance with auditing standards, auditors report whether accounts are free from material misstatement whether caused by fraud or error. ISA 240 sets out the auditor’s responsibilities relating to fraud in the audit of financial statements. It is widely acknowledged that there is an audit expectations gap and that the auditor’s role and responsibilities need clarifying, which includes the auditor’s responsibilities in respect of fraud. This is also an area in which internal audit could have a more formal role for reporting specifically on the organisation’s framework for preventing and detecting fraud. One option under the proposed Code of Audit Practice is that auditor’s comment on an organisation’s arrangements for preventing and detecting fraud and corruption as a part of the VFM arrangements commentary.

Chapter 3 – Audit and wider assurance	
Q10. Should the scope of the VFM opinion be expanded to explicitly require assessment of the systems in place to support the preparation of some or all of the reports that statute requires to be presented to full Council? If you do, which reports should be within scope of the external audit VFM engagement? If not, should these be assessed through another form of external engagement? If you believe that the VFM opinion should be extended to cover these reports will there be implications for the timing of audit work or auditor reporting?	The proposed revisions to the Code of Audit Practice to some extent address this issue, but importantly the NAO's further consultation on the AGNs can help find the right balance of cost/benefit. The scope of the VFM arrangements work, specifically in the area of governance, will mean that aspects of the systems in place to support the production of key reports could *potentially* be defined as within the scope of the commentary. However, formal assessment of those systems is likely to involve additional audit cost. An alternative type of engagement review of the statutory reports would need to be tightly defined to achieve acceptability to all parties, consistency of application and common understanding. 'Agreed upon procedures' is one option, but the professional framework involved would need to be considered in full (there is guidance on the ICAEW website https://www.icaew.com/technical/audit-and-assurance/assurance/what-can-assurance-cover/unaudited-financial-statements/agreed-upon-procedures). The guidance includes the following – *'the procedures and tests should be sufficiently detailed so as to be clear and unambiguous, and discussed and agreed in advance with the engaging parties so that the factual findings are useful to them and, depending upon the engagement, others to whom the report is made available. The practitioner's report does not express a conclusion, and therefore it is not an assurance engagement in the technical sense.'* To be of value reviews would need to be timely. Given the current pressures on audit resource adding to the external auditor's remit with a specific time-related task could have unhelpful consequences. An alternative is that a more in depth review of the preparation of these reports could be commissioned from internal audit, and could include matters such as validation of data. Authorities are free to engage specialists to report on any matter of their choosing, but this does not ensure either universal coverage (potentially expensive and arguably disproportionate for some) or coverage of the bodies most in need of review. We support the NAO's emphasis in the proposed Code on timely reporting, and so although the proposed date of the overall VFM arrangements work is after the statements, auditors should report any significant concerns as soon as practicable rather than wait for the final report.

Q11. Should external auditors be required to engage with Inspectorates looking at aspects of a local authority's service delivery? If you believe that this engagement should happen, how frequent should such engagement be and what would be the end purpose of doing so?	The current Code of Audit Practice requires that the auditor should be mindful of the activities of inspectorates and other bodies, and take account of them where relevant to prevent duplication and ensure that the demands on audited bodies are managed effectively. There is scope to develop the relationship with inspectorates further for the purposes of the proposed VFM arrangements commentary in order to enable the auditor to provide a richer picture, noting though that client confidentiality issues would need to be worked through, and that this will include adhering to statutory and professional frameworks. At the sector level, there may be scope for a more coordinated approach whereby inspectorates share intelligence and risks in order to ensure that VFM arrangements work is able to add more value in the context of local risks. The benefits of increased engagement need to be measured against the costs of increased liaison, as there are resource implications for the auditors, inspectorate bodies and the audited bodies in getting to a point where the VFM arrangements commentary reflects an up-to-date position – for sound reasons there can be a significant gap between inspectorate visits and auditors cannot be expected to conclude on progress on another organisation's recommendations at an audited body. In summary there is merit in a more regular dialogue, proportionate to the type of body and risk profile. However, it will need careful planning if this is to be more than updates on what is already in the public domain.
Chapter 4 – The governance framework for the audit system	

Q12. Does the current procurement process for local authority audit drive the right balance between cost reduction, quality of work, volume of external audit hours and mix of staff undertaking audit engagements?	Our response to this question focuses on PSAA's procurement process for the opted in bodies. However, we note that "the current procurement process" for local government bodies also includes the arrangements adopted by bodies which decided to opt out. The PSAA procurement strategy was based on the aim of maximising value for local government bodies by; • Securing the provision of high quality, independent audit services; • Incentivising audit suppliers to submit highly competitive prices; • Awarding contracts to a sufficient number of firms to enable the appointment of an appropriately qualified auditor to every participating body; and • Supporting a long term competitive, sustainable market for local public audit services which has value for all relevant authorities. PSAA then considered a range of detailed procurement options to meet the objectives outlined, taking professional procurement advice as necessary. Responding to feedback from the sector we ensure that the procurement placed a strong emphasis on audit quality. We were conscious that all firms needed to go through the new Recognised Supervisory Body registration requirements before being able to bid on our contracts, and that this would ensure that firms were able to satisfy a number of eligibility criteria. Nevertheless, in order to further strengthen arrangements, we adopted a tender evaluation framework which placed greater emphasis on quality than the Audit Commission's 2012 and 2014 procurements. It placed an equal weighting on price and quality compared to the previous 60 (price):40 (quality) model. PSAA decided to undertake the procurement based on five graduated national lots to allow firms to bid at levels which matched their capacity/appetite for work. A sixth lot, with no guaranteed quantum of work, was also incorporated to provide coverage if an audit could not be assigned to another firm because of exceptional independence issues.

	Key features of the procurement are summarised below.

Key features of the PSAA procurement approach
Lot sizes: six lots of varying size including an insurance lot to cover exceptional independence conflicts. Individual firms could win one lot only meaning that, if all lots were awarded PSAA would enter into contracts with six firms or consortia.
Contract term: 5 years with an option for PSAA to extend for up to a further 2 years.
Scope: the work required as an appointed auditor is set out in the Act and the NAO Code of Audit Practice.
Prices: the firms' required remuneration for any given lot.
Quality: assessed via PSAA's systematic evaluation of tenders submitted.
Social Value: encouragement to firms to demonstrate the added social value which the contracts could leverage, especially in relation to recruitment, training and development of apprentices.
Auditor appointments: to reflect a hierarchy of relevant principles.

The tender process include a selection questionnaire (SQ) with evaluation of financial position followed by the Invitation to Tender (ITT). PSAA used the International Auditing & Assurance Standards Board (IAASB) Framework for Audit Quality to inform the development of the ITT and assess the quality of the bids submitted. Bids were received from firms and consortia.

The evaluation of tenders was particularly thorough and exacting. Best practice was followed including complete separation of financial and quality evaluations. Independent quality assessments were completed by three experienced professionals as the prelude to a consensus meeting with oversight provided by a Board Member and a sector representative. The evaluation of the bids focused on a range of quality of service criteria including;

- Sector knowledge;
- Audit approach;
- Resourcing and capacity;
- Capability; and

	• Transition between audit firms. The audit methodology employed by a firm is a key determinant of the volume of hours an engagement will take, along with the level of audit risk at the individual body. Viewed in isolation 'hours spent' is not a reliable indicator of quality. For example, data analytics software can enable entire accounting balance populations to be reviewed instantly against set criteria to identify the matters of concern to be followed up, whereas manually selecting and testing a sample of that population provides less assurance and can take considerably longer. The mix of staff undertaking audits varies per engagement in accordance with risk of that engagement and taking into account factors such as the experience of audit team members, continuity and training requirements. Whilst the procurement process was ongoing, eligible bodies were deciding whether or not to opt in (the legislative timescale meant that we could not wait until the opt-in deadline to start the process). This meant the decisions on all aspects of the bid process were determined with some knowledge of the emerging position on opt-ins but before the overall number, location and type of body that were fully settled. Future procurements should not be constrained in that way. We understand why audited bodies were required to make the decision to opt-in at a full council meeting (or equivalent) for the first procurement, but we question whether this should be necessary to require such a high level of formality when bodies renew their decisions to opt-in for subsequent appointing periods. The particular benefits of opting-in to the PSAA scheme were; • assured appointment of an independent, qualified, and registered auditor; • appointment wherever possible of the same auditors to bodies involved in significant collaboration/joint working initiatives or combined authorities, if the parties believe that it will enhance efficiency and value for money; • on-going management of independence issues; • securing highly competitive prices from audit firms; • minimising scheme overhead costs; • savings from one major procurement as opposed to a multiplicity of small procurements; • distribution of any surpluses to participating bodies; • a scale of fees which reflects size, complexity and audit risk; • a strong focus on audit quality to help develop and maintain the market for the sector;

	• avoiding the necessity for individual bodies to establish an auditor panel and to undertake an auditor procurement; • enabling time and resources to be deployed on other pressing priorities; and • setting the benchmark standard for audit arrangements for the whole of the sector. A further benefit was assurance of appointments of auditors to all opted-in bodies. It is likely that some authorities, for example, in remote locations, might struggle, acting independently, to attract sufficient potential auditors to run a compliant tender. We understand that some of these difficulties are beginning to emerge in NHS bodies. Appointments of the successful audit firms to authorities were made in accordance with a hierarchy of relevant principles; • Ensuring auditor independence • Meeting contractual commitments • Accommodating joint/shared working arrangements between bodies • Ensuring a blend of authority types for each audit firm • Taking account of a firm's principal locations • Providing continuity of audit firm where appropriate There are currently 487 bodies that are part of the PSAA scheme and 11 that made local arrangements. Of the 11 bodies that opted-out, two have now decided to join the PSAA scheme. PSAA's procurement was supported by an Advisory Panel of representatives of local authority Treasurers' Societies and the LGA. Information on the procurement is provided on the PSAA website and in the detailed file of relevant documentation provided to the Review team. We were pleased to be 'highly commended' in the Public Finance Innovation awards 'Outstanding Procurement Initiative Category' in April 2018. The PSAA Board and staff were keen to ensure that learning should be carefully captured from all of the preparatory work in relation to the company's Appointing Person role, not least so that it could be carried forward systematically to future appointing periods which operate on a five year cycle. We therefore engaged Cardiff Business School (CBS) to carry out an independent review of our work. The CBS report and action plan were subsequently posted on the PSAA website in January 2019. The report commented very positively on PSAA's work describing it as *'an outstanding example of sector-led improvement'.* It

identified a number of important lessons learned and made recommendations for improvement where appropriate. It also highlighted and discussed some of the challenges in relation to the strength and sustainability of the local audit market.

PSAA has responded to the challenges outlined, paying particular attention to market sustainability which has emerged as a more graphic challenge following the difficulties experienced in the audit of 2018/19 accounts. We have commissioned research concerning the views of firms - both licensed and currently unlicensed - concerning the current market position and any changes which make the market more attractive to firms. We hope to be able to share the results of this work with the Review team in January.

We are also currently exploring the option of commissioning work to establish whether market sustainability would be assisted by the establishment of an alternative non-market supplier, such as a state-owned body or a social enterprise. This work will examine the parameters, viability and costs and benefits of such an initiative. In the event that such an option was taken forward it would, of course, require the support of a number of key stakeholders.

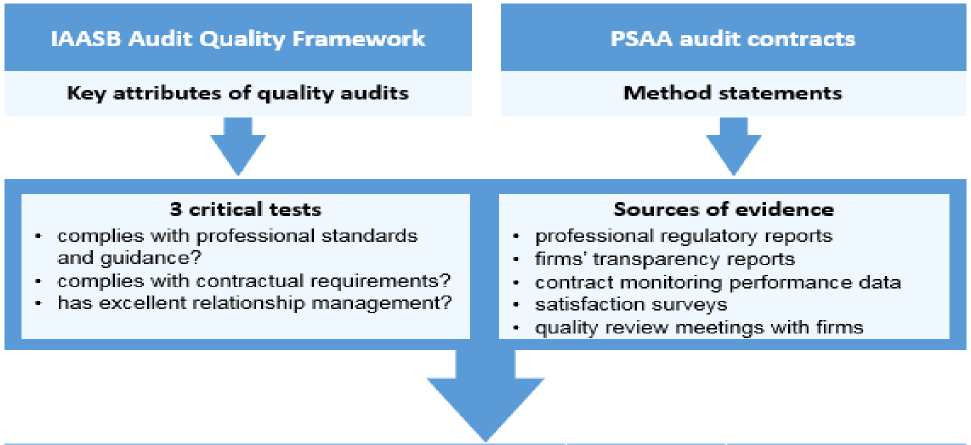
Audit Quality Arrangements

PSAA's methodologies for ensuring a strong focus on audit quality throughout the procurement process has been explained above. To coincide with the commencement of the new system PSAA has also developed a new approach to monitoring and publicly reporting on audit quality and audit contract compliance. Developed using the IAASB Framework for Audit Quality, our new approach will, as it is populated**,** bring together information in three key areas to provide a well evidenced, rounded picture for each firm:

- Professional regulation;
- Contract Compliance; and
- Relationship Management.

PSAA's new methodology is illustrated below.

PSAA audit quality monitoring methodology



Evidence-based outputs	Firm focus	System wide focus
Quarterly report against a scorecard of KPIs	✓	✓
Quarterly report and latest insights into audit quality		
• Regulatory reports	✓	
• Transparency reports	✓	
• Satisfaction surveys	✓	✓
Annual summary report	✓	✓

Importantly key elements of the firms' tender documentation has been incorporated within the contracts as method statements - another new development. This will enable audited bodies to provide more informed feedback on auditor performance when we survey them, reflecting an understanding of the client service expectations set out in the tender documents.

Q13. How should regulators ensure that audit firms and responsible individuals have the skills, experience and knowledge to deliver high quality financial and VFM audits, whilst ensuring the barriers to entry do not get too high?	The framework for regulating local audit and licensing local auditors borrows from the Companies Act requirements for regulating the audits and auditors of listed companies. Those arrangements are designed to protect the interests of shareholders and other investors. It is debatable whether such arrangements are relevant and appropriate to local government. The legal and constitutional position of local authorities is different from that of listed companies. Similarly the interests of electors and taxpayers are different from the position of shareholders. In our view this is an important issue because it is increasingly clear that local audits are being significantly impacted by the regulatory pressures arising from controversial financial failures in the private sector. These pressures are having significant implications for price and quality, including in some circumstances auditors are being required to carry out more work to secure higher levels of assurance on issues that are critically important in a listed company, but are less significant in the context of assessing risk in a local authority's financial statements – noting though the obligation on all parties to meet the requirements of WGA reporting. The framework includes a licensing regime, setting entry requirements for firms and individuals to undertake local audits. The FRC has delegated this responsibility to ICAEW which manages the scheme for registering 'Key Audit Partners' and firms, such that individuals have a specific level of experience of local audit before being licensed to provide a local audit opinion. These arrangements pose a challenge for existing supplier firms wishing to stay in the local audit market, and represent a significant hurdle for potential new entrants to the market. No other types of public sector audit are subject to statutory regulation in this way. It is not considered necessary for central government departments, education or housing bodies, or for local audits in Scotland or Wales. In our view it is important to evaluate whether the benefits to the sector of the licensing of local auditors are outweighed by the limitations/barriers to entry created for firms considering entering the market, recognising that similar burdens are not placed on other public and private audits. It would be possible to relax the licensing criteria for individuals within firms while continuing to maintain licensing of firms. ISA 220 'Quality Control on the Audit of Financial Statements' specifies requirements on ensuring that engagement teams '*collectively have the appropriate competence and capabilities*'. Within audit firms partners and senior staff have to demonstrate competence and up-to-date training and knowledge to undertake work for the firm in certain areas e.g. Charities or US GAAP. Competence, training and knowledge requirements in respect of local audit could be addressed and tested in the same way.

	Alternatively it would be possible to rely upon procurement processes to evaluate the qualifications and experience of individuals and/or firms avoiding the need for a prior licensing requirement. A compounding factor is that time spent on local audit does not count towards the accumulation of audit experience required for the ACA qualification despite the accounts being IFRS compliant. We acknowledge that final decisions about whether regulation of local audit should be decoupled from the regulation of listed company auditing, as well as whether licensing arrangements are necessary and valuable in local audit, will depend upon Government's response to the changes recommended by the CMA, Kingman and Brydon reviews, and its appetite for implementation of them. In our view the ideal outcome would be a regulatory framework which is able to be responsive to the needs of and unique challenges affecting local bodies whilst at the same time sitting logically alongside any new arrangements put in place for other sectors of the economy, recognising the desirability of a level of consistency across all sectors on some issues. A further factor to be considered is the overall level of experienced local auditor resources generally, and the supply chain of audit trainees becoming qualified local auditors. We have referenced the audit resources issue in question 18, including the need to review the implications of maintaining 31 July as the industry target for publishing audited accounts. The 2018/19 audits have indicated systemic stresses that were not apparent in earlier years. They reflect the fallout from the series of controversial financial failures in the private sector which have given rise to the CMA, Kingman and Brydon reviews, including the efforts of firms to demonstrate greater scepticism and achieve higher levels of assurance to confirm that opinions are sound. A significant proportion of audits were not completed by the publishing date of 31 July in part due to a lack of auditor resources (albeit that this was not the only reason for delays). Affected firms have indicated that this is due to an insufficient and finite number of relevant experienced individuals in 2018/19 due to attrition rates, particularly at manager and senior auditor grades. The number of licensed KAPs is at a concerning level, especially given the move towards specialisation in internal or external audit within some of accredited firms, which will impact on the numbers available to conduct local audits. A consistent picture is emerging that firms are having to resort to overseas to fill vacancies in both public and private sector auditing due to low levels of interest within the UK.

Q14. What metrics should regulators use when assessing whether financial and VFM audits are delivered to an appropriate level of quality?	The relatively complex nature of the local audit system tends to result in a variety of specialist organisations focusing on measurement of performance in sub-compartments of the system. In our answer to question 15 we have referred to the need for a system leader. Such a role would, in our view, be best placed to develop a more joined-up, system-wide approach to performance including interpreting and disseminating performance information. It is generally recognised that output-based audit quality metrics are difficult to define and whilst individual KPIs shed light on particular variables, there is no comprehensive suite of KPIs which provides a definitive overall picture. The best overall assessment of audit quality is therefore obtained by thorough independent reviews of a sample of completed audits. The PSAA framework for monitoring audit quality as part of contract compliance takes a wide view of audit quality based on the IAASB Framework for Audit Quality. As well as focusing on professional standards which might be thought of as “technical quality”, PSSA’s approach also addresses compliance with contractual requirements and relationship management. Both internal and external reviews provide scored judgements on the quality of audits. Each firm has its own quality monitoring arrangements. The corporate sector review arrangements are now being applied to local audit with the FRC’s AQRT reviewing major local audits (those with expenditure above £500m) and audits that meet the definition of a ‘Public Interest Entity, which includes some relatively small bodies. The ICAEW’s QAD review the remaining audits with a different reporting regime. The situation is further complicated by the fact that firms and the external reviewers have different scoring methodologies. The FRC has stated that it expects all FTSE 350 audits it reviews with year-ends from June 2019 onwards to be scored as 2A (limited improvement required) or better. The target applied previously by the Audit Commission’s contracts included 2B (acceptable overall with improvements required) as an acceptable score. Interestingly, the FRC now classifies 2B as simply ‘improvements required’. We understand that the FRC intends the expectation for all review scores to be at least 2A to apply to local audits. In our response to question 13 we discuss whether current regulatory and licensing arrangements for local audit are appropriate and are sufficiently responsive to sector needs and, accordingly, able to add value. In our view there would be potential advantages in a tailored approach for local audit which was able to prioritise the specific needs and unique challenges of local bodies. One option would be to position this responsibility alongside the role of setting the code of practice for local audit. This would enable the

	approach to regulation and reviews to be fully aligned with the Code including having regard to the local auditor's wider duties and powers. We acknowledge that this issue should ideally be considered in the context of the Government's plans for audit regulation and licensing post Kingman and Brydon. We note that there is an intention for the regulator to engage with local government bodies on the results of their inspection of the financial statements audit and the VFM arrangements conclusion (we understand that the VFM arrangements commentary is under discussion). However, we are concerned that at present the regulator's remit does not cover the auditor's additional powers. For example, the auditor's power to issue a statutory recommendation under Schedule 7 of the LAAA 2014 is a vital part of public audit, and if that power is exercised, it should form part of the assessment of the auditor's delivery of the Code responsibilities. If the regulator's feedback to a client fails to address the auditor's work on the Schedule 7 recommendation it will present an incomplete picture and potentially undermine the auditor's position and authority with the client. We believe that this anomaly should be resolved as a matter of urgency.

Q15. Do you agree with the Independent Review of the Financial Reporting Council's findings and recommendations; and why do you agree/not agree? If you agree with the recommendations do you think the 'single regulatory body' should be the "successor body to the FRC" or a sector specific entity? If you do not agree with the recommendations are there any other changes you would make to the regulatory framework for local authority audit?	We have raised a number of issues relevant to this question in our responses to questions 13 and 14. In our view it would be helpful to decouple responsibility for local audit from that for company audit, recognising that local authorities and listed companies are fundamentally different and have their own distinctive needs and challenges. The solutions appropriate for a company are unlikely to be appropriate for a local authority and vice versa. In our view local audit should be subject to regulatory arrangements which are tailored to the needs of local bodies and their stakeholders. One option would be to co-locate this function with the Code-setting responsibility for local audit. This would enable better alignment with the Code, including the local auditor's wider powers. If the option of locating regulation of local audit within an overarching regulator is continued, we would recommend the development of tailored governance and management sub-structures to ensure that local bodies' needs and interests, and the needs and interests of their stakeholders, are prioritised in the regulatory arrangements and approaches developed. In relation to local audit, the Kingman review highlights a concern which extends beyond his focus on regulation. He raises concerns about the fragmented system for local audit. We agree that this is a potential weakness of the system which allocates responsibilities to a variety of different specialist bodies without addressing the need for clear arrangements for system leadership and co-ordination. This results in a dependence on the goodwill and co-operation of all the players to share findings, views and intelligence. However, despite the willingness of the parties to play their part, it is inevitable that an informal framework is vulnerable to legal and professional restrictions on information sharing. In our view the issue of system leadership requires attention in order to ensure that all of the relevant parties are committed to the same overall aims and objectives and that mechanisms exist to resolve any differences of view which may arise. One option would be to establish an independently chaired Board to oversee the local audit system with a remit to ensure the smooth operation of the whole system including providing leadership and coordination to the various bodies responsible for administering different aspects of the system. If such a Board was located within the architecture of MHCLG it would be possible to implement some of its most significant decisions by way of ministerial directions on the advice of the oversight Board. These arrangements could potentially be implemented quickly and would enable current issues to be addressed with greater urgency and force. It would avoid the disruption, delay and uncertainty that the creation of a new body would be likely to engender. We do not agree with Kingman that it is necessary to incur the expense, delay and potential added complexity of establishing a new public body to take on this system leadership role as well as an unspecified number of further responsibilities. We note that although the Kingman Review stressed that there was no intention to recommend the re-establishment of the Audit Commission, its report appears to

	envisage a new body with many of the Commission’s former powers and, potentially, a wider role in relation to the regulation of accountancy bodies. We are not clear what the evidence base is for this proposal. Creating a new body would also distract from the live issue of shortage of available auditor resource. The background is that widely reported financial failures in the private sector have led to concerns being expressed about the role of auditors and the value of audit. The Government’s response has been to commission a series of high profile reviews. Some, such as Select Committee Inquiries and the Competition and Markets Authority Review have impacted directly on firms influencing risk averse, cautious behaviours including many additional tests and increased application of firm-wide procedures. The Kingman review itself has impacted on audit regulation. Importantly, the responses of both the regulator and firms to these various pressures do not differentiate between public and private sector work. The cumulative impact has been to cause audits to take more time leading to delays in the issue of some audit opinions. These difficulties have then been compounded by issues with the working papers within some audited bodies and the identification of significant technical issues in accounts. Several firms have referred to the attrition rate from their public sector teams as the pressures arising from the new timetable and the juxtaposition of NHS and local government audits become more apparent. The result is that there is a shortage of experienced auditors with the depth of knowledge needed for local government audit.

Chapter 5 – Audit product and Quality	
Q16. Do external audit firms have enough understanding of the local authority regulatory framework to focus audit work on the right areas? How do they/should they demonstrate this? Who should regulate this work?	The Code of Practice states that it is for the independent auditor to determine what work is needed in order to discharge the Code responsibilities. Audit work is required to comply with auditing standards taking into account any relevant adaptions such as Practice Note 10, and to have regard to the AGNs issued by the NAO. In order to be able to undertake local audits firms and individuals have to be registered with ICAEW, and appointed through an appropriate procurement process. The auditing standards on planning (ISA 300) and reporting (ISA 260) require communication with those charged with governance (typically the audit committee) concerning how the audit is to be conducted, including the approach to key risk areas, and how the results and conclusions of that work will be reported. In the current debate around local audit there is a wide consensus that the role of auditors is to give a true and fair opinion on IFRS-compliant financial statements prepared in accordance with the CIPFA/LASAAC Accounting Code. However, there are tensions and disagreements in relation to the extent of auditors' work and emphasis on valuation of Property, Plant and Equipment where the prioritisation and risk profile assigned by the auditor does not match many preparers' views of the value of assurance. Quality monitoring arrangements have not reported any issues with respect to the auditing standards on planning. The NAO is currently consulting on a new Code of Audit Practice which proposes changing the auditors' work on VFM arrangements in response to a sector-wide consultation.

Q17. Do auditing standards have a positive impact on the quality of local authority financial audits?	Auditing standards provide an internationally recognised framework for assurance for the users of the accounts and underpin a true and fair audit opinion. In our view they are as indispensable as recognised accounting standards and an important component of the overall arrangements designed to inspire trust and confidence in the stewardship of public funds. The Code of Audit Practice requires (proposed Code reference 1.17) that auditors comply with standards issued by a relevant regulatory body (in this case the auditing standards as issued by the FRC). When assessing the positivity of the impact of auditing standards on local authority audits it is important to acknowledge the variety of the users of the financial statements and that their priorities differ. For example, what's important to the local user may be different from what is valued by HM Treasury for WGA purposes, for example the extent of work on PPE. We note that Practice Note 10 issued by the Public Audit Forum contains guidance on the application of quality control and auditing standards issued by the Financial Reporting Council (FRC) to the audit of public sector bodies in the UK. We understand that this is due for revision in 2020.

Q18. Do audit firms allocate sufficient resources to deliver high quality and timely audits? How is consistency and quality maintained in external audit work? To what extent is there consistency in audit teams year on year? What more can be done to ensure consistency between firms?	We recognise that there has been a significant audit resourcing issue in 2018/19. However auditor resourcing was not the only reason for the increase in the number of opinions given after the publishing date. There is much debate about the impact of the 31 May deadline for accounts to be submitted for audit, and the 31 July audit target for publication of audited accounts. Whilst the latter is non-statutory, it is the expectation of the sector. As we have reported publicly, the number of local government opinions not awarded by 31 July rose significantly in 2018/19 to 208, up from 64 in 2017/18. Based on information from the audit firms there are three main reasons - an increasing shortage of audit resources suitable for local government work (including significant recruitment and retention challenges), and/or concerns about the quality of draft accounts and working papers (CIPFA acknowledges that producing IFRS-based, code-compliant accounts is a time-consuming annual task, placing considerable strain on what are now leaner finance teams), and/or challenges resolving technical issues within increasingly complex accounts. In our view the 31 July target has exacerbated the audit resource issue. Local government audit is a specialist area, and reducing the audit window means that those experienced in it can cover fewer audited bodies. It has also created an intense period of local audit in the Spring and Summer that we understand has resulted in higher audit staff attrition rates, exposing the lack of a secure pipeline. In the circumstances we believe that it would be helpful to reconsider the 31 July target with a view to reverting to the previous deadlines. Whilst this would not be a panacea, it would help to make best use of the audit resources available as well as providing more time to improve the quality of working papers and the consideration of technical issues. It would also help to address the unattractiveness of local audit as a career. Delivery of a high quality audit may require additional time to obtain the required level of assurance. Consistency and quality in external audit work is maintained by: • Use of standardised programmes of work with inbuilt checks and balances; • Internal Quality Monitoring; and • External Quality Monitoring. The outcomes of a consistent approach will be different at different authorities because of specific and individual factors such as materiality and culture (e.g. the body's approach is attempting to generate commercial revenue streams). Consistency must not equal rigidity; it must include the flexibility to tailor the audit to the needs and circumstances of the particular audited body.

	Changes within an audit team will be a natural part of training and progression and are a requirement of a sustainable profession. The challenge for firms is to ensure that change is managed well, and that ‘new’ staff are properly briefed and inducted. As part of our contract monitoring responsibilities we are surveying audited bodies’ chief finance officers and audit committee chairs. Our survey questions invite feedback on this issue.

Q19. To what extent are senior audit staff, particularly the responsible individual signing the audit certificate, visibly involved in audit work? Who do senior audit staff meet with?	We would expect involvement by the Key Audit Partner (KAP) at the main decision points of the audit. The requirements are specified by the audit standards. However it is important to acknowledge that KAPs with substantial portfolios are likely to have diary clashes (the 31 July deadline has reduced the window by two months) if Committees are concertinaed into a short window and will need to make alternative arrangements. The engagement with authority staff will depend on the nature of the authority and its risks, but we would expect meetings to be held routinely with the finance director. As a general courtesy, we would expect auditors to be responsive to requests for meetings from leading officers and members of the audited body.
Q20. Should external auditors consider financial resilience as a key factor when designing their VFM work programme? If so, what factors do they/should they consider as indicative of a lack of financial resilience?	The proposed revision to the Code of Audit Practice address the issue to some extent as the VFM arrangements work will include financial sustainability. This is not necessarily the same as financial resilience although there is a strong argument that financial resilience is a prerequisite for financial sustainability. A commentary on financial sustainability is likely to include arrangements that relate to financial resilience, such as the track record in delivering on-target performance against budgets, strengths and weaknesses in financial controls, the robustness of medium and long term plans and the reserves position.
Q21. Does the Code of Audit Practice provide enough guidance on how much work needs to be done to support the VFM opinion? If not, what should it cover?	As with the current Code of Audit Practice, the NAO will support the Code with AGNs which auditors are required to have regard to. These cover a range of topics and sector specific guidance and are publicly available on the NAO’s website. With respect to the planned commentary we understand that the NAO intends to develop guidance as a part of the AGNs which will be subject to consultation.

Q22. Do auditing standards provide appropriate guidance on quality standards for VFM audits? If not, is guidance needed and should it be included in the Code of Audit Practice or elsewhere?	The auditing standard ISQC1 covers the audit of financial standards and information published with them, and in respect of the public sector, covers '*reporting on an entity's arrangements for the proper conduct of its financial affairs, management of its performance or use of its resources*'. ISQC1 is the overarching standard of engagement quality control and is appropriate for these engagements. We have referred to the AGNs in our answer to Q21.
Q23. What is the current relationship between external and internal audit? How should that relationship be developed to add most value to local authorities and local residents?	The extent of the current relationship is impacted by the ISA 610 (Using the Work of Internal Auditors), which was revised and published in 2013. The ISA sets limitations on that usage at paragraph 5-1 as follows – '*The use of internal auditors to provide direct assistance is prohibited in an audit conducted in accordance with ISAs (UK). For a group audit this prohibition extends to the work of any component auditor which is relied upon by the group auditor, including for overseas components. Accordingly, the requirements and related application material in this ISA (UK) relating to direct assistance are not applicable.*' Although direct assistance is prohibited, Paragraph 7 of ISA 610 recognises that internal audit can '*inform external audit's understanding of the entity and its environment and identification and assessment of risks of material misstatement ISA (UK) 315 (Revised June 2016) addresses how the knowledge and experience of the internal audit function can inform the external auditor's understanding of the entity and its environment and identification and assessment of risks of material misstatement. ISA (UK) 315 (Revised June 2016) also explains how effective communication between the internal and external auditors also creates an environment in which the external auditor can be informed of significant matters that may affect the external auditor's work.* The ISA also states at paragraph 3 that '*Nothing in this ISA (UK) requires the external auditor to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed directly by the external auditor; it remains a decision of the external auditor in establishing the overall audit strategy.*' This ISA framework for the relationship recognises that internal audit performs its work on behalf of the audited body (whether the service is provided by directly employed staff or outsourced). In that context ISA 610 sets out the requirements that external audit must meet to be able to make use of internal audit

	work. The extent of the work needed to reach this point has led to the current position that it is the norm for external auditors to conclude that it is not efficient to seek to do so when setting their testing strategy (in line with paragraph 3 above). However, in addition to internal audit being able to inform external audit's work to meet ISA 315 referenced above, we believe there is potential to explore how the relationship with internal audit could assist the external auditor to construct the proposed VFM arrangements commentary. It is important to recognise that internal audit has an important and distinct role to play which must be its primary purpose and priority. Audited bodies need to ensure that it has sufficient resources to deliver its remit, whether or not this includes an enhanced relationship with external audit.

Q24. What should happen when a regulator finds that a local authority audit has not met quality standards? Where should the balance between ensuring effective enforcement action against auditors and maintaining participants in the audit market lie?	We note that all professional audit staff face penalties in the shape of fines or removal from specific types of audit if they fail to meet quality standards. Firms drew this to our attention in their tender bid documents. Those who are qualified accountants are also subject to potential disciplinary action and penalties from their professional body. Whilst it is important that quality standards should be enforced there is a danger if the risk of audit enforcement action outweighs the rewards from undertaking local audit. In a recent judgment the FRC noted '*We also take into account that a fine should not be such as to deter accountants from accepting audit or CASS audit engagements*." The PSAA contract provides that in the first instance firms are given an opportunity to address matters with the agreement of an expected timetable for improvement. Failures which are persistent or incapable of remedy may result in the revocation of an auditor appointment.
Chapter 6 – Auditor Reporting	
Q25. Do you think that the format of the VFM audit opinion provides useful information? If not what would you like it to cover?	The NAO'S proposed revision to the Code of Audit Practice replaces the engagement risk binary conclusion on VFM arrangements with a narrative commentary on financial sustainability, governance and arrangements for securing economy, efficiency and effectiveness. We understand that the NAO is preparing example reports and guidance that will be help all parties to understand what to expect. As mentioned in question 7 it will be important to ensure that the commentary is more than a description of arrangements or current practice.

Q26.Do you think the VFM opinion should be qualified solely because a local authority has received an inadequate Ofsted opinion or a similar opinion from another inspectorate?	In our response to the NAO's first consultation stage for the new Code we set out our position as follows - *'There appears to be a particular perception issue in relation to 'except for' conclusions that are driven by reports by others, for example OFSTED. Quite rightly auditors are required to take into account the unsatisfactory results of inspections, particularly those that relate to key areas of service expenditure such as Children's services. There is therefore a logic in the auditor's resulting except for conclusion, although noting that some perceive it to be double jeopardy given the public nature of Inspectorate reporting, especially as the auditor does not play any part in the inspection. In addition there is often more than a year's gap before any re-inspection of the service is reported on, and so in the following year it is common for the auditor to maintain the except for conclusion. These factors have led to a tendency to see except for conclusions that relate to inspectorate reports as less important as it adds nothing to the public's knowledge. We suggest that an option would be for the auditor's VFM arrangements reporting to refer to the results of the inspectorate report, but then to state that the matter is outside of the auditor's scope and then report on their findings on the rest of the body's arrangements.'* The NAO has subsequently proposed a move to a VFM commentary which enables the auditor to reference any relevant Inspectorate findings. The AGNs can provide guidance on how the auditor is expected to comment – for example**,** if the audited body is confident that it has addressed the findings, but the inspectorate has not yet revisited. This may be an exception where the auditor's commentary remains factual rather than qualitative in nature.
Q27. Do you think that the VFM opinion is presented at the right point in a local authority's annual financial management and budgeting cycle? If not when do you think it would be most useful?	The proposed Code emphasises that where there are significant findings, these should be reported as soon as possible during the audit cycle. The VFM arrangements work will be summarised in the Annual Auditor's Report which should be prepared by 30 September. If this is not possible, a statement will be required to explain the delay. In our view these revisions will promote more timely and effective reporting. If the principle of de-coupling the VFM arrangements conclusion from the opinion on the financial statements is accepted, there may be a case for considering reporting at a different point in the financial year, possibly informing a body's Annual Governance Statement. However there are practical issues to consider given the NHS deadlines, and it may be sufficient to have the requirement to report significant findings as soon as possible. Management should then have the auditor's up-to-date position when compiling the AGS, as should Those Charged With Governance when approving it.

Q28. Where auditors have identified significant issues, audit certificates and reports have often been delayed? Why do you think this is and can changes be made to the framework to encourage earlier reporting of significant issues?	The proposed new Code of Audit Practice stresses the importance of timely reporting, and not waiting until the issuing of the Auditor’s Annual Report at the end of the reporting process if a significant issue arises during the audit cycle.
Q29. In your view, what sorts of issues should Public Interest Reports be used to highlight?	A public interest report (PIR) should be used for reporting the most serious matters that require to be brought to wider attention. The Freedom of Information Act, publicity requirements, and the transparency agenda often mean that matters on which auditors could conceivably make a PIR are already widely known and publicised. It appears that auditors are leaning more towards making statutory recommendations as they perceive that they are quicker to process and receive appropriate publicity. However, statutory recommendations are also used relatively infrequently. The NAO does provide guidance in this area.

Q30. Statistics demonstrate that very few Public Interest Reports and Statutory Recommendations have been issued. Why do you think this is? Does it indicate an issue with the framework or common behaviours? If you think this is an issue, what can be done to incentivise more frequent and timely reporting of significant issues?	It is for the independent auditor to consider the particular circumstances and the appropriate action to take. Auditors may choose not to issue a Public Interest Report as a matter is already widely known and publicised, or the authority has already taken action to address a problem. However, we note that one of the criteria for considering a PIR is to provide the auditor's view. The proposed Code puts additional emphasis on the need for auditors to consider the public interest more widely when deciding whether to issue a Public Interest Report as a result of receiving an objection. The proposed Code sets the expectation that auditors will not only consider the extent to which the issue is already known to the public, but also consider whether it is in the public interest for the auditor to publish their independent view on the matter. The proposed Code stresses the importance of reporting on a timely basis and not waiting for the Auditor's Annual Report if necessary. It also introduces formal follow up and reporting procedures enabling monitoring of the effectiveness of authorities and 'those charged with governance' in dealing with matters brought to their attention. In our answer to question 40 we have provided an analysis of objections determined since 2015.

Q31. Does a publication summarising the results of local authority audits add value? If so who should publish it and what information would they need to have access to perform this function effectively?	Publication of results does add value. We understand that the NAO is considering options for reporting in this area. The content of any report summarizing the results should focus on information concerning the formal outcomes of the audit eg opinions, public interest reports and statutory recommendations. The VFM arrangements commentary may be more difficult to summarise, but the proposed Code encourages the auditor to make recommendations and a summary and an analysis of them would be useful. Whilst we would expect the Auditor’s Annual Report to be available on an authority’s website, there would be merit in making this information available in respect of all bodies through an information portal. The logical publisher would be the system leader that we call for in question 12. Something similar might be helpful in respect of smaller authorities. A commentary from the system leader on the results of audits for the sector as a whole would be beneficial, as it would provide a sense of the health of the sector which over time would provide an interesting and potentially informative trend. The system leader could also set out how issues are to be addressed, and the aims for the future.

Chapter 7 – Framework for responding to auditor findings	
Q32. To whom should external auditors present audit reports and findings; is it the audit committee, to full council or equivalent or another committee? If findings are not presented to full council or equivalent what information (if any) should full council or equivalent receive?	ISA 260 requires that the auditor '*shall determine the appropriate person(s) within the entity's governance structure with whom to communicate'*. This is typically the audit committee although the name and detailed terms of reference will vary by authority. The ISA 260 expectation is that it has responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity, including overseeing the financial reporting process. Given the nature of the financial statements and audit deliberations (eg ISA 260 reports) in our view the 'audit committee' is the appropriate forum to continue to receive the reports on the financial statements. The Audit Committee should be apolitical, requiring elected members to adopt a different mindset and to conduct themselves differently that they might in other fora. There is scope to enhance the profile of audit work and findings through engagement with other elements of the body (e.g. cabinet and/or scrutiny committee and/or full council), and in our view that engagement and deliberation should also be conducted in an apolitical manner. It is important that ownership of the financial statements and response to audit findings sits with the leadership of the body, whatever the delegation arrangements for practical purposes. The Auditor's Annual Report as proposed by the NAO provides the scope for a degree of flexibility in reporting. For example, detailed discussions could take place within the audit committee but the final VFM arrangements report might be presented for discussion at full council. This will depend on the governance arrangements at individual councils and the effectiveness of the audit committee's role within them. PSAA has developed the local audit quality forum as a vehicle to support the development of local audit committees and the sharing of good practice.
Q33. In your authority, what is the membership of the audit committee (number of members, how many are independent etc) and which officers typically attend?	This is a question for individual audited bodies.

Q34. How should local authorities track implementation of recommendations made by internal audit, external audit and relevant statutory inspectorates? What should the external auditors do if recommendations are not being implemented?	We would expect these matters to be tracked as a matter of course by the Audit Committee or other relevant body at an authority. Where recommendations (regardless of the issuer) are not being acted on the external auditor will need to consider if taking further action is appropriate. Options available include the powers within the LAAA 2014, and the proposed Auditor's Annual Report which provides a further public-facing opportunity to raise concerns. It would be possible for the NAO to provide more explicit guidance to auditors on the escalation process to be followed in the context of the new commentary.
Q35. Should there be a role for an external body in tracking action taken in response to modified audit opinions and/or statutory recommendations and public interest reports? If so should that responsibility sit with MHCLG, the sector specific oversight body recommended by the Independent Review of the Financial Reporting Council or another body?	It is the responsibility of the authority to take action in response to these matters. The proposed Code of Audit Practice specifically provides for the auditor's annual report to include *'details of any recommendations arising from the audit and follow up of recommendations issued previously, along with the auditor's view as to whether they have been implemented satisfactorily'.* Schedule 7 of the LAAA2014 provides that copies of public interest reports, and written recommendations made under schedule 7(2) commonly referred to as statutory recommendations are provided to the Secretary of State. In our view requiring another body to monitor the implementation of all recommendations would be excessive.

Chapter 8 - Financial Reporting Framework	
Q36. Do local authority accounts allow the user to understand an authority's financial performance and its financial resilience? If not, how could they be revised to be more understandable? What information could be presented to enable users of the accounts to understand whether the financial position of a specific LA is getting better or worse?	The accounts provide financial performance information (income statement) and also show the financial position at a point in time (balance sheet). The core financial statements will not show the financial resilience of an entity but the supporting information and notes alongside the financial statements should provide relevant information and detail. The narrative report should be a key part of the way that bodies provide information, and this could include analysis of the financial position. However, it is important to recognise that there may not be a consensus about the financial position. For example, it has not been unusual for local government bodies to increase available reserves in recent years, but if the long-term outlook is less positive then the question as to whether they are in a better or worse financial position may be disputed. The VFM arrangements commentary in the proposed Code could be used to set out future challenges, and the auditor's commentary could potentially consider and make reference to key financial projections and assumptions, etc. However, care needs to be taken to ensure that the commentary does not result in a new form of expectation gap as the auditor's work is likely to remain based on the adequacy of arrangements, not verified projections.
Q37. The UK Government is committed to maintaining IFRS based accounting for the UK public sector. Given this, how would you recommend resolving the mismatch between the accruals and funding basis to improve the understandability of local authority accounts?	We think that it is important local authority accounts should be IFRS-based. IFRS provides an internationally recognised basis for accounts preparation, enables a level of comparability across countries, and assures consistency within 'Whole of Government Accounts' thereby enabling bodies to discharge a significant duty. The dual bases (accruals and funding) adds to complexity. CIPFA has acknowledged the difficulties which this creates and its current Accounts Code consultation is beginning the process of exploring possible solutions. One possible option may be to decouple the accounts and have an IFRS accruals-based set of financial statements supported by a viability statement on the authority's funding position.

Q38. Do you think that summary financial information should be reported in the annual report section of the accounts? If so, on what basis and should this information be covered by the financial audit opinion?	If it is decided that summary financial information is to be produced then it would be preferable if it is within the narrative report rather than a separate document. A separate document would risk further undermining the importance of the financial statements. The summary financial statements would then be subject to the auditor's responsibilities under ISA 720, and effectively be a consistency check with the financial statements.
Q39. If you think that summary financial information should be reported in the annual report section of the accounts, should it be presented with performance information? If so, what performance information would be of most interest to stakeholders?	Our understanding is that the narrative report within financial statements should already include information on key performance indicators (KPIs). However, there does not seem to be a consistent application of this Accounting Code requirement. We think that CIPFA could strengthen the requirement, but, by definition, KPIs need to be seen to be relevant at the local level and should provide part of 'telling the story' in the local context.
Chapter 9 – Other Issues	
Q40. For larger authorities, does the inspection and objection regime allow local residents to hold their council to account in an effective manner? If not, how should the regime be modified?	The right of an elector to inspect wide-ranging aspects of an audited body's activities is a long-standing and important part of local democracy, along with use of the Freedom of Information Act, expenditure in excess of £500 being reported on websites, and social media providing scope for wider highlighting of concerns, for example, in relation to service delivery. Ideally though objections should not be the primary way of holding a council to account. Interactions with staff and members should resolve the majority of issues. The objections process provides a mechanism for when those interactions fail to do so, but is a costly process both in terms of audit costs and staff and other costs within the audited body. Our analysis set out below of 109 objections from April 2015 to June 2019 shows that very few result in formal action.

Outcomes of objections from 1 April 2015 to 30 June 2019

Outcome	Number	%
Public interest report (PIR)	1	1%
Auditor seeks a declaration (Auditors can apply to the court for a declaration that an item of account is contrary to law)	0	0%
Auditor makes Schedule 7 recommendation (Schedule 7 of the 2014 Act allows for the auditor to make written recommendations which place statutory requirements on an audited body)	1	1%
Auditor makes other recommendations (Auditors have a power under section 27 of the 2014 Act to make recommendations that do not place statutory requirements on the body. These may be used where the auditor wishes to bring a matter in respect of an objection to an audited body's attention, but where it may be disproportionate to require the body to put in place additional arrangements, and incur additional cost, to respond to the recommendation)	42	38%
Auditor takes no further action, having considered the objection	66	60%
Number of objections	109	

Source: PSAA analysis of objections 01/04/15 to 30/06/19

For the objections where the auditor did not use the available statutory actions (to issue a PIR, seek a court declaration, or make recommendations), the main reasons are set out below. In most cases more than one reason applied to each objection decision.

Cases where the auditor determined no further action was required

Outcome	Number
Auditor takes no action as authority action lawful and appropriate	58
Auditor takes no action as while expenditure may be unlawful discretion exercised not to apply to Court	18
Auditor takes no action as matter not considered to require a PIR	28
Auditor takes no action as while law is unclear it is not the role of the auditor to clarify	4
Objection beyond the auditor's jurisdiction (outside auditor's remit)	14

Source: PSAA analysis of objections 01/04/15 to 30/06/19

The range of issues covered by the objections in our analysis and the audit cost is set out below.

Subject matter of objections and audit costs

Category	Number	Total Audit Cost £
LOBO arrangements	24	407,498
Parking	14	188,597
Environment/waste	7	90,687
Planning	7	80,644
Transport	7	74,568
PFI and contracts	6	86,148
Legal expenses	5	85,347
Taxi licensing	3	45,818
Housing	2	19,181
Council tax benefit	2	28,435
Other	32	320,759
Total	**109**	**1,427,682**

The audit costs of objections are borne by the relevant local authority. The average cost of dealing with an objection is £13,098, although there is a wide range, with auditor costs ranging from £892 to £92,949 for individual objections. We have no record of authorities' costs, such as officer time and legal advice.

	We have also analysed the time taken by auditors to determine the objections from receipt to the date of the final outcome letter. It varies considerably, depending upon a number of factors. From the data held, the time taken has been between 25 days to 1,348 days, with an average time taken of 445 days. For those objections still being investigated, the average time taken from the date the objection was accepted to either 30 June 2019 or the date of the final outcome letter (if the objection has since been determined) is 717 days. There are 17 objections from 2015/16 outstanding, 24 from 2016/17 and 12 from 2017/18. We are currently finalising a short paper on the results of our work and will provide a copy to the review team. We welcome the proposals in the Code that there be quarterly auditor communication on progress on objections.
Q41. Is more guidance needed to help auditors assess the impact of significant changes to common business models? If so is this guidance needed to support the financial audit, the VFM audit or both?	Given that audited bodies are required to prepare IFRS-compliant accounts further guidance is unlikely to be required for the audit of the financial statements which should follow auditing standards. However, where audited bodies diversify into new business models there is often an impact on the accounting arrangements, and local audit teams are more likely to need to draw on the services of specialists either from within their firms or externally if there are complexities. This has an associated cost. The NAO will be developing AGNs for the VFM arrangements work, and could include guidance on considering commercial arrangements and partnership working.
Q42. Is the financial reporting and audit framework for larger category 2 authorities appropriate? If not, what additional information should be subject to audit/assurance and what would be the cost implications of this?	We consider it would be helpful if larger category 2 authorities were subject to extended audit/assurance procedures. The application of the Companies Act income and expenditure audit thresholds can mean that very large category 2 authorities can fall to be treated as principal authorities (requiring a costly full financial statements audit and VFM arrangements conclusion) if their expenditure exceeds £6.5m for two successive years. The use of extended procedures would enable appropriate assurance to be given on public expenditure but retain proportionality if the audit requirements were based on body type rather than level of expenditure.

Q43. For smaller authorities, does the inspection and objection regime allow local residents to hold their council to account in an effective manner and is the cost of processing and responding to objections proportionate? If not, how should the regime be modified?	We recognise that the costs of the inspection and objection regime for smaller authorities can be burdensome. It is not clear the extent to which objectors take into account the costs to their local authority when making an objection. Not only are there the costs of the auditor but also the hidden costs to the authority. Possible options for improvement include • pooling across all authorities; • encouraging auditors to use section 27(4) more widely; and • encouraging electors to use alternative access powers such as the Freedom of Information Act.