



Ministry of Housing,
Communities &
Local Government

Assessing the impact of changes to the local audit regime: scoping and baselining study

Final Report



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Any enquiries regarding this document/publication should be sent to us at:

Ministry of Housing, Communities and Local Government
Fry Building
2 Marsham Street
London
SW1P 4DF
Telephone: 030 3444 0000

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Preface

This report was completed prior to the change in name of the Department to the Ministry of Housing, Communities and Local Government (MHCLG). All references to DCLG should be read as MHCLG.

In April 2015, RAND Europe was commissioned by the Department for Communities and Local Government (DCLG) to undertake the baselining and scoping work for a possible future evaluation of the impact of reform of local audit in England. These reforms began in 2010 and included: the ending of the Audit Commission's inspection and assessment functions; the outsourcing of audits undertaken by the Audit Commission's in-house practice; the closure of the Audit Commission itself; the introduction of the Local Audit and Accountability Act 2014; and setting out the new local audit regime. This document provides the baseline data and methodology for a possible future evaluation.

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For more information about RAND Europe or this document, please contact:

Dr Christian van Stolk
RAND Europe
Westbrook Centre
Milton Road
Cambridge CB4 1YG
United Kingdom
Tel. +44 (1223) 353 329
Email: stolk@rand.org

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Summary

Background

1. **In April 2015, RAND Europe was commissioned by the Department for Communities and Local Government (DCLG) to undertake the baselining and scoping work for a possible future evaluation of the impact of reform of local audit in England.** This process of reform began in 2010 and included: the ending of the Audit Commission's (the Commission) inspection and assessment functions; the outsourcing of audits undertaken by the Commission's in-house practice; the closure of the Commission itself; the introduction of the Local Audit and Accountability Act 2014; and setting out the new local audit regime. The reforms relate to the audit of local public bodies – local authorities, fire authorities, Police and Crime Commissioners, clinical commissioning groups and NHS Trusts¹. Table 1 summarises this programme of developments, which are hereafter referred to as 'the reforms'. The prime focus of our report is on principal bodies, although reference is also made to the changes for smaller authorities.
2. **The research was not an evaluation of the reforms themselves, but provides a description of the baseline for use in any future evaluation.** Although large reductions in expenditure have been made, legislation passed and a new regulatory regime established, it is too early to draw any overall conclusions on their effects. For the purposes of this project we took 2009/10 as the baseline year. This was the last full year in which the Audit Commission was in operation prior to announcement of its abolition.
3. While this report only suggests a methodology for a potential future evaluation, the wider importance of conducting this evaluation should be also highlighted as well. Conducting the potential evaluation would not only allow for an investigation of whether the policy objectives of the reform have been fulfilled, but can also generate wider valuable insights into sector developments which can be helpful for decision-makers beyond measuring the reform impact. Conducting the evaluation requires consolidating data from different sources which might no longer be collected centrally and therefore provides a framework for a conversation around which actors should be responsible for collecting data which is of importance for wider sector steering and informing decision-makers beyond the purpose of the evaluation itself.

Research approach and baseline data

4. **Our research was undertaken between May 2015 and February 2016, and involved a number of methods for gathering data.** We reviewed relevant documents, developed a 'theory of change model' with officials from DCLG, undertook interviews with a range of stakeholders, analysed administrative and finance data, surveyed the finance directors of local public bodies affected by the changes, and interviewed partners of audit firms and other interested parties. Using 2009/10 as a baseline year presents methodological, practical and data challenges. For some aspects of our research, administrative and survey data for that year (or

¹ Foundation Trusts have been able to appoint their own auditors since their inception in 2004.

close) was available. In other cases – particularly where we are seeking opinions – we have used the best available data or have gathered views relating to the period of the most recent audit appointment. A list of indicators used is set out in the body of this report in Part 3.

Table 1: Timeline of the main developments

2010	End of the performance and inspection responsibilities of the Audit Commission
	Announcement of the abolition of the Audit Commission
2011	Decision to transfer all work previously undertaken by the Audit Commission's in-house Audit Practice into the private sector
2012	Award of five-year contracts to four firms
	Audit Commission staff transferred to private sector audit employers
2013	Audit Commission repackaged and tendered the remaining 30% of audit work already carried out by private firms
2014	Local Audit and Accountability Act 2014 received Royal Assent
2015	Closure of the Audit Commission on 31 March and opening of Public Sector Audit Appointments Limited
	National Audit Office and Financial Reporting Council take on new responsibilities
	Establishment of the Smaller Authorities' Audit Appointments Limited
2017	Start of new audit appointments regime for NHS bodies and smaller authorities
2018	Start of new audit appointments regime for principal bodies

Baseline and key issues for consideration in the potential future evaluation

5. **The Government set out a series of interconnected objectives for local audit reform designed to: secure greater local accountability and transparency; maintain competitive audit fees; save £1.35bn as part of the overall local audit reform programme; and uphold standards of auditing.**² In addition, these reforms fit with wider government objectives to 'deliver greater localism, decentralisation and transparency'.
6. The Department emphasised that the objectives for the reforms had evolved in the course of the passage of the Bill and early stages of implementation. The emphasis remains to maintain a high-quality audit regime at a lower cost than under the Audit Commission. However further discussion has underlined the importance of a flexible response to future procurement vehicles, as well as care to ensure that arrangements do not adversely affect smaller authorities and those bodies in less accessible parts of the country, which may be seen as less attractive to audit firms. These objectives have priority against a background of continuing public expenditure reductions.

Progress against objectives

Although implementation of the reforms is likely to continue until 2019, a number of the Government's objectives have already been met or are in progress at the time of the writing of this report. The Audit Commission closed in 2015 and its responsibilities transferred successfully to other bodies, leading to significant reductions in expenditure (according to DCLG's impact assessment, from almost

² DCLG. 2014 Local Audit and Accountability Act 2014: 'Local audit impact assessment'.

£249m to an estimated £87m in 2014/15).³ Following the transfer of staff from the Commission to private firms in 2012, statutory audit fees for 2012/13 audits were reduced by 40 per cent on 2011/12 levels for five years.⁴ Further retendering in 2014 of the remaining 30 per cent of work already carried out by private firms generated further savings. The Commission estimated these savings could amount to £440m between 2012 and 2020.⁵ Timetables for the ending of transitional arrangements and the introduction of local appointment in the different sectors have been agreed and work is currently under way to make the changes for NHS bodies and smaller authorities, followed the year after by principal bodies. A sector-led body for smaller bodies was established at the end of 2015⁶. Progress has been made towards aligning oversight of regulation of local audit with private company audit. The National Audit Office has taken over responsibility for the Code of Audit Practice and has fulfilled its role of reporting regularly on local service issues.

Fee levels

7. Most local bodies that took part in the online survey conducted for this project (see chapter 3.4.3 and detailed survey results in Appendix G) were happy with their most recent audit fee – 25 per cent of respondents considered it ‘completely appropriate’ and 69 per cent ‘acceptable’.⁷ Satisfaction levels with fees appear to be higher than in an Ipsos MORI survey conducted in 2008, although the results are not directly comparable.⁸ Amongst the audit firms interviewed for this project (see Appendix A for more details on the interviews conducted), there were mixed views about fee levels, some considering they had been ‘generally good’, but there was also concern amongst several firms that current levels were unlikely to be sustainable in the long run. Firms interviewed for this project considered they had made efficiency savings since the 2012 and 2014 procurements and further reductions in fees were seen as likely to lower the potential for ‘added value’ work.

Annual cost of the local audit regime

8. The total cost of the local audit regime in 2009/10 was £248.57m.⁹ This sum included the full range of Audit Commission responsibilities, several of which

³ DCLG Local Audit and Accountability 2014. 2014. ‘Local audit impact assessment’, p. 34.

⁴ House of Commons Research Paper 13/56, p. 10. Audit Commission (unpublished): ‘In the public interest: Lessons from the Audit Commission’s work for other public bodies and those receiving our functions’. Audit Commission 2013-4 work programme and scale of fees, p. 5.

⁵ Audit Commission (unpublished): ‘In the public interest: Lessons from the Audit Commission’s work for other public bodies and those receiving our functions’, p. 5.

⁶ In July 2016 Ministers announced that Public Sector Audit Appointments Ltd had been appointed as the sector led body for larger authorities audit procurement services from 1 April 2018.

⁷ Our survey was sent to 427 principal bodies from a list provided by DCLG – 354 in local government, 42 police bodies, and 31 fire and rescue authorities. It was sent by link in an email to a named senior financial officer. In addition, a slightly amended version of the survey was sent to 211 Clinical Commissioning Group (CCG) Finance Leads via the NHS England Finance Portal and to 90 Directors of Finance and Deputy Directors of Finance in NHS Trusts via TDA (including four part-year NHS trusts in 2015/16). The survey was finally closed on 28 February 2016. In total, we received 168 completed responses (a response rate of 23.2 per cent). For more details see Appendix A.

⁸ Ipsos MORI. June 2008. ‘Stakeholder perceptions of the Audit Commission’. Audit Commission archive.

⁹ DCLG Local Audit and Accountability Act 2014. 2014. ‘Local audit impact assessment’, p. 21-30.

subsequently ended altogether, so these economies have already been made, and was the figure at a time when only 30 per cent of the work was outsourced. Significant reductions in expenditure have since taken place and all audit work is now outsourced. The DCLG's Impact Assessment¹⁰, published in September 2014, sets out in detail how savings looking forward can be estimated and – based on the information from the Impact Assessment – this report (Part 5) indicates how costs and savings can be calculated when conducting the possible future evaluation.

Number of participating audit firms

9. In 2009/10, 30 per cent of the Commission's principal body audits were undertaken by five private sector firms, with the remainder of the work undertaken by the Commission's in-house practice.

Levels of satisfaction with audit services in recent years

10. Our survey of local public bodies,¹¹ conducted for this research, suggests that most authorities that responded were broadly satisfied with the audit service they had received in recent years. Some 75 per cent considered that the overall service was 'value for money', although 17 per cent did not. In particular, over 84 per cent were satisfied with their ability to contact and communicate with their auditors; with the extent to which the last audit plan was tailored to key risks; the timeliness of reporting; the practicality of report recommendations; and the 'usefulness' of reports.
11. Local public bodies were least satisfied with their ability to reduce the cost of external audit (67 per cent were completely or mostly satisfied). These figures would seem to broadly equate with levels of satisfaction identified in a survey undertaken in 2008 by Ipsos MORI for the Audit Commission (albeit there are limits to how far the surveys can be compared). The main areas where local public bodies would like to see improvements were a reduction in fee level and the 'time burden' associated with audit; greater emphasis on 'big picture' issues and less on detail; more risk-based audit; and more continuity in audit staff.

Technical quality of audit work in the baseline year

12. Overall, using data relating to 2009/10 audits, the Audit Commission considered that suppliers were meeting its regulatory requirements and standards of performance, and the requirements of professional auditing standards. More specific assessments are available for 2011/12 which combined regulatory compliance and audit quality performance scores. These rated two firms as 'Green' and three plus the Audit Commission as 'Amber' – levels considered acceptable. No firms were rated as 'Red'.

Views on the reforms raised by local bodies and audit firms

13. There was some uncertainty amongst both local bodies and audit firms about the reforms. This is unsurprising since they are still ongoing. There was little consensus

¹⁰ DCLG Local Audit and Accountability Act 2014. 'Local audit impact assessment'. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349418/2014_FINAL_Local_Audit_IA.pdf (accessed 1 April 2016).

¹¹ See Appendices for further details on research methodology and survey results.

as to whether local appointment would be valuable for audited organisations among the local bodies that responded to our survey. However, the majority (60 per cent) of respondents considered they would be well equipped to make an informed choice about their auditors (specifically, only five per cent of the respondents strongly disagreed that they would be well equipped, while 20 per cent neither agreed or disagreed and 15 percent somewhat disagreed). There were mixed views around plans for new contracting arrangements: 11 per cent of respondents envisaged going alone – ie appointing auditors themselves, 33 per cent expected to participate in a joint procurement exercise with others, 35 per cent envisaged using a sector-led body if it was established, and the remainder did not know. When asked whether they anticipated the reforms would improve the quality of the audit service received, 26 per cent thought it would, 52 per cent envisaged no difference and 19 per cent were unsure.

14. Amongst **the audit firms interviewed** for this project there was acknowledgement of the rationale for the changes even though many firms did not made public statements at the time of consultation on the Bill. There was a strong sense that the most important changes had already taken place when the Audit Commission's in-house practice had been outsourced in 2012, so that more recent changes were seen as continuation of a programme. There was preference for coordinated, sector-led arrangements and some concerns about the possibility of inefficiencies in transaction costs associated with multiple small procurements. There was also some scepticism as to whether major additional savings would now materialise. Firms were confident that none of them would allow standards to drop, but there was concern that further reductions in fees would lead to a reduction in their ability to 'add value'.

Views of audit firms on the changing regulatory regime

15. There was support among the firms for the change in regulatory responsibility. There were positive observations made about the Audit Commission and its staff (although several drew a distinction between pre-2012 and afterwards), although there was also criticism expressed by the firms in the interviews for what was seen as an overly bureaucratic and a 'box-ticking' approach, particularly latterly when the relationship was characterised as 'contract management' rather than a partnership. The National Audit Office (NAO) was seen to have started effectively in its new role and there were positive comments about the alignment of oversight and quality regimes under the Financial Reporting Council.

Views on the reforms raised by stakeholders

16. In our interviews we got the impression that when considering a major reform of practices, there could be an overall tendency for those involved to focus on risks rather than the anticipated benefits. A number of stakeholders nevertheless welcomed the opportunities for efficiencies that the changes have offered – for example, drawing local audit into the existing oversight and quality regimes for private firm audit under the Financial Reporting Council (FRC), or for extending the Code of Audit Practice to foundation trusts and so broadening the Comptroller and Auditor General's responsibilities around public audit as a whole. Some stakeholders also commented positively on the reduced costs and increased efficiencies associated with the contracting out of audit work since 2012. And the opportunities of sector-led bodies were also highlighted by several stakeholders, who saw them as a way of reconciling the benefits of more local control with value for money.
17. Stakeholders also identified a series of challenges to the success of the reforms. Some felt there had not been sufficient acknowledgement of the likely barriers to new entrants to the audit market. There was some concern about a possible loss of specialist skills in the sector; the risk of potential gaps in audit coverage in some remote areas and for smaller bodies; some concerns at fragmented responsibility for oversight as a result of a number of different bodies taking on roles from the Audit Commission; and acknowledgement that the NAO's role on value for money was more limited than that under the Audit Commission, and therefore its studies would need to be augmented by sector-led research and data collection such as the Local Government Association's (LGA) Local Government Inform service. A number of stakeholders also commented that, with the demise of the Audit Commission, there was no central collection of information on different aspects of local audit, and felt this raised an important issue of whether there remained the capacity to identify early warning signs of problems.

Smaller authorities

18. The main concerns raised during the research in connection with the 9,000 smaller authorities related to whether they would have sufficient purchasing power, whether audit standards and fee levels could be maintained, and whether the lighter-touch audit regime in place since 2003 would be retained. In December 2015, the Government announced a sector-led body for smaller authorities. All smaller authorities were to be included unless they opted out. The Smaller Authorities' Audit Appointments Limited (SAAA) announced that the company will formally appoint

external auditors on behalf of the authorities for a five-year period. The new arrangements were due to start from the financial year 2017/18.

Proposed methodology for a potential future evaluation

19. Part 5 of our report sets out the proposed methodology for a possible future evaluation. The questions to be addressed in this future evaluation are:

- What were the financial savings from the local audit reforms given effect to by the Local Audit and Accountability Act and were these in line with those projected in the impact assessment (and if not, what was the cause of change)?
- Did the changes improve the transparency of audit costs?
- Did the changes make the auditor appointment process clearer?
- Did the changes maintain transparency and standards of audit regulation?
- Is there a more accessible audit market and an increase in the number of audit providers?
- Have audit standards been maintained or improved, and not been compromised by local audit reforms?

Source: DCLG Research Specification

20. The proposed methodology involves a mixed-methods approach to capture both quantitative and qualitative evidence need to address the questions. The main elements are:

- **Document review** – in order to secure an updated picture of developments since this report, it will be important to review official documents from key participants in the audit processes.
- **Review of administrative data and data trends** – including the number of firms involved in local audit, cost of the local audit regime, the number of objections by local electors, the number of Public Interest Reports (PIRs), audit quality data, etc.
- **Analysis of the cost of the audit regime** – examining expenditure trends over the period of transition and validating the elements of the costs in the framework set out originally in the Impact Assessment. These include audit fees, costs incurred by local bodies, but also regulatory costs including those of the NAO and FRC. Attempts should also be made to identify compliance costs within authorities.
- **Local public body survey** – a possible future evaluation should rerun the survey of local public bodies used in 2015/16, making any adjustments for developments in the interim. This will allow the evaluators to compare how perceptions of senior finance officers within local authorities have changed over time.
- **Interviews with partners of audit firms** – we recommend that interviews with relevant partners at each of the participating firms are repeated, using similar questions to those used in 2015/16. This will allow the evaluator to gauge changes in views on audit arrangements and on the regulatory regime.

- **Interviews with other stakeholders** – the evaluation should include interviews with relevant individuals within stakeholder bodies such as the NAO, FRC, LGA, the Institute of Chartered Accountants in England and Wales (ICAEW) and the Chartered Institute of Public Finance and Accountancy (CIPFA).
- **Case studies of the audit of local bodies** – to supplement data collection and enable the evaluator to probe the reasons for changes, we suggest local case studies.
- **Comparison with other nations' audit arrangements** – brief comparisons with developments over the same period in Scotland, where the Accounts Commission has remained in place, and in Wales, where the Auditor General of Wales audits most public bodies, could add insight into English developments.

Practical challenges for a potential future evaluation

21. **It is for DCLG and the Department of Health (DH) to decide when, if appropriate, to commission an evaluation, but we consider it could not be completed until there has been at least one year of audits for all bodies under the new arrangements.** This means that a more complete evaluation would be unlikely until early 2020. There are, however, merits in collecting some data in advance of that, in order to validate expenditure in the interim years, undertake some interviews, and examine progress with NHS bodies and smaller authorities in advance of looking at principal bodies (which begin local appointment a year later).
22. **In comparing the cost of local audit between the baseline year and the point at which the evaluation takes place, future evaluators will need to take account of changes in the environment in which audit is conducted.** These changes include:
 - **Major changes in the functions undertaken relating to local audit.** The Audit Commission had five main functions in 2009/10. Several of these responsibilities were ended or transferred to other bodies. Thus, there will be a noticeable difference in the extent of audit activity undertaken at the point of the evaluation compared with the baseline year.
 - **Significant changes in context in local government, police, fire and rescue and NHS over the period.** These will include smaller budgets for local public bodies, transformational change and redesign, as well as demographic changes including immigration and the ageing of the population. In the case of local government, there will be a substantial change in the 'balance of funding', including localisation of business rates and reduction in central government grant. Smaller budgets could affect the quality of financial management in place, increasing the risk of financial control problems and possibly increasing the amount of auditor effort required.
 - **Changes in the technical and professional requirements on auditors.** These will include the bringing forward of local audit timetables, and technical accounting changes. These may impact on the audit and how it is conducted, although have nothing to do with the reforms themselves.

23. **DCLG still need to consider the feasibility of, and responsibility for, collecting certain data at a national level, which will be important to support any future evaluation.** This data include fee levels for each principal authority, a complete list of public interest reports and qualifications of accounts, and number of elector objections, etc. In some cases, should a decision be made not to collect the data centrally, the evaluators may be able to collect the data themselves. However, it also suggests that the evaluation should examine carefully whether data gaps are having an effect on the ability of Government to identify signs of systemic failure and poor value for money within local bodies.
24. **The proposed evaluation should start with an evaluability assessment to ensure that adequate evidence is available** to allow all the issues to be examined and agreement reached with the client if elements of the research need to be scoped out.

1. Background to this project and the reform of local audit

1.1 Background to this project

25. The following sections set out the purpose of this project, the research methodology used for conducting this project and the structure of the wider report.

1.1.1. Purpose of this project

26. This project examines the local audit reforms that were initiated from 2010 onwards, and included the Local Audit and Accountability Act 2014. These reforms relate to the audit of local public bodies – local authorities, fire authorities, Police and Crime Commissioners, clinical commissioning groups and NHS Trusts¹² – and apply to England only. The project was commissioned by the Department for Communities and Local Government (DCLG) in April 2015. The purpose of the work was to capture and record the baseline data necessary for a possible future evaluation of the reforms, and to develop the methodology for this evaluation. The work also included development of a Theory of Change (ToC) for the reforms and clarified the assumptions sitting behind the policy changes.
27. The work has been undertaken on the assumption – in keeping with commitments made to Parliament during the passage of the 2014 Act – that there could be a potential formal post-implementation evaluation. A final decision on the timing and focus will be for officials at DCLG, but a probable date (discussed later) is around 2019/20, once all elements of the changes have had at least a year to take effect. The DCLG’s Research Specification stated that the likely research questions to be answered in this evaluation will be:

- What were the financial savings from the local audit reforms given effect to by the Local Audit and Accountability Act and were these in line with those projected in the impact assessment (and if not, what was the cause of change)?
- Did the changes improve the transparency of audit costs?
- Did the changes make the auditor appointment process clearer?
- Did the changes maintain transparency and standards of audit regulation?
- Is there a more accessible audit market and an increase in the number of audit providers?
- Have audit standards been maintained or improved, and not been compromised by local audit reforms?

Source: DCLG Research Specification

¹² Foundation Trusts have been able to appoint their own auditors since their inception in 2004.

1.1.2. Research approach used for this project

28. Our research was undertaken between May 2015 and February 2016, and involved a number of methods for gathering data and information. A more detailed overview of the research approach used for this project can be found in Appendix A.

Document review and data analysis

29. We undertook a focused literature review relating to the reforms. The rationale behind the changes to the local audit regime has been set out in a number of policy documents since the announcement was made in August 2010 to abolish the Audit Commission and to transfer the audit of local public bodies to the private sector. In addition, we reviewed relevant third party literature (e.g. practitioner literature, academic coverage, etc.). We gathered and analysed relevant administrative and finance data. This included material produced by the Audit Commission itself, the LGA, CIPFA, ICAEW, NAO and Public Sector Audit Appointments Limited (PSAA).

Theory of Change workshop

30. On 8 June 2015, we held a workshop with key DCLG officials to develop the Theory of Change (ToC) which underpins the local audit reform. A draft ToC diagram, based on our initial document review, was used as the basis for workshop. Eight members of DCLG officials were involved, including a number who had been involved in discussions about the policy reform throughout its life. The ToC – prepared by RAND Europe and discussed and refined with the help of DCLG policy staff – sets out how a number of activities are expected to lead to the achievement of the desired objectives. It also identified a series of indicators that can be used to track whether these objectives have been accomplished.

Interviews with stakeholders and audit firms

31. Semi-structured interviews were conducted between July 2015 and February 2016 with a number of stakeholders (13 interviews with stakeholders, 7 interviews with audit firms, see also Appendix A) affected by, or with an interest in, the reforms. We undertook interviews with a range of stakeholders other interested parties, and interviewed the partners/directors leading the audit of local public bodies' work.

Survey of finance directors of local public bodies affected by the changes

32. To complement existing secondary/administrative data, we developed a baseline survey of local public bodies to gather information on their recent audit arrangements and their views on the pros and cons of changes. This was designed to help us establish a baseline position for local public bodies' views on their audit arrangements prior to the changes. Whilst these views were not gathered during the baseline year, in many cases the current auditors had been in place for some years. Our survey was drawn up based on our literature review and following a number of interviews with stakeholders and we worked closely with DCLG to develop the content of the survey. The survey was launched in November 2015 using RAND Europe's Select Survey tool. The survey was finally closed on 28 February 2016. In total, we received 169 completed responses (a response rate of 23.2 per cent – for

more details on how the survey was conducted including detailed results and efforts undertaken for increasing response rate see also Appendix A and G).

1.1.3. Outline of this report

33. This report is the final output from the RAND Europe research project and brings together, and adds to, material contained in two interim reports. Its purpose is to describe the basis for a possible future evaluation of the local audit reforms. The report is structured as follows:

Part 2: Theory of Change for local audit reform – this part summarises our analysis of the theory of change behind the changes, which is provided in more detail in Appendix C.

Part 3: Baseline data and description for a potential future evaluation – this part summarises and discusses the key data sources which provide the baseline information needed for a future evaluation.

Part 4: Issues for consideration in a potential future evaluation – this part sets out a series of further issues which a future evaluation will need to take into account.

Part 5: Methodology for a potential future evaluation – this part proposes the methodology for the future evaluation.

1.2. Background to the reform of local audit

1.2.1. Development of local audit arrangements

34. Within a democracy, there is a strong interest in understanding how public bodies use the resources made available to them, and in particular, whether they use them with due regard for regularity and propriety, as well as value for money (VfM). From 1983 to 2015 the Audit Commission (the Commission) was responsible for overseeing the audit of local public bodies in England (and Wales until 2004). The Commission's responsibilities included appointing local auditors, and for some years it outsourced 30 per cent of the work by value, the remaining 70 per cent being carried out by its in-house practice.¹³ The Commission also gathered data and reported on the value for money of local public spending and had powers to look at 'best practice' across groups of bodies. The Commission was also responsible for preparing, and keeping under review, Codes of Audit Practice, which set out how auditors were to carry out their functions.
35. In 2015 (the year in which the Commission was abolished) the 11,000 public bodies were responsible, between them, for £200bn of public expenditure per year. Of the 11,000 public bodies, around 800 were designated 'principal' bodies – including 353 local authorities, 263 National Health Service (NHS) bodies, 76 police authorities and 82 other bodies including fire and rescue authorities and national park bodies. The remaining 10,000 were 'smaller bodies', with turnovers below £6.5m.¹⁴

¹³ Duncan Campbell-Smith. 2008. *Follow the Money: A History of the Audit Commission* states the 70/30 split was unchanged for around 25 years. Appendix 6 provides a summary of private firms' share of audit work.

¹⁴ DCLG. 2013. 'Local Audit and Accountability Bill: A Plain English Guide'; (2014) 'Local Audit and Accountability Act: local audit impact assessment'. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349418/2014_FINAL_Local_Audit_IA.pdf (accessed 1 April 2016).

1.2.2. Local audit arrangements in 2009/10 (baseline year)

36. A possible future evaluation of local audit reform will want to compare arrangements as they existed in the designated baseline year and at the time of the evaluation. In any comparison between the two points, it will be essential to establish the full range of activities undertaken – the total ‘value’ that was secured from audit work – for the resources expended. To allow this to happen, we start with a description of arrangements as they stood in 2009/10, the final full year of operation of the Audit Commission prior to the reforms (for further discussion of the baseline year, see section 3.2).¹⁵
37. The DCLG’s impact assessment stated in that year the Commission had **five main functions**.¹⁶ These were:
- Overseeing local public audit as regulator, commissioner and provider of local external audit services.
 - Making arrangements for certifying claims and returns in respect of grants or subsidies from Government departments.
 - Undertaking assessment and inspection of various local bodies (e.g. Comprehensive Area Assessments) in education, social care, housing and benefit fraud.
 - Undertaking or promoting VfM and research studies, including to improve financial management of health service bodies and local government bodies.
 - Conducting data matching exercises in order to assist in the prevention and detection of fraud, through the National Fraud Initiative.
38. The core business of the Audit Commission was to **appoint auditors** to give their professional opinion on the financial accounts presented by councils, police, fire and rescue authorities and NHS trusts. To audit these bodies the Commission either appointed a qualified individual employed within the Commission’s own in-house practice or one of the audit firms with which it contracted at the time: Deloitte, KPMG, PKF, Pricewaterhouse Coopers and Grant Thornton.
39. The Audit Commission also undertook **VfM work** in which it rated how well local bodies commissioned services, took decisions and handled natural resources, assets and people. Auditors gave councils scores on how well they performed on their use of resources, as well as evaluating the VfM performance of Primary Care Trusts. The Commission produced a series of studies during the year, including on how councils could cope with financial pressures; on fraud against council tax; on spending on the health of children under five; and on the financial effects of ageing.
40. As part of its **comparative work**, the Commission also produced an interactive tool for Primary Care Trusts to check their value for money profiles and an online tool showing comparative financial ratios to assess the financial performance of councils. It produced a ‘National Benchmarker’ tool for health information. The Commission also worked with HM Inspectors of Constabulary (HMIC) to assess police authorities. The Commission led work on **Comprehensive Area Assessments** involving six

¹⁵ Information drawn from Audit Commission annual report and accounts 2009/10; DCLG’s Local Audit and Accountability Act 2014: Local audit impact assessment (2014).

¹⁶ DCLG’s Local Audit and Accountability 2014: Local audit impact assessment (2014).

public-service inspectorates to provide overall assessments of public services in each local area. These were designed to help residents to hold to account councillors and others commissioning and providing services.

41. During the year, the Audit Commission also undertook a **number of other related activities** as part of its wider role in respect of local audit. In particular:

- It consulted on the five-yearly update of the audit Codes of Practice, which secured parliamentary approval in March 2010.
- Made representations to Government asking for amendments to statutory requirements for the approval of accounts to allow for timelier financial reporting.
- Supported the ongoing transition of public bodies to International Financial Reporting Standards, which created new rules for how bodies treat transactions and value assets, and on disclosure.
- Under the National Fraud Initiative, brought together public data to flag anomalies for investigation, which councils and other bodies used to detect fraud, error and overpayment
- Reviewed data assurance in the NHS to help trusts ensure the integrity of clinical performance assessment.
- Monitored and reported on the quality of audit undertaken by its in-house practice and suppliers.¹⁷
- Provided guidance to auditors in undertaking their duties.
- In response to continuing serious problems in Doncaster, the Commission undertook a corporate governance inspection and reported to the Secretary of State, who introduced measures for improvement.
- Reported publicly on the overall results of auditors' work on financial statements, summarising key findings and trends.¹⁸

1.2.3. Understanding what 'value' the Audit Commission provided

42. Against this background, it is clear that prior to its abolition, the Audit Commission was seen by many stakeholders (including contracted audit firms and local public bodies) as providing more than simply a statutory audit function, but also engaging in a wider range of assurance, research and benchmarking activities. The abolition of the Commission led to the ending of a number of activities, which have (through policy choice) not been replaced, as well as the dispersal of other powers to other organisations including the NAO and the Cabinet Office.

43. These activities were nevertheless seen by some stakeholders to have some 'value' (see Parts 3 and 4). For example, it was observed by stakeholders we interviewed that the Audit Commission:

¹⁷ 'Audit practice annual quality report 2009/10'. 'Quality review programme: Annual Report 2010'. Online: <http://collections.europarchive.org/tna/20121114095218/http://audit-commission.gov.uk/aboutus/publications/pages/corporate-papers-archive.aspx> (accessed 1 April 2016).

¹⁸ Auditing the accounts 2009/10. 'Councils and local government bodies, police and fire and rescue authorities'. Online: <http://collections.europarchive.org/tna/20121114095218/http://audit-commission.gov.uk/aboutus/publications/pages/corporate-papers-archive.aspx> (accessed 1 April 2016).

- Provided a national overview of developments in the key sectors that it oversaw, which no longer exists.
 - Provided insights into systemic themes through its national reports, which local bodies were able to draw on when considering their own position.
 - Gathered and made available benchmarking data, which was used by the sectors.
 - Had in one place a team of experts, which has now been dispersed.
 - Had 30 years of accumulated knowledge and memory of the issues facing local public bodies and around accountability considerations, which is no longer available.
44. Whilst acknowledging that the value of these features is hard to quantify, and that in making its choice to abolish the Audit Commission, such considerations are likely to have been taken into account, nevertheless we consider that any future evaluation of the impact of the reforms must consider what ‘value’ has been lost through the changes, as well as the extent to which – if at all – replacement arrangements have filled the gaps. This is particularly relevant to whether standards of audit in the widest sense have been maintained, which we consider is more than a matter of technical compliance with audit requirements.

1.2.4. Changes to the local audit regime after 2010

45. Changes to audit arrangements were initially announced in the summer of 2010 by the Coalition Government. Further developments took place during the following years, leading to the Local Audit and Accountability Act 2014. The key changes prior to passage of the Act are set out in Table 2 (below).

Table 2: Key changes to local audit regime prior to the Local Audit and Accountability Act 2014

Date	Key change
June 2010	The Government ended the performance and inspection responsibilities of the Audit Commission, including the Comprehensive Area Assessments. The Use of Resources Assessments also ceased so that audit work was scaled back to more limited procedures supporting a more straightforward, binary conclusion on whether or not proper arrangements were in place.
August 2010	The Department for Communities and Local Government announced changes to the audit of local public bodies in England. This included the decision to abolish the Audit Commission as part of its programme of closures of a number of non-departmental public bodies.
2011	The Government decided to transfer all the work previously undertaken by the Audit Commission’s in-house Audit Practice into the private sector.
April 2012	The Audit Commission announced the award of five-year contracts to four firms. Separate arrangements were announced for the 9,800 smaller local public bodies.
November 2012	Around 700 Audit Commission staff transferred to private sector audit employers and the Audit Practice closed.
April 2013	The Audit Commission repackaged and tendered the remaining 30% of audit work that was already being carried out by private-sector firms.

46. The impact of these changes has already been seen. In particular, it has been estimated that outsourcing of audit work, ending of assessment and inspection functions, slimming down of the Audit Commission prior to closure, and efficiency programmes led to reductions in expenditure from £248.57m to £86.98m.¹⁹ These reductions over the five-year period of contracts allowed the Commission to reduce audit fees for local bodies by up to 40 per cent on 2011/12 levels.

1.2.5. Key changes under the Local Audit and Accountability Act 2014

47. **The Local Audit and Accountability Act 2014 (which received Royal Assent on 30 January 2014) implemented major reforms** to the audit of local public bodies in England. The legislation fulfilled the coalition government's expressed desire to 'radically scale back centrally imposed, bureaucratic and costly inspection and auditing'.²⁰ In particular, the Act:

- Provided for the previously announced abolition of the Audit Commission.
- Set out the new audit regime for local public bodies, including transitional arrangements, and the arrangements for smaller bodies.
- Distributed certain functions of the Audit Commission to other bodies, including giving responsibility for issuing the Code of Audit Practice (governing how auditors conduct their work) and supporting guidance to the NAO; making the FRC the overall regulator of audit standards for both the statutory and local audit regimes; and designating the professional accountancy bodies with putting in place eligibility rules.

48. In its 2014 impact assessment, DCLG gave five reasons for reforming local public audit. These were: a lack of local accountability as a commissioner of audit services, which meant that local bodies had very little influence over who their auditor was or what they paid for that service; a lack of transparency and incentives to drive down costs of audit as a result of the Commission charging for its own corporate costs and inspections; local bodies funding wider non-audit activities over which they had no control; duplication across regulatory regimes; and because it believed there was no inherent justification for the public sector to be the main provider of local public audit.²¹ The Government also considered that the existing arrangements with the Audit Commission as regulator, commissioner and provider of local audit services, inefficient and unnecessarily centralised. The Commission's remit and functions were described as having expanded a lot beyond what had been originally intended,

¹⁹ DCLG Local Audit and Accountability 2014: 'Local audit impact assessment' (2014, 34).

²⁰ DCLG announcement, 13 August 2010. 'Eric Pickles to disband Audit Commission in new era of town hall transparency'. Online: <https://www.gov.uk/government/news/eric-pickles-to-disband-audit-commission-in-new-era-of-town-hall-transparency> (accessed 1 April 2016).

²¹ DCLG Local Audit and Accountability Act: 'Local audit impact assessment'. 2014. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349418/2014_FINAL_Local_Audit_IA.pdf (accessed 1 April 2016).

and its multiple roles to have 'created a system with weak cost incentives that became too focused on reporting to central government rather than to local people'.²²

49. Against this background, the Government stated that it believed that ending state provision of local audit services and increasing competition in the market would deliver greater value for money.²³ In particular, it stated that the objectives of the reform were designed to:
- Secure greater local accountability and transparency.
 - Maintain competitive audit fees.
 - Save £1.35bn as part of the overall local audit reform programme already underway.²⁴
 - Uphold standards of auditing.
50. By implication, the government has indicated that it is keen to develop a diverse and competitive market for local audit service providers.²⁵
51. During the course of the research, officials from DCLG also highlighted that the wider objectives of the reforms were also 'to deliver greater localism, decentralisation and transparency'.²⁶ This can be seen, for example, in the objective of moving from central to local appointment of auditors.
52. DCLG also emphasised to us that the objectives for the reforms had evolved in the course of the passage of the Bill and early stages of implementation. The emphasis remains to maintain a high quality audit regime at a lower cost than under the Audit Commission. However further discussion has underlined the importance of a flexible response to future procurement vehicles, as well as care to ensure that arrangements do not adversely affect smaller authorities and those bodies in less accessible parts of the country, which may be seen as less attractive to audit firms. These objectives have priority against a background of continuing public expenditure reductions, whilst the Department indicated that additional concerns to widen the number of audit firms in the market was of lower priority [Interview 11].

1.2.6. Timeline for further changes

53. Reforms to local audit arrangements are being introduced on a staged basis, with different changes coming in, potentially over four to five years. It is now clear that elements of the reforms are being introduced to slightly different timetables in different parts of the public sector; for example, the last year of transitional

²² DCLG Local Audit and Accountability Act: 'Local audit impact assessment'. 2014. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349418/2014_FINAL_Local_Audit_IA.pdf (accessed 1 April 2016). p. 1.

²³ DCLG. 2014 Local Audit and Accountability Act 2014: 'Local audit impact assessment'.

²⁴ DCLG. 2014 Local Audit and Accountability Act 2014: 'Local audit impact assessment'. The figure of £1.35bn is taken from the DCLG's impact assessment (2014) and is the estimated net benefit over the ten-year period from 2009/10. It includes reductions in annual costs of the audit regime and factors in transitional costs over the period.

²⁵ This objective, while not explicitly listed in the reform plan, is stated throughout documents describing the local audit regime change such as the Local Audit and Accountability Act 2014: 'Local audit impact assessment'.

²⁶ House of Lords Grand Committee on the Local Audit and Accountability Bill (26 June 2013).

arrangements for smaller authorities and NHS bodies is a year before those for principal bodies. Table 3 summarises the timeline following passage of the 2014 Act.

Table 3: Key dates in implementation of local audit reform after Local Audit and Accountability Act 2014

April 2015	National Audit Office and Financial Reporting Council begin to take on regulatory responsibilities Public Sector Audit Appointments Limited established as transition body for contracts to run remaining years, taking over responsibility previously discharged by the Audit Commission
December 2015	Establishment of the Smaller Authorities' Audit Appointments Limited
2016/17	Last year of transitional arrangements for NHS bodies and smaller local government bodies. New appointment regime starts 1 April 2017
2017/18	Last year of transitional arrangements for principal local government bodies. New appointments regime starts 1 April 2018
2018	The monitoring of audits by the Audit Quality Review team of the Financial Reporting Council will begin in respect of financial years ending 31 March 2018

1.2.7. Key developments during 2015/16

54. During the course of our research, aspects of the reforms continued to be implemented and new announcements were made. In particular, the main developments are set out in Table 4. Particularly significant was the establishment of new regulatory arrangements. Under the new arrangements, local bodies appoint private-sector audit firms, which must be registered with a Registered Supervisory Body (RSB) which has been recognised for local audit, and be subject to regulation by that body. In June 2014, the Government laid an Order before Parliament that delegated to the FRC most responsibilities for oversight of the regulation of auditors of local public bodies by RSBs. These powers took effect in August 2014. The FRC has been delegated three specific responsibilities – make regulations on the transparency report that auditors of major local bodies are required to publish each year; makes regulations on the keeping of the Register of Local Public Auditors; and give statutory guidance to RSBs on the level of competence and experience required for approval of those individuals within a firm who are able to sign an audit opinion on behalf of the firm. To date, ICAEW and the Institute of Chartered Accountants of Scotland (ICAS) have been recognised as RSBs for local audit from 1 November 2015, and CIPFA as a Recognised Qualifying Body from 1 October 2014.²⁷ This has involved processes of assessment to understand whether these bodies are capable of fulfilling these roles in respect of local audit.

²⁷ Financial Reporting Council. Local Audit. Online: <https://www.frc.org.uk/Our-Work/Conduct/Professional-oversight/Local-Audit.aspx> (accessed 1 April 2016).

Table 4: Developments during 2015/16

Date	Development
April 2015	National Audit Office issued new Code of Audit Practice. ²⁸
July 2015	Public Sector Audit Appointments Limited issued its 'Report on the results of auditors' work 2014/15: NHS bodies'. ²⁹
October 2015	Secretary of State for Communities and Local Government decided to extend the transitional arrangement for principal local government bodies to 1 April 2018. Once the transitional audit arrangements come to an end, local public-sector bodies will have the power to appoint their own auditors. ³⁰
December 2015	Announcement of the appointment of Smaller Authorities' Audit Appointments Limited as the sector-led body for smaller local authority audit appointments. ³¹
December 2015	The Chartered Institute of Public Finance and Accountancy published 'Guide to Auditor Panels'. ³²
December 2015	Public Sector Audit Appointments Limited issued its 'Report on the results of auditors' work 2014/15: Local government bodies'. As in previous years, this concluded that against the background of financial challenges the sector was working hard to achieve appropriate standards in its stewardship of resources. ³³

55. In addition, the NAO, headed by the Comptroller and Auditor General, the auditor for central government, took over responsibility for preparation, publication and maintenance of the Code of Audit Practice. This sets out what local auditors are required to do to fulfil their statutory responsibilities under the Act. The Comptroller and Auditor General can also issue guidance to auditors which may explain or supplement the provisions of the Code of Audit Practice. The Act also allows the Comptroller and Auditor General to examine the economy, efficiency and effectiveness with which local authorities and other local public bodies use their resources, providing evaluation, commentary and advice of a general nature rather than examining specific authorities. These complement the NAO's work in helping to hold central government to account.³⁴

²⁸ National Audit Office. 2015. 'Code of Audit Practice'. Online: <https://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2015/03/Final-Code-of-Audit-Practice.pdf> (accessed 1 April 2016).

²⁹ Public Sector Audit Appointments. 28 July 2015. News release. Online: <http://www.psa.co.uk/wp-content/uploads/2015/07/PSAA-press-release-Report-on-the-results-of-auditors-work-2014-15-NHS-bodies.pdf> (accessed 1 April 2016)

³⁰ Local Government Association. 2016. 'Preparations for new appointment arrangements'. Online: www.local.gov.uk/web/guest/external-audit/-/journal_content/56/10180/7534520/ARTICLE (accessed 1 April 2016).

³¹ DCLG. 2015. 'Announcement of sector led body for smaller local authority audit appointment'. Online: <https://www.gov.uk/government/publications/announcement-of-sector-led-body-for-smaller-local-authority-audit-appointment> (accessed 1 April 2016).

³² CIPFA. 2015. 'Guide to Auditor Panels'. Online: www.cipfa.org/policy-and-guidance/g/guide-to-auditor-panels-pdf (accessed 1 April 2016).

³³ PSAA. 2015. 'Report on the results of auditors' work 2014/15: Local government bodies'. Online: <http://www.psa.co.uk/wp-content/uploads/2015/07/PSAA-press-release-Report-on-the-results-of-auditors-work-2014-15-LG-bodies.pdf> (accessed 1 April 2016).

³⁴ NAO. 2014. 'Local audit'. Online: <https://www.nao.org.uk/about-us/our-work/local-audit/> (accessed 1 April 2016)

1.2.8. Arrangements for smaller authorities

56. Some 9,000 bodies are classified as 'smaller authorities' or 'smaller bodies'. These are a very diverse range of bodies and include councils as large as Shrewsbury Town Council, with a budget of £3.5m, through to small parish councils, parish meetings and internal drainage boards. A smaller authority is an authority that has gross annual income or expenditure (turnover) below £6.5 million for three years running, including those 'exempt authorities' with a turnover below £25,000.³⁵ They have been subject since 2002/03 to a 'limited assurance' audit regime.
57. Under the new arrangements, bodies with an income and expenditure under £6.5m are required to undergo a 'limited assurance review' of their accounts, with a report by the auditor on the authority's financial return, rather than a full-scale audit. Those smaller authorities below the £25,000 threshold for income and expenditure ('exempt' authorities) will only need to comply with the publication requirements of the Transparency Code for smaller authorities. They will not need to hold an audit or limited assurance review, but must prepare a statement of accounts. The aim is to prevent very small bodies from what was considered an undue reporting burden. A smaller authority's right to exemption does not apply if the auditor has made a PIR, made a recommendation to the authority or declared an item unlawful. In December 2015, the Government announced that the Smaller Authorities' Audit Appointments Limited (SAAA) has been established under the Local Audit (Smaller Authorities) Regulations 2015. At the time we finalised this report, the chair and two other independent members were in place and work was under way to prepare for issuing an Official Journal of the European Union (OJEU) notice in April 2016. The SAAA had begun to issue letters from the chair with information and guidance to councils.
58. Following discussions with DCLG, we have not considered smaller authorities in detail in our research, and in particular, we did not survey them given the need to avoid overburdening small bodies. We have, however, identified a number of issues in Part 3 for follow up in any future evaluation, which reflect points made to us by a number of stakeholders.

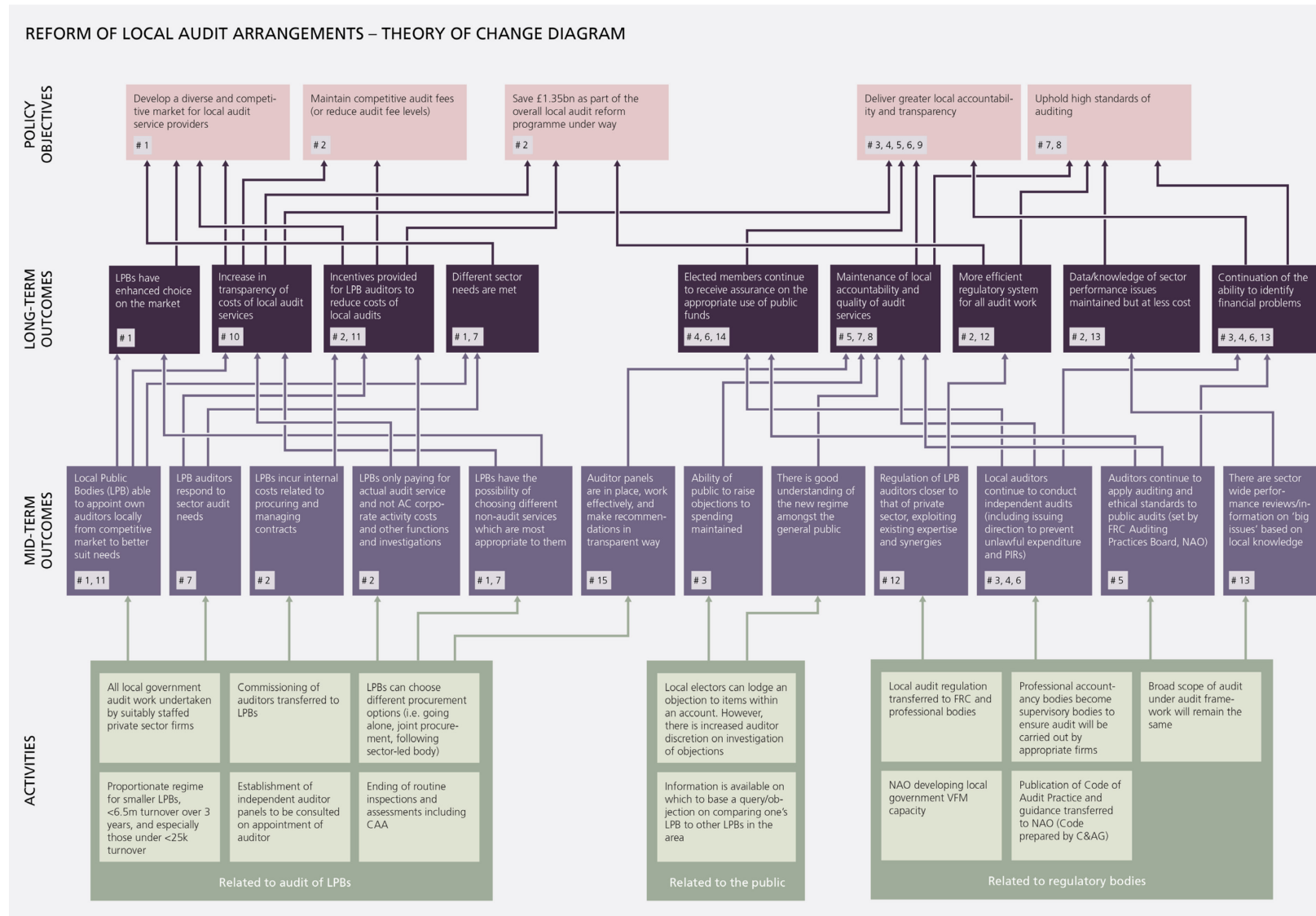
³⁵ DCLG. 2015. 'Changes to the smaller authorities' local audit and accountability framework: a guide'.

2. Theory of change for local audit reform

2.1. Using a Theory of Change approach

59. This section of the report illustrates diagrammatically (Figure 1) and in narrative form, the Theory of Change (ToC) underpinning local audit reform. A ToC approach helps an organisation to identify what it wants to achieve through a given initiative, and the steps it needs to take in order to achieve it. The ToC sets out the building blocks for delivering policy objectives, and makes explicit the range of assumptions (or underlying logic) which can lead to desired results. Using a ToC approach meant that we could:
- Gain a better understanding of the original purposes of the changes and the assumptions DCLG used to inform its reform programme.
 - Clarify the strategic vision for the future, both short-term and long-term, of the audit of local public bodies.
 - Identify how the reforms can achieve this vision, and how the evaluations will help to support putting this framework in place.
 - Identify the indicators that can be used to assess the extent to which reforms have achieved what was intended.
60. The ToC diagram later in this section of the report illustrates the **key policy objectives** of the reform of the local audit regime; the **long-term and medium-term outcomes** that need to be accomplished for the objectives to be fulfilled; and the **related activities** undertaken as a part of the reform, which are designed to secure the outcomes. Overall, we have divided the **key policy objectives of the audit regime reform** into two main categories:
- Those related to the conduct of audit within local public bodies.
 - Those linked to the regulation of the audit regime.
61. The first three objectives (top row, from the left in the ToC diagram) relate to the first category while the last two policy objectives (top row on the right) to the second category.

FIGURE 1: REFORM OF LOCAL AUDIT ARRANGEMENTS - THEORY OF CHANGE DIAGRAM



2.2. Overview of the Theory of Change diagram and indicators

2.2.1. Elements of the ToC: long-term policy objectives, related outcomes and activities

62. Figure 1 is the ToC diagram, developed initially by RAND Europe and based on our literature review and in particular our examination of Government statements of its objectives for local audit reform. It was subsequently discussed and refined with DCLG policy officials during a workshop in June 2015, and over the course of this research. A more detailed discussion of the various element of the ToC is at Appendix C.
63. Described below are the stated policy objectives, the expected mid-term and long-term outcomes that need to be achieved in order to secure these objectives and the related activities being carried out in order to achieve outcomes and objectives. Firstly, we will describe those policy objectives and related outcomes which link to the conduct of audit within local public bodies (policy objectives 1-3, left half of the ToC diagram). Secondly, those policy objectives and related outcomes linked to the regulation of the auditors and the audit regime will be described (policy objectives 4-5, right half of the ToC diagram).

2.2.2. Policy objectives and long-term outcomes related to the conduct of audit within Local Public Bodies

64. **Policy objective 1: Develop a diverse and competitive market for local audit service providers.** This objective, while not explicitly listed in the reform plan, is implicit in various documents describing the local audit regime change and appears of high importance.³⁶ The achievement of such a state is conditional on a set of **long-term outcomes** (see ToC diagram):
- Opening up the local audit market to a wider range of providers (including smaller, local firms) so that Local Public Bodies (LPBs) have more choice of auditors on the market.
 - Increasing the transparency around the cost of audit services so that there is greater visibility as to what is included in fees (which may prompt discussions about reductions).
 - Ensuring the presence of incentives for the reduction of the costs by auditors (for example, through innovation in audit approach and elimination of unnecessary work).
65. To fulfil this objective, it is also important that the market is capable of meeting the specific needs of different categories of public body and that work can be tailored to different sectors.

³⁶ For example, the Local audit impact assessment for the Local Audit and Accountability Act 2014 which states that: 'Ending state provision of audit services and increasing competition in the market will drive better value for money for the taxpayer.'

66. **Policy objective 2: Maintain competitive audit fees (or reduce audit fee levels).** To achieve this objective the government considers there needs to be a set of **long-term outcomes**. These are increased transparency around the costs of local audit services and the removal from the audit fees of costs associated with non-audit activities that individual LPBs have not commissioned. Audit fees previously covered the cost of the actual audit service but also a top slice to pay for Audit Commission corporate costs and the cost of its other work. There will need to be incentives for auditors of LPBs to reduce the costs of their audits through greater competition and innovation and greater exposure of their costs to LPB scrutiny, so that bodies can see what work auditors are doing for the purposes of giving an opinion.
67. **Policy objective 3: Save £1.35bn as part of the overall local audit reform programme under way.** The DCLG has estimated that the introduction of the new local audit regime will result in saving a total of £1.35bn over the course of ten years from 2009/10.³⁷ The **long-term outcomes** required to help secure this policy objective are similar to those for the first objective stated above. Savings will be secured by further reductions in audit fees, which are expected to be generated by greater transparency of costs of local audit services, incentives provided for auditors to reduce costs of local audits, and the ending of non-audit activities. In addition, reforms to the oversight of the public audit regime are expected to generate a more efficient regulatory system for all audit work. This will be in addition to the reduction secured as a result of the ending of inspection and assessment work.

Related medium-term outcomes

68. In order to achieve the above stated long-term outcomes (which in turn are designed to secure the fulfilment of the three key policy objectives related to the conduct of audit within LPBs) certain **outcomes also need to be accomplished in the medium-term**.
69. In particular, LPBs having an enhanced choice on the market depends on **local appointment of auditors for LPBs from a competitive market** and having the ability to **request non-audit assurance services** within the boundaries of what is appropriate work. An increase in the transparency of costs of local audit services depends on the same medium-term outcomes as well as LPBs **paying only for actual audit services**, which no longer include costs for any other Audit Commission activities.
70. Furthermore, whether incentives for LPB auditors to reduce costs are created will depend on the **responsiveness of the auditors** of LPBs to the audit needs of the sector. The expectation is that auditors will be more responsive if they come under greater pressure from LPBs. This pressure may be generated from LPBs by **greater awareness of the costs of their audit service** and thus greater interest in securing value from it. This may arise from **LPBs directly incurring costs** themselves relating to the procurement and management of audit contracts, which were previously incurred by the Audit Commission, as well as paying for the actual audit services only.

³⁷ DCLG Local Audit and Accountability Act 2014. 2014. 'Local audit impact assessment'. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349418/2014_FINAL_Local_Audit_IA.pdf (accessed 1 April 2016).

Activities undertaken to achieve mid- and long-term outcomes

71. There are a number of activities included as part of the reforms designed to yield the aforementioned outcomes and in turn achieve the policy objectives. Following outsourcing in 2012, all local government audit work is now undertaken by private-sector firms with staff with suitable qualifications and experience. Under the reforms, responsibility for commissioning auditors is being transferred to local appointment by LPBs. They will have the option to go it alone and procure themselves, procure jointly with other LPBs, or use a sector-led collective procurement body. Where they decide to go alone, they will be expected to establish an independent audit panel to be consulted on the appointment. Furthermore, LPBs with an annual turnover not exceeding £25,000 are exempt from external audit, while those with a turnover between £25,000 and £6.5m are subject to a proportionally smaller regulatory regime. Finally, wider reforms have already put an end to the routine inspections and assessments (including CAA) which were undertaken by the Audit Commission.

2.2.3. Policy objectives and long-term outcomes related to the regulatory bodies

72. **Policy objective 4: Deliver greater local accountability and transparency.** Public audit provides detailed information on how public funds have been spent and allows a range of stakeholders, including residents, to know how money entrusted to public bodies has been used. Where they have concerns it provides the basis for holding public bodies and their representatives to account. This policy objective is linked to **four main long-term outcomes** that Government wants to see achieved through the reforms. These outcomes are:
- Continuing the use of audit to provide assurance to elected members, paid officials and the public that funds have been spent appropriately.
 - Maintaining the local accountability and quality of audit services.
 - Continuation of the ability of the audit regime to identify financial problems within local bodies.
 - Increasing the transparency around the cost of local audit services.
73. **Policy objective 5: Uphold high standards of auditing.** The quality of audit is related to adherence to technical standards set by the audit and accounting professions, as well as timeliness in undertaking and reporting the work, which ensures that the outputs are useful to decision makers and assurance on the use of public funds given in a timely manner. In the particular context of the audit of public funds, high standards of audit also require a broader assessment of the value for money and propriety with which funds are used. Fulfilment of this objective is conditional on the achievement of four long-term outcomes. These are:
- Maintaining the local accountability and quality of audit services, including via the key role of the Financial Reporting Council.
 - Having a more efficient regulatory system for all audit work.
 - Ensuring that data and knowledge of sector performance issues continue to be gathered by the NAO, but at a lesser cost than under the Audit Commission regime.
 - Maintaining the ability of the audit regime to identify financial problems.

Related medium-term outcomes

74. In order to achieve the above mentioned long-term outcomes (which in turn are designed to secure the fulfilment of the key policy objectives) certain medium-term outcomes also need to be accomplished.
75. Elected members, paid officials and the public will continue to receive assurance on the appropriate use of public funds if the auditors of LPBs should continue to conduct independent audits that are undertaken in adherence to the auditing and ethical standards, and continue, where necessary, to issue 'reports in the public interest'.
76. The maintenance of local accountability and quality of audit services depend on the achievement of the following set of mid-term outcomes: the **public should continue to have the right to raise objections** on specific items of expenditure and the arrangements for doing so need to be simple and transparent so that this right is easily exercised. Furthermore, **local auditors must continue to be able to conduct their work independently, applying applicable auditing and ethical standards**. Where they have cause for concern about the way public funds have been spent they **must be able to report publicly without fear**. In addition, **auditor panels (where in place) need to be seen to be working effectively** and making recommendations which are acted upon in a transparent way.
77. The desired long-term outcome of efficiency gains in the regulation of local audit arises from LPB **auditors being subject to the same regulation as those for private sector audits**, which will allow for the exploitation of efficiencies as a result of merging of regulatory regimes through the FRC, given that the firms involved in both are often the same.
78. Maintaining sector wide knowledge about performance (but at a lesser cost than under the Audit Commission regime) is contingent on the **NAO undertaking suitably targeted studies** of themes across local public bodies and publishing a number of reviews on cross-sector themes within the agreed budget, as well as sector led bodies maintaining a role in providing information on developments across the sector (e.g. LGA or other sector-led bodies). The continuation of the ability to identify financial problems depends on the **local auditors continuing to conduct independent audits**, as well as auditors **applying auditing and ethical standards** to public audits.

Activities undertaken to achieve mid-term and long-term outcomes

79. The above mentioned outcomes are expected to be achieved by a set of activities which are primarily undertaken by the new regulatory bodies (although some of the activities related to the LPBs also feed into the achievement of the respective policy goals). In addition, the wider public can play a role by lodging objections to items within an account (albeit increased discretion has been given to auditors regarding the investigation of the objections).
80. The set of activities related to the regulatory bodies (the FRC, NAO and professional bodies) includes the transfer of local audit regulation to the FRC. Currently, audit firms have to meet requirements laid out by the Companies Act 2006 before they can be a statutory auditor for a listed company and they also needed to meet a separate set of requirements set by the Audit Commission to act as a statutory auditor of a local public body. Monitoring of audit quality and the work of the firms is also undertaken under the Companies Act 2006 by recognised supervisory bodies (the professional institutes) and

the FRC, and under the Audit Commission Act 1998, local public audit quality was assessed by the Audit Commission. Moving the regulation of the local public audit regime to the FRC and professional audit bodies is designed to remove the duplication and rationalise arrangements.

81. In order to uphold high (and consistent) standards of audit the National Audit Office (NAO) has taken over the role of preparing and updating the Code of Audit Practice and related guidance. The NAO has also taken on the role of preparing value for money studies in the local government field. It states that the Act allows it to carry out 'examinations to complement [its] role in holding central government to account or to provide evaluation, commentary and advice of a general nature to all or particular descriptions of local public bodies authorities. This allows [it] to add value both centrally and locally by providing an 'end to end' view of the impact of government policy.'³⁸ This is designed – along with some sector-led performance sources – to provide continuing analysis, albeit on a limited number of topics. The same broad scope of public audit will continue to be undertaken by auditors of local public bodies. Together, these measures are designed to achieve the overall objective of upholding high standards of auditing.

2.2.4. List of indicators

82. The list of indicators in Table 5 was primarily developed in order to measure medium-term and long-term outcomes (the numbering of the indicators corresponds to the numbers shown in the ToC diagram above). During a potential future evaluation these indicators would be used to measure change over time compared to the baseline year, which was set as 2009/10. Some of the indicators are also used as broad indicators for measuring the achievement of the overall policy objectives. While this might mean some overlap in terms of the use of the indicators (i.e. one indicator that measures outcomes should ideally not be the same as an indicator that is assigned to broader high-level objectives), it might still be useful to have some indicators that can be monitored as proxies when examining the achievement of wider policy goals.

³⁸ NAO. 2014. Local audit. Online: <https://www.nao.org.uk/about-us/our-work/local-audit/> (accessed 1 April 2016).

Table 5: List of indicators

No	Theme	Indicator
1	Number of participating audit firms	Number of audit firms registered and undertaking local public audit work, including information on size/turnover of audit firm; market share; and value of contracts held with local public bodies.
2	Annual cost of local audit regime	Annual cost of local audit regime including procurement costs, fees paid, regulatory oversight, etc.
3	Local elector objections to accounts	Number of cases in which local electors lodge an objection to items within the accounts/number of cases in which the auditor decided to investigate. ³⁹
4	Qualification of audit opinions	Number of cases where the audit opinion on local public body accounts is qualified.
5	Health of the audit system	Number of cases in which local bodies failed to appoint auditor by principal bodies and smaller bodies; number of cases of violations of the FRC Auditing Practices Board's ethical standards in local audits; number of cases where local public bodies removed their auditors/auditor resigns.
6	Public Interest Reports	The number of Public Interest Reports issued.
7	Satisfaction with audit services	Level of satisfaction with the quality of audit services amongst local public bodies.
8	Measure of the technical quality of audit	Measure of technical quality of audit undertaken (where quality is defined as compliance with the Audit Commission's regulatory requirements and with professional standards).
9	Small local public bodies' compliance with transparency expectations.	Number of small local public bodies not complying with transparency standards.
10	Local public bodies' views on composition of fees	Extent to which local public bodies are clear about the composition of the audit fees.
11	Audit firms' views on fee levels	Extent to which firms feel incentivised/encouraged to reduce audit fees.
12	Firms' satisfaction with the regulatory regime.	Level of satisfaction of audit firms with new regulatory regime.
13	Data and knowledge of sector maintained.	Number of NAO reports published relating to local public bodies and existence of broader, sector-led data sources.
14	Meeting of statutory deadlines for audit	Number of cases where: Approval of accounts not done by 30 June 2010 Number of delays in having accounts published Audit opinions issued by 30 September
15	Role of auditor panel	Number of local public bodies that did not follow auditor panel recommendations.

³⁹ Sandford, M. 2013, 21. Local Audit and Accountability Bill 2013 (HL). Research paper 13/56. House of Commons Library.

2.2.5. Assumptions and related risks

83. The ToC discussed above is based on a series of assumptions about developments and about the behaviours of different stakeholders. We have divided these assumptions into three groups – those relating to: market development; public and regulatory oversight; and political context. Table 6 provides an overview of the assumptions, as well as considering related risks and possible impact should those risks materialise.

Table 6: Overview of assumptions and related risks

Assumption	Risk	Impact
Market development		
A competitive market develops which is of interest to a growing number of firms	<ul style="list-style-type: none"> • ‘Cherry-picking’ of the more profitable audits by firms, leaving some bodies without auditors 	<ul style="list-style-type: none"> • Competitiveness undermined
The ability of LPBs to appoint their auditor, including from local firms, leads to new firms entering market	<ul style="list-style-type: none"> • Most LPBs do not want responsibility of choosing auditors and opt for sector-led arrangements 	<ul style="list-style-type: none"> • Costs increase/fee levels cannot be reduced or maintained • Savings cannot be delivered
Transparency of costs is improved through a more competitive market, generating greater market competition	<ul style="list-style-type: none"> • Market contracts or consolidates around small number of firms due to high barriers to entry • Upward cost pressures outweigh those leading to efficiencies 	
Sufficient incentive for firms to enter the market will be provided (i.e. the work is deemed profitable and attractive) and they continue to have sufficient appropriately qualified staff available to do the work	<ul style="list-style-type: none"> • Incentives to enter are not sufficient for new entrants to see merit in seeking work, which may be exacerbated if contracts are extended and incumbents remain in place 	<ul style="list-style-type: none"> • Market retracts or consolidates around small number of firms • Competitiveness undermined
Barriers to enter the market are sufficiently low that new firms are attracted	<ul style="list-style-type: none"> • Barriers to entry (in particular, eligibility criteria to undertake local audit work, logistical issues around being present in certain areas, lack of capacity to handle work) are too high for small local firms to justify recruiting specialist auditors • Decline in the attractiveness of public-sector audit within firms leads to reduced number of staff training and qualifying, making it harder for a larger number of firms to compete for work 	<ul style="list-style-type: none"> • Wider technical expertise for local audit within the market has declined

<p>Procurement skills and technical audit knowledge exist within LPBs or can be built up to allow them to make informed judgements on auditors</p>	<ul style="list-style-type: none"> • Knowledge of how and what audit service to procure is lacking within LPBs' finance function to allow for informed procurement judgements (e.g. either due to lack of knowledge on the services offered and/or lack of ability to know own needs and what type of audit will match these) 	<ul style="list-style-type: none"> • LPBs opt for sector-led or joint procurement, rather than seek auditors on their own, diminishing the scope for competitiveness and anticipated savings
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<p>Some, but not all, LPBs will want to create shared procurement arrangements/set up effective sector-led bodies</p>	<ul style="list-style-type: none"> • LPBs struggle to know when it is better to do own procurement, joint procurement or to establish sector-led body • Majority of LPBs opt for sector-led arrangements, thereby essentially re-creating an Audit Commission model 	<ul style="list-style-type: none"> • Competitiveness undermined through creation of large procurement vehicle
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<p>Standards of audit can be upheld across all geographical regions and types of LPBs</p> <p>Pricing does not vary significantly across geographical regions</p>	<ul style="list-style-type: none"> • Audit firms with suitable skills are less available/less interested in certain areas (e.g. remote areas or areas in which they currently do not have a presence), reducing competition in parts of the country • Smaller LPBs cannot afford high-quality audit/costs for audit rises disproportionately for smaller LPBs • 'Cherry-picking' of the more profitable regions by firms 	<ul style="list-style-type: none"> • Standards and quality of audit cannot be upheld in particular parts of the country • Audit costs increase/decrease disproportionately for certain types of LPBs and in particular parts of the country, resulting in poor value for money for some residents
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Public and regulatory oversight

<p>Auditors will remain independent and will continue to conduct work in line with expected technical and ethical standards</p>	<ul style="list-style-type: none"> • Oversight and regulation do not effectively mitigate pressures 'to sail closer to the wind', leading to a decline in audit independence 	<ul style="list-style-type: none"> • Decrease of quality and reputation of local audit • Reduced ability to detect financial mismanagement • Financial mismanagement can occur
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<p>The Code of Audit Practice and associated guidance will strike the right balance between the quality and rigour of audit and the cost of compliance</p> <p>VfM outputs by the NAO will be proportionate, risk-based and add value</p>	<ul style="list-style-type: none"> • Code of Audit Practice is made increasingly stringent and makes audit work increasingly onerous and costly • NAO VfM outputs are seen as onerous by sectors and deemed to be insufficiently valuable 	<ul style="list-style-type: none"> • LPBs complain about the burden of audit • Costs of audit (administrative burden) increase on LPBs, undermining credibility of audit regime
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<p>The system is coherent and understood by all stakeholders – LPBs, public, politicians and audit firms</p>	<ul style="list-style-type: none"> Stakeholder comprehension of system is undermined by fragmentation of responsibility between different and unfamiliar players Decline in number of people who understand how to raise concerns about local public spending Technical expertise is too thinly dispersed around different bodies (e.g. NAO and FRC) whose responsibilities primarily rest in other sectors 	<ul style="list-style-type: none"> System lacks credibility with stakeholders Public loses faith in effectiveness and propriety of local spending Transparency and accountability undermined Loss of expertise reduces the quality of oversight of sector and decline in informal networks which sustained standards
<p>Appropriate levels of useful data and insight about the performance of the sector will be gathered and available but at less cost than under the Audit Commission</p>	<ul style="list-style-type: none"> Data cannot easily be obtained and compared due to lack of standardisation The NAO's approach to performance data gathering and reporting is undermined by lack of local presence and links to Parliament Performance and outcomes increasingly hard to measure in a world of partnerships and different delivery models 	<ul style="list-style-type: none"> Transparency and accountability undermined, leading to decline in standards of financial management and value for money
<p>No reduction in ability of the public to object to items contained in LPB accounts</p>	<ul style="list-style-type: none"> Public knowledge about this option declines 	<ul style="list-style-type: none"> Transparency and accountability decreases
<p>Auditor special investigations and Public Interest Reports can still be carried out, as prior to the reforms</p>	<ul style="list-style-type: none"> Auditors do not have the resources and/or inclination to investigate issues either at all or to the same extent 	<ul style="list-style-type: none"> Accountability decreases and reputation of system declines Major and damaging instances of poor/illegal use of public resources are only belatedly identified or not all, leading to a decline in confidence in the audit regime.
<p>Installed auditor panels work effectively and make transparent recommendations</p>	<ul style="list-style-type: none"> Auditor panels lack the capacity and technical knowledge to make fair and transparent recommendations 	<ul style="list-style-type: none"> Transparency and independence of appointment process decreases Competition in the market undermined

Political context

Cross-party support for reform enables the new system to bed in and become accepted by all

- Short-term weaknesses and incidents of poor financial management lead to criticism of reforms, especially abolition of Audit Commission

- Reputation of new system undermined and audit of local public bodies gets politicised

- Calls for further reform and possible re-creation of Audit Commission-type regulatory body

Configuration of LPBs remains largely as now and the system is able to adapt to changes in environment without any impact on the quality of audit

- Audit regime struggles to cope with changes in local government regime, including the creation of new service delivery mechanisms

- Audit quality and effectiveness decline, reducing the assurance that can be provided on new and important risks to the use of public money
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3. Baseline data and description for a potential future evaluation

3.1. Background

84. The Theory of Change (ToC) – prepared by RAND Europe and discussed and refined with the help of DCLG policy officials – sets out how a number of activities are expected to lead to the achievement of the desired objectives. It also identified a series of indicators that can be used to track whether these objectives have been accomplished. This section of the report recommends and discusses the baseline data (quantitative and qualitative) for these indicators that should be used when undertaking any future evaluation.
85. Baseline data is collected at the beginning of a project or before an intervention has occurred. It serves as a point of comparison. In this case, the baseline provides the basis for assessing the changes to the local audit arrangements following the election of the Coalition Government in May 2010, including (but not exclusively) as a result of the Local Audit and Accountability Act 2014 (see Part 1). The baseline data aims to capture the position across a number of aspects of the audit arrangements as they existed prior to the start of the changes. They will be a starting point for any future evaluation against which to measure developments.

3.2. The relevant baseline year for a potential future evaluation

86. Ideally, the baseline data would be straightforward to capture and relate to the same point in time for all aspects of the evaluation. Relevant data would also have been captured during the baseline year. However, in this case, there are a number of factors which make this hard and, in some cases, impossible. As a result, any future evaluation will need to use different baseline years for different aspects of the evaluation.
87. In the first place, we agree with DCLG that the **2009/10 financial year should be treated as the final year of the pre-reform regime**. This is the baseline year used in the DCLG's impact assessment 'since it was the final full year of operation of the Audit Commission prior to the beginning of the programme to disband it and implement a new local audit regime.' DCLG therefore treats 2009/10 as the counterfactual when the functions and associated costs of the Audit Commission were considered (Impact Assessment, p18). For the purposes of some quantified administrative data (e.g. costs, numbers of audit firms, etc.) 2009/10 is also used as the baseline year. Data was collected at the time and is available either publicly or via DCLG.
88. However, evaluating all aspects of the audit reforms in a comprehensive manner in the future evaluation will require that more than just administrative data is gathered. In particular, we are interested in **opinions from participants in the audit process**. This is because a number of aspects of the reforms are designed to change behaviours or involve the exercise of professional judgement (e.g. around satisfaction with an audit service). This requirement raises a number of challenges for research. In particular:
 - In some cases, we were not been able to find data for the baseline year.

- In other cases, where no data from the baseline year exists, we are collecting data on perceptions and recollections of past events and processes. Thus, we are interested in the views of stakeholders in arrangements as they existed in the past or ‘under the Audit Commission’s regime’. This is far from ideal and will not necessarily provide views as they might have been expressed exactly in 2009/10, but they are the best available in the absence of the views being gathered at the time.
 - In some other cases, no baseline data exists at the moment because changes have yet to take place, for example, the introduction of auditor panels.
89. To establish some elements of the baseline, we sought to make the best of available secondary information and what could be captured during interviews. In particular:
- To secure the views of **LPBs about their auditors** in 2009/10, we have identified in the Audit Commission archive a survey commissioned from Ipsos MORI by the Commission, carried out in 2008. Although slightly earlier than the baseline year, this will still provide a fair (and detailed) reflection of views of the audit firms prior to the announcement of the reforms. Given the nature of a routine, annually provided service, it is unlikely that views will change much over a short period of time. This data will be added to by information from our survey of LPBs, which gathers views on the latest audit, many of which were conducted under arrangements initiated in 2012.
 - To secure the views of **audit firms undertaking local audit** about the arrangements as they existed in the past, during our interviews, we asked firm partners responsible for local audit for their perceptions about the effectiveness of the ‘later stages’ of the Audit Commission regime. In several cases, partners have considerable experience going back many years, or were accompanied in the interview by a colleague who could take a longer-term perspective. We also bolstered our understanding by reviewing the submissions made by a number of audit firms to parliamentary hearings after the announcement of the abolition of the Audit Commission. In this way, we aimed to re-create a roughly contemporary view.

3.3. Sources of baseline data

90. The needs of the possible future evaluation which addresses the questions set out in paragraph 1.1 require that baseline data is drawn from different types of evidence – both quantitative and qualitative. In particular, it will require use of a combination of:
- **Official published data and reports** – including data published by or made available by the Audit Commission and DCLG
 - **Survey data** – in particular, RAND Europe’s 2015 survey of local public bodies
 - **Qualitative evidence** – evidence from interviews with stakeholders including audit firms, professional bodies and regulators, written submissions to parliamentary select committees.
91. In some cases (see last part of Table 7), there will be no baseline data for certain indicators available. Sources of data against the indicators for any future evaluation are discussed in Part 5. Table 7 includes our suggestions for which bodies might be responsible for data collection.

Table 7: Indicators and type of evidence used to provide baseline data

No	Indicator theme	Type of evidence	Responsibility for data collection in interim period and/or at time of evaluation	
			Local government	Health bodies
1	Number of firms in local audit work	Official data	PSAA Sector-led bodies	NHS England NHS Improvement NAO
2	Cost of local audit regime	Official data	PSAA Sector-led bodies Regulatory bodies	NHS England NHS Improvement
3	Number of objections by local electors ⁴⁰	Official data	Sector-led bodies	N/A
4	Qualification of audit opinions	Official data	Sector-led bodies	NHS England NHS Improvement
5	Health of audit system – e.g. violations of ethical standards, removal of auditors, etc., plus shortcomings in the procurement and appointment processes	Official data	FRC Sector-led bodies	NHS England NHS Improvement
6	Number of Public Interest Reports	Official data	Sector-led bodies	NHS England NHS Improvement
7	Local public bodies' satisfaction with audit services	Survey data; qualitative evidence	Evaluator will repeat survey	NHS England NHS Improvement
8	Quality of audits performed	Official data	FRC	FRC DoH
9	Number of small local public bodies not complying with transparency standards	Official data	SAAA	N/A
10	Local public bodies' views on composition of fees	Survey data; qualitative evidence	Evaluator will repeat survey	NHS England NHS Improvement
11	Audit firms' views on fee levels	Qualitative evidence	Evaluator will repeat interviews	Evaluator will repeat interviews
12	Audit firms' satisfaction with the regulatory regime	Qualitative evidence	Evaluator will repeat interviews	Evaluator will repeat interviews
13	Number of NAO reports on local issues as well as existence of broader, sector-led data sources ⁴¹	Official data/qualitative evidence	Evaluator review of NAO/other sources (such as LGA etc.)	Evaluator review of NAO/other sources (such as LGA etc.)
14	Meeting of statutory deadlines for audits	Official data	PSAA Sector led bodies	NHS England NHS Improvement

⁴⁰ It might be difficult in practice to collect this information because some 'objections' can be also not accepted by auditors as valid; furthermore local government electors for the area to which the accounts relate can also ask formal questions to the auditor about the accounts under the Local Audit and Accountability Act 2014. It is also not clear at this point who will collect this information (objections – valid or not – and questions in future) as a 'sector-led body' may choose not to do so or may not have complete coverage.

⁴¹ It should be noted that any future evaluator should also look at the issues raised in these reports from a qualitative point of view, as well as any evidence that these issues raised are being acted upon.

Indicators for which there is currently no baseline data

No	Indicator theme	Reason
9	Number of small local public bodies not complying with transparency standards	Too early, this information will only be available at a later point in time
15	Number of local public bodies that did not follow auditor panel recommendations	This process is not yet in place before this project will be concluded

3.4. Baseline data for a potential future evaluation

92. The policy objectives for the reform were set out in section 1.3 in Part 1. The indicators (Table 6) identified during the work on the Theory of Change (ToC) will help to assess the extent to which the main policy objectives and outcomes leading to them have been met. We have gathered baseline data against the indicators where possible. They are brought together under the following headings which broadly mirror the high level policy objectives set out in the ToC diagram:

- Diverse audit market, costs and fee levels – indicators 1, 2, 10, 11
- Accountability, transparency and sector knowledge – indicators 3, 4, 5, 6, 13
- Uphold high standards of auditing – indicators 7, 8, 14, 12.

DIVERSE MARKET, COSTS AND FEE LEVELS

93. The following indicators cover the overall audit market, costs and fee levels. The high-level objectives are to expand the market of audit providers, reduce the costs of audit and maintain competitive audit fees or reduce fee levels.

3.4.1. Indicator 1: Number of participating audit firms

Indicator: Number of audit firms registered and actively undertaking local public audit work, including information on size/turnover of audit firm; market share; and value of contracts held with local public bodies.

94. This indicator is linked with the policy objective of **developing a diverse and competitive market for local audit service providers**, and can be measured by looking at the number and type of audit firms participating in the market at the baseline year (2009/10) and at the point of undertaking the evaluation. The indicator will help establish whether LPBs have an enhanced choice of auditors through opening up of the market to a larger number of suppliers. A decline in the number of participants in the audit market could reflect firm decisions about the perceived profitability of the work and its potential risks, and/or high 'barriers to entry' for audit firms due to the specialised nature of local audit.

95. **Baseline position:** The Audit Commission's Annual Report and Accounts for 2009-10 states that in the baseline year, 30 per cent of the Commission's audits were undertaken

by five private-sector firms, with the remainder carried out by the Audit Commission.⁴² In 2012, Ernst and Young, Mazars, KPMG and Grant Thornton won the outsourced in-house practice work. BDO took over PKF in early 2013 and the contract was novated to BDO. In 2014, KPMG, Ernst & Young and BDO won work that was previously done by Grant Thornton, KPMG, PwC, BDO and Deloitte. Table 8 below summarises change since the baseline year for principal authorities.⁴³ The future evaluator should also explore during repeated firm interviews reasons why companies have/have not entered or dropped out of the market.

Table 8: Market share of participating audit firms for principal authorities

2008/09 audits (1)		2013/13 audits (2)		2015/16 audits (3)	
Audit Commission	70%	Grant Thornton	40%	Grant Thornton	31%
PwC	8%	KPMG	25%	KPMG	30%
KPMG	7%	Ernst & Young	16%	Ernst & Young	28%
Grant Thornton	8%	PwC	8%	Mazars	5%
Deloitte	4%	Mazars	4%	BDO	6%
PKF	3%	Deloitte	4%		
		BDO	3%		

1) after 2007 contract letting exercise 2) following 2012 outsourcing of Audit Commission practice 3) after 2014 procurement
Source: PSAA

In addition, the appointed auditors for smaller bodies for 2014/15 to 2016/17 are made up of BDO, Grant Thornton, PKF Littlejohn and Mazars.⁴⁴

3.4.2. Indicator 2: Annual cost of local audit regime

Indicator: Annual cost of local audit regime including procurement costs, fees paid, regulatory oversight, etc.

96. This indicator is linked to the policy objective of **maintaining competitive audit fees (or reducing audit fee levels) and saving £1.35bn on avoided costs due to the new framework**. It can be measured by comparing the baseline cost figure and the equivalent costs of audit under the new framework. **Any consideration of cost must, however, be taken in the light of an understanding of what activity was purchased for this sum.**
97. The baseline cost data for 2009/10 is best gained from the data contained in the Impact Assessment.⁴⁵ The cost in that report included payments to firms for outsourced audit work; payments to researchers, contractors and consultants; cost of in-house auditors; cost of assessment/inspection work; Audit Commission statutory responsibilities, support and overhead costs, and costs to local bodies of compliance. The number of cost elements of the future audit arrangements will be reduced given that the Government

⁴² Audit Commission. 2010. Annual report and accounts 2009 to 2010. Online: <https://www.gov.uk/government/publications/audit-commission-annual-report-and-accounts-2009-to-2010> (accessed 1 April 2016).

⁴³ PSAA data. 2015. (Unpublished).

⁴⁴ PSAA. 2016. Appointing auditors. Online: <http://www.psa.co.uk/appointing-auditors/> (accessed 1 April 2016).

⁴⁵ DCLG. 2014, 21-30. Local Audit and Accountability Act 2014. 'Local audit impact assessment'. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349418/2014_FINAL_Local_Audit_IA.pdf (accessed 1 April 2016).

decided to end aspects of the work of the Audit Commission. Table 9 (below) summarises the cost elements for each stage of the reform process.

98. **Baseline position:** The total cost for the local audit regime as it existed in 2009/10 was £248.57m.⁴⁶

Table 9: Cost elements at different stages of reform

Audit Commission framework	Transitional framework	New framework
Audit work by private firms	Audit fees	Audit fees paid directly by local bodies to their auditor (includes costs of regulation by FRC and professional bodies)
Paid to researchers, contractors and consultants	Paid to firms for outsourced audit work	NAO regulatory costs
Costs of in-house auditors (minus overhead)	Contract management (transitional body)	NAO Value for Money studies
Cost of assessment/inspection (minus overhead)	FRC and prof bodies regulatory costs	Local bodies' compliance costs (i.e. procurement and independent panel members)
AC statutory responsibilities, support and overhead costs (includes NFI and PbR costs)	Surplus	
Transitional liabilities		
Stranded costs		
Surplus: contribution to reserves		
Local bodies' compliance costs (i.e. CAA compliance)		

3.4.3. Indicator 10: Local public bodies' views on composition of fees

Indicator: Extent to which local public bodies are clear about the composition of the audit fees.

99. This indicator reflects the government objective of increasing transparency around audit fees and ensuring that local public bodies understand what they are paying for, as well as that these payments relate only to work directly applicable to their authority. This understanding of the composition of the audit fees remains important even when some local bodies might opt for a sector-led body whereby fees are more negotiated on an aggregate level via the sector-led body. In the past, the audit fee included Audit Commission on-costs related to their additional responsibilities. Around 25-30 per cent of fees funded the Audit Commission's programme of VfM studies.⁴⁷
100. To establish whether LPBs understand the makeup of their audit fees, the subject was included in our survey of local bodies. This specifically asked them to respond to statements on the appropriateness of fee levels and whether revisions were communicated clearly. It also asked them whether they agree with certain statements about fee levels and clarity of fee composition. Government objectives will be met if there is an increase in the levels of satisfaction when the survey is repeated as part of the evaluation work. In this case we have to take results from our 2015 survey as a baseline.

⁴⁶ DCLG (2014, 21-30) Local Audit and Accountability Act 2014. 'Local audit impact assessment'. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349418/2014_FINAL_Local_Audit_IA.pdf (accessed 1 April 2016).

⁴⁷ House of Commons Research Paper 13/56, p. 10.

However, respondents were asked to consider a period which in many cases went back several years since the audit contract was established. We were also able to draw on responses in the 2008 Ipsos MORI survey.

101. **Baseline position:** Our survey found:

- In response to the question **whether their initial audit fee was appropriate**, 25 per cent of respondents considered it was 'completely appropriate' and 69 per cent said it was 'acceptable'. Five per cent said it was 'not appropriate'.
- In response to the statement **'To date my organisation has been concerned that we have been paying too much for our audit over the last three years'**, 34 per cent 'somewhat agreed' and five per cent 'strongly agreed'. 21 per cent 'somewhat disagreed' and five per cent 'strongly disagreed'. 35 per cent neither agreed nor disagreed.
- In response to the question **'Were any revisions to the fee clearly communicated and explained?'**, 83 per cent of respondents said 'yes', and six per cent said 'no'. The remainder did not know.
- In response to the statement **'To date, my organisation has not been clear what our audit fee has included'**, 9 per cent agreed or strongly agreed, whilst 73 per cent 'somewhat disagreed' or 'strongly disagreed'. 17 per cent neither agreed nor disagreed, which means that they were neutral towards this statement since they did not pick the option 'don't know', which was also given in the survey.

102. We are able to make a broad comparison with figures drawn from the 2008 survey commissioned by the Audit Commission, although given the differences in sample size, make up of organisations and composition of respondents it is largely impressionistic. As a result a direct comparison is not possible.⁴⁸ In response to being asked whether their initial fee was appropriate, 25 per cent responded it was 'completely appropriate', 69 per cent considered it 'acceptable', 5 per cent 'not appropriate' and 2 per cent did not know. In response to the question about whether revisions to the fee were clearly communicated and explained, 83 per cent stated agreed, while 6 per cent disagreed and 11 per cent did not know. This suggests an improvement in local body satisfaction when looking at the 2008 survey. However, it should be noted again that the sample used for the 2008 survey is not identical with the one used for our 2015/16 survey in terms of size and type of bodies surveyed.

3.4.4. Indicator 11: Audit firms' views on fee levels

Indicator: Extent to which firms feel incentivised/encouraged to reduce audit fees.

103. A key government objective for reforming local audit is to maintain the competitiveness of fee levels or reduce them. This will come about if audit firms have incentives to do so, or are able to make economies while still meeting professional standards and consider the work remains sufficiently profitable. In 2012, the 70 per cent of audit work undertaken by the Audit Commission in-house practice was contracted out and the 700 auditors transferred to private firms. These arrangements led to the reduction in statutory audit fees for 2012/13 audits of around 40 per cent for five years. This fall was deemed to be, in part, attributable to the fact that fees paid were no longer required to support the VfM programme, but the Commission also suggested that its bulk purchasing power had been

⁴⁸ Ipsos Mori. 2008. Stakeholder perceptions of the Audit Commission (from Audit Commission archive).

a factor.⁴⁹ In addition, firms taking on Commission staff made efficiencies in practices and reduced audit staff numbers. The retendering of the 30 per cent already carried out by the firms led to further savings.

104. To establish the views of audit firms on fee levels, we interviewed partners, including about the current fee levels and whether they are satisfied with them, as well as what scope there is for further reductions. We also reviewed published submissions and oral evidence from firms during parliamentary hearings on the local audit reforms.⁵⁰ Any future evaluation would want to repeat the questions to assess whether participating firms' views had changed.
105. **Baseline position:** A number of themes came out of the interviews and submissions. Some firms [Interviews 1, 4, 6] felt that **fee levels had been generally good and competitive**, particularly where they had thought carefully about pricing in different parts of the country [6]. Another stated they had gone in at the lowest price possible for an acceptable standard of work in keeping with their market position that they were not a 'bulk standard provider' and so would not be the cheapest [7]. One firm [3] thought that firms had considered that the most recent procurement was seen as the last chance to remain in the market for a while and so had pitched at a very low level in order to secure work. As a result, several interviewees **did not consider the levels were sustainable in the long run** [3, 5].
106. A number of firms voiced **concerns about whether there was much more potential for further decreasing fee levels**. Reductions in costs and fees had been made as a result of the 2012 and 2014 procurements,⁵¹ which several interviewees [2, 3, 5, 7] described as very 'price-driven' exercises, once a minimum quality threshold had been reached. One of these said there was insufficient attention paid to 'quality' in the scoring system and this gave little scope for firms to offer much added value or for public bodies to have a choice about whether they wanted to pay more [2]. One interviewee [1] noted that they felt the biggest savings had already been achieved through the ending of the in-house Audit Commission practice. Efficiency savings were also made by firms taking over the work (as they had challenged the performance and resource levels of the transferring teams).
107. Linked to this, several interviewees [1, 5, 7] considered **further reductions could jeopardise audit quality** since auditing standards required certain levels of work and firms would not risk reputational damage by delivering substandard audits. One [7] said that ultimately the firms were commercial organisations and they could not drop their prices without taking something out and there was a risk that the quality of some audits would suffer. Lowered fee levels would also limit the potential for 'added value' work. Concern was also expressed that further pressures on fee levels would make worthwhile VfM work very difficult, and in the words of one firm, 'reduced to a tick-box exercise'.

⁴⁹ House of Commons Research Paper 13/56, p. 10. Audit Commission (unpublished): 'In the public interest: Lessons from the Audit Commission's work for other public bodies and those receiving our functions'. Audit Commission 2013-4 work programme and scale of fees, p. 5.

⁵⁰ House of Commons Communities and Local Government Committee. 2010-12. Audit and inspection of local authorities. Online: <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmcomloc/763/763.pdf> (accessed 1 April 2016).

⁵¹ In the public interest document, Audit Commission. £280m between 2012 and 2017 for local public bodies including small bodies.

108. Anecdotally, decreasing fee levels were reported by one interviewee [1] as having led to **concerns from local bodies about declining standards in audit work**. Another interviewee [3] felt that the current rate of fees was unsustainable; firms had been pricing low in recent tendering processes to retain market share in the short run and so creating a false impression of the level of quality available at this fee level in the longer term.
109. In addition, **firms pointed to factors they felt could push fees upwards**. In particular, one [6] explained they could be dependent upon:
- **The form of procurement vehicle** – entity by entity procurement might lead to more costly cost of tendering.
 - **Portfolios of work** – widely dispersed programmes of work, work in outlying places, where the cost of travel would start to become more of an issue.
 - **Riskier work** – the audits of poorly managed authorities that might have financial difficulties and poor controls, which might require additional work.

ACCOUNTABILITY, TRANSPARENCY AND SECTOR KNOWLEDGE

110. A number of indicators relate to the maintenance of the audit system, in particular whether it delivers greater local accountability and transparency, and whether new arrangements will maintain levels of knowledge of sector performance.

3.4.5. Indicator 3: Local elector objections to accounts

Indicator: Number of cases in which local electors lodge an objection to items within the accounts/number of cases in which the auditor decided to investigate.

111. A sign of the health of the local audit regime is the ability of local electors to personally inspect the accounts of their council. Having done so, an elector can ask the external auditor to apply to the High Court for a declaration that an item of account is unlawful, or to issue an immediate report in the public interest. Objections have to be about specific items in the accounts and an unlawful item must be one where the council spent or received money without powers to do so; or took from or added to the wrong fund or account; made a decision to spend money which was wholly unreasonable or irrational. Under the change of responsibilities, the Comptroller and Auditor General, the head of the NAO has agreed to maintain and publish the publication *Council Accounts: a guide to your rights*. The current edition was issued in April 2015 by the NAO.⁵² The rights of local electors to view accounts and question the auditor on items within them, and to object to items, do not apply to local health bodies.
112. **Baseline position:** Based on discussions with a representative of PSAA, it seems unlikely that there was any robust data collected centrally on the number of objections. Individual objections would have been raised, examined and a decision made locally by the appointed auditor on whether to pursue. However, RAND Europe has reviewed 378 management letters and has identified 24 cases where reference is made to objections. This information is offered as baseline data, although it would be for any future evaluators to undertake a similar trawl of individual audits as it seems unlikely that any particular body will take responsibility for gathering this information centrally. Future research may also want to make an assessment of the gravity of these objections and if there are any trends

⁵² National Audit Office. 2015. 'Council Accounts – a guide to your rights'. Online: <https://www.nao.org.uk/code-audit-practice/council-accounts-a-guide-to-your-rights/> (accessed 1 April 2016).

and common issues arising in terms of the content of these objections. An alternative source could be ISA 260 reports (which communicate the main audit findings) in the absence of comprehensive data about the number of questions/objections, although there is a risk of gaps gathering the data this way. A future evaluator may also want to consult with the NAO and auditors – ‘prescribed persons’ under the Public Interest Disclosure (Prescribed Persons) Order 2014 – to establish whether they have received reports of concerns.

3.4.6. Indicator 4: Qualification of audit opinions

Indicator: Number of cases where the audit opinion on local public body accounts is qualified.

113. The auditor has a responsibility to express an opinion on a set of financial statements. An unqualified opinion on the financial statements is given where they give a true and fair view, in all material respects, in accordance with the identified reporting framework. Non-standard opinions may arise where the auditor is unable to obtain material evidence (limitation of scope), where there is a material disagreement on treatment of a matter in the financial statements (disagreement), where there is a major disagreement such that financial statements are misleading or incomplete (adverse opinion) or where the auditor was unable to express (disclaimer of opinion). A significant increase/decrease in the number of qualified opinions provides an indicator of the quality of accounts and financial management in place at LPBs. This links to the long-term outcomes on the Theory of Change diagram of ‘Continuation of the ability to identify financial problems’ and ‘Maintenance of local accountability and quality of audit services’. A large increase in qualified opinions could be a sign of strain within the financial management arrangements of audited bodies.
114. **Baseline position:** Auditors issued a non-standard opinion on the 2009/10 accounts of two councils (one per cent). In addition, they issued a non-standard opinion on eight local government bodies (seven larger internal drainage boards, and one larger town/parish council). There were no unqualified opinions at police authorities and fire and rescue authorities.

3.4.7. Indicator 5: Health of the audit system

Indicators: Number of cases in which local bodies failed to appoint an auditor; number of cases of violations of the FRC Auditing Practices Board’s ethical standards in local audits; number of cases where local public bodies removed their auditors/auditor resigns.

115. The government objective of high standards of auditing will only be maintained if auditors continue to apply auditing and ethical standards as set out by the FRC Auditing Practices Board. Signs of problems would be increased levels of failure to appoint auditors; violations of ethical standards; and increased numbers of removal of auditors or auditor resignations. These would suggest problems in the relationship between auditor and auditee, which may arise from the auditor challenging activities within an organisation, or alternatively, auditee dissatisfaction with standards of audit. The Local Audit (Auditor Resignation and Removal) Regulations 2014 govern the procedures to be followed when an auditor wishes to resign their appointment, or the local public body wishes to terminate it. This includes the local public body publishing a decision to remove an auditor, the auditor panel’s response and the auditor’s response.

116. Complete failure to appoint will be very rare and non-compliance with ethical standards that comes to the attention of the FRC will also be rare. More likely are problems and shortcomings in the procurement and appointment process, weaknesses in the operation of local auditor panels, and non-recognition of breaches of ethical standards such as local audit committees/local auditor panels not understanding or applying restrictions on non-audit work, or firms taking a more generous view of what is allowable by way of non-audit work.
117. **Baseline position:** Consideration of this indicator by a future evaluator will require interviews with the FRC to identify whether there have been cases of failure to have regard to the ethical standards of the Auditing Practices Board. These include requirements to ensure that no one acts as an engagement partner for more than five years; anyone who has been an engagement partner for an entity for five years cannot subsequently participate for another five years; non-audit work is treated as a potential conflict of interest. For the removal or resignation of auditors we would expect to see adherence to the Regulations.

3.4.8. Indicator 6: Public Interest Reports and statutory recommendations

Indicator: The number of Public Interest Reports issued.

118. Appointed auditors are required to consider whether to issue a report in the public interest on any significant matter coming to their notice in the course of an audit, and to bring it to the attention of the audited body and the public. Issues may include suspicions of misspending of public money as a result of poor governance or acting outside legal powers. Although a report is rare, particularly amongst principal bodies, the process is seen as a vital element of public sector audit and an essential tool of holding public bodies to account. Most cases of PIRs have been of parish councils (in part because there are so many more of them), but there have also been larger high-profile cases such as with Westminster City Council in the 1980s. During the consideration of the 2014 Act, some concerns were expressed that under local appointment of auditors, there may be pressures to avoid issuing a report in the public interest to avoid being branded as a 'difficult firm'.⁵³ It was also noted that the Audit Commission indemnified the auditor against certain legal costs, which the Commission considered meant they could resist undue financial or other pressures not to issue a report. In future, the auditor will be able to recover costs from the audited body. This indicator may help consideration of whether local accountability and transparency has been maintained or enhanced since the reforms, although an evaluator will need to be very careful about drawing conclusions from movements in either direction of small numbers.
119. **Baseline position:** PIRs were issued on three principal bodies in the period covered by the 2009/10 Audit Commission report 'Auditing the accounts'.⁵⁴ Overall, there were more than 60 PIRs, almost all for small bodies. In addition, from 2009/10 to 2014/15, 165 were issued, of which 155 related to smaller bodies which can also be explained by the fact that

⁵³ UK Parliament. 2103. Draft Local Audit Bill: Pre-legislative Scrutiny – Draft Local Audit Bill ad hoc Committee. Online: <http://www.publications.parliament.uk/pa/cm201213/cmselect/cmdraftlocaudit/696/69607.htm> (accessed 1 April 2016).

⁵⁴ Cheltenham Borough Council, Lindsey March Internal Drainage Board and London Borough of Lambeth.

there are many more smaller bodies than principal bodies.⁵⁵ We would expect a potential future evaluation to probe in interviews with firms whether they have felt under any pressure not to report given that there was some reference to this possibility during our 2015 interviews. An auditor cannot issue a direction to prevent unlawful expenditure in a local health body, but must instead refer the matter to the Secretary of State. There is no requirement for a PIR on a health body to be published; it must be sent to the NHS Commissioning Board (NHS England).

3.4.9. Indicator 13: Data and knowledge of sector maintained

Indicator: Number of NAO reports published relating to local public bodies, as well as existence of broader, sector-led data sources.

120. The Audit Commission maintained considerable knowledge of local service delivery and performance. Its research function was disbanded and its responsibilities have not been taken over by any other organisation. Whilst not intended to replicate the work of the Audit Commission, the NAO has been provided with specific legislative powers under the Local Audit and Accountability Act 2014 to undertake VfM studies that consider how local services use their resources. The aim is for the work to ‘add value centrally and locally by providing an ‘end to end’ view of the impact of government policy implementation’.⁵⁶ On its own the NAO’s work was not intended to replicate that of the Commission, so that the NAO reporting publicly on a regular basis on aspects of local service delivery (it states it will publish at least six reports a year) will only be a partial indication that knowledge and data is being maintained.⁵⁷ In addition, we would expect to see a number of well-supported sector-led data gathering facilities available to ensure that detailed comparative information is available for authorities to use.
121. **Baseline position:** The baseline could be taken as the number of publications in the first year of the new regime – the NAO’s 2015/16 financial year (April-March) – which is seven reports so far.⁵⁸ This does, however, seem a very narrow measure of whether knowledge of the sectors is being maintained and we would expect a broader understanding to be gained via sector-led initiatives. Assuming these are maintained, these include:
- **Local Government Inform** – a benchmarking service run by the Local Government Association for councils and fire and rescue authorities.⁵⁹
 - **Public Sector Audit Appointments Limited value for money profiles** – The VfM profiles bring together data about the costs, performance and activity of local

⁵⁵ Audit Commission (p. 27). ‘In the public interest’.

⁵⁶ National Audit Office. 2015. ‘The NAO’s role in local audit’. Online: http://www.nao.org.uk/wp-content/uploads/2014/05/10773-001-The-NAOs-role-in-local-audit_2015.pdf (accessed 1 April 2016).

⁵⁷ National Audit Office. 2015. Local audit. Online: <http://www.nao.org.uk/about-us/our-work/local-audit/> (accessed 1 April 2016).

⁵⁸ Care Act first phase reforms (June 2015); ‘Local Government new burdens’ (June 2015); ‘Financial sustainability of police forces in England and Wales’ (June 2015); ‘Funding for disadvantaged pupils’ (June 2015); ‘Devolving responsibilities to cities in England’ (July 2015); ‘Care leavers’ transitions to adulthood’ (July 2015); Care Act first phase reforms – local experience of reforms (August 2015).

⁵⁹ Local Government Association. 2015. LG Inform. Online: <http://www.local.gov.uk/about-lginform> (accessed 1 April 2016).

councils and fire authorities. The data is displayed under sections that give an overview of the chosen organisation and the services it delivers.⁶⁰

UPHOLD HIGH STANDARDS OF AUDITING

122. These indicators cover aspects of the quality of the public audit process. All audit brings with it expectations of independence from the audited body, objectivity and professional competence. 'Public audit' is a broader concept than the audit of companies, encompassing regularity and propriety, as well as considerations of VfM. For the purposes of this project we consider 'quality' has a number of different aspects – **whether audited bodies are satisfied with the quality of the audit service received** (indicator 7), the **technical quality of the work** undertaken by the audit firms as identified through quality review processes (indicator 8), and whether **statutory deadlines for delivery of audits** are met (indicator 14). Whilst these are different aspects of quality, they nevertheless help us to consider whether the audit regime is technically robust, accounts and audits are delivered in a timely manner, the requirements of a rigorous, professional and efficient audit (undertaken within the terms of legislation, the Code of Audit Practice, auditing and ethical standards) are met, and whether the overall process is regulated in an efficient and effective manner. Under this heading, we also consider indicator 12 – audit firms' satisfaction with the regulatory regime, as an indication of whether the overall framework is considered well managed and efficient by those subject to it. In considering the 'quality' of audit, however, we need to be mindful that delivery of an apparently 'high-quality' audit may be a reflection of well-prepared draft financial statements, rather than the quality of audit work.

3.4.10. Indicator 7: Local public bodies' satisfaction with audit services

Indicator: Level of satisfaction with the quality of audit services amongst local public bodies.

123. For this indicator we have gathered data from 2008 (the nearest to the baseline year we can find) and 2015-16. As part of its role, the Audit Commission surveyed stakeholders, including public bodies, about the levels of satisfaction with the service that they received. In 2008, the Audit Commission contracted with Ipsos MORI to carry out the survey⁶¹, which asked, among other things, the following questions:
- How satisfied are you with the extent to which your last audit plan was tailored to focus on key risks and priorities faced by your organisation?
 - How satisfied are you with the timeliness of reports?
 - How satisfied are you with the practicality of reports' recommendations?
 - How satisfied are you with the usefulness of reports?
 - How satisfied are you with the impact of audit reports?
 - How far do you agree with the statement: 'My initial audit fee was appropriate'?

⁶⁰ PSAA. 2016. Value for money profiles. Online: http://vfm.psa.co.uk/NativeViewer.aspx?Report=/profiles/VFM_Landing&EntityGroupID=189&SelectedCategoryID=-1&TopLevelCategoryID=7422 (accessed 1 April 2016).

⁶¹ Ipsos MORI survey for Audit Commission.2008. (From Audit Commission archive).

124. **Baseline:** In the absence of a survey for 2009 or 2010 (closer to the announcement of the abolition of the Audit Commission), we drew on the satisfaction survey of stakeholders from 2008 commissioned by the Commission. This provided independently gathered data on the level of satisfaction with the quality of audit services provided under the previous regime. Table 10 (below) summarises the level of satisfaction with their recent audit on a scale of 1-10, where 1 is poor and 10 excellent. The final column shows the mean score.

Table 10: Satisfaction levels for audit firms 2008

Firm/Rating	1-3	4-7	8-10	Mean
KPMG	2	52	43	7.0
PwC	0	36	57	7.8
Deloitte	5	53	37	6.6
Grant Thornton	0	65	30	7.1
PKF	7	40	53	7.1
Mazars	0	25	75	7.8
Baker Tilly	0	71	29	7.1
Audit Com	5	48	44	7.0

Satisfaction with recent audit arrangements – survey results 2015/16

125. **Baseline:** To secure an understanding of levels of satisfaction with their audit service around the time of the abolition of the Audit Commission, RAND Europe surveyed LPBs during 2015/16. The survey instrument is at Appendix D and covered a wide range of different aspects of the audit service, the relationship between the body and its auditors, the added value that the firm could bring, as well as the usefulness of the work. In considering the audit service, we need to be mindful that the organisations audited are public bodies and are required to have an independent audit. Firms are required to maintain appropriate professional distance and may in some cases have cause to be critical of the organisation and its management. The nature of the relationship may therefore influence the responses given in both positive and negative ways.
126. A total of 169 respondents completed the survey, an overall response rate of 23.2 per cent. This overall response rate was made up of 29 per cent in local government, 32 per cent in fire and rescue and 36 per cent in police bodies, and 14 per cent in NHS bodies. Considerable efforts were made by RAND Europe, DCLG, DoH, LGA and others to raise the response rate. Further information on the survey approach is given in Appendix A. For a potential future evaluation, additional effort should be made in advance of any further survey to get more buy-in from specific type of organisations involved and their overseeing bodies.

Overall results from the survey regarding satisfaction with current audit arrangements

127. Results from our survey suggests that, in general, most authorities were broadly satisfied with their current audit arrangements, particularly in terms of the ease with which they were able to contact and communicate with the firm (95 per cent of the respondents were mostly or completely satisfied). 83 per cent of respondents were 'mostly' or 'completely' satisfied with the extent to which the last audit plan was tailored to focus on key risks and priorities faced by their organisation.
128. Overall, our survey suggests that a large majority (at least three-quarters) were satisfied with the most recent audit they received under existing arrangements in terms of both

price and many aspects of the conduct of the work. A total of 75 per cent of authorities which responded considered that the overall audit service provided value for money (17 per cent did not). This figure from our 2015 survey would seem to equate broadly with the satisfaction levels of about seven out of ten in the 2008 Ipsos Mori survey (Table 7).

Areas with high levels of satisfaction with regard to current audit arrangements

129. High levels of satisfaction with current audit arrangements (i.e. people answering ‘completely satisfied’ or ‘mostly satisfied’) were also seen with regard to the timeliness of reports (81 per cent total), the ease with which the authorities were able to get an earlier involvement of the auditor when preparing the accounts (77 per cent total), practicality of report recommendations (82 per cent total), and usefulness of reports (80 per cent total) – see also table 11 below. With the exception of the ‘earlier involvement’ question, less than five per cent of respondents were ‘not at all satisfied’ with their auditors on these issues.

Table 11: Overview of LPBs high levels of satisfaction with current audit arrangements

High levels of satisfaction with:

Timeliness of reports	81%
The ease with which LPBs were able to get an earlier involvement of the auditor when preparing accounts	77%
Practicality of report recommendations	82%
Usefulness of reports.	80%

Areas with lower levels of satisfaction with regard to current audit arrangements

130. There was slightly less satisfaction with the extent to which the external auditors placed appropriate reliance on internal audit (73 per cent), the impact of audit reports on the operation of their organisation (75 per cent), and the ease with which firms provided staff and capacity to conduct the audit in a timely manner (76 per cent). An area where LPBs reported being less satisfied were in the effectiveness of their organisation in reducing the cost of external audits, where only 28 per cent of the respondents were completely satisfied, 39 per cent mostly satisfied, 19 per cent partially satisfied, and seven per cent not satisfied at all.

Actions undertaken by the auditor in the course of recent audits

131. When asked what was valuable about the auditors’ approach to their work, four per cent of the respondents did not select any of the options suggested while 86 per cent selected at least two and 48 per cent at least four (only one per cent selected all five). The proportion of respondents identifying approaches is shown in table 12 below. These results suggest that a majority of local public bodies see their auditors as offering a service which went beyond simply auditing the accounts.

Table 12: Overview of auditors' approach taken to the work

Auditors' approach taken to the work	
Provided advice/guidance/helped to address important issues	72%
Been a true 'critical friend'/developed a good working relationship with us	71%
Been good at communicating/keeping in touch	72%
Been available to discuss/listen to issues about the operation of this organisation	78%
Demonstrated good knowledge and understanding of this body	71%

132. The responses were less homogeneous when we asked about the impact that auditors' additional focus had brought to the relationship (Table 13). In this case, 13 per cent of authorities that completed the survey did not consider they received any additional benefits from their auditors, whereas 65 per cent received more than one. Auditors providing 'honest and constructive feedback on our performance' was the most popular benefit reported.

Table 13: Overview of additional focus provided by audit service

Auditors' focus	
Helped improve our management arrangements	13%
Helped demonstrate/highlight best practice/share information from elsewhere	54%
Encouraged my organisation to prioritise/provided action plan	25%
Provided benchmarking/comparative data	19%
Given honest and constructive feedback on our performance	70%
Helped improve financial management and governance	42%

Changes LPBs would like to see made to improve impact of audit

133. Finally, we asked LPBs about the changes they would like to see in their audit. In terms of the relationship, a small proportion of respondents would like to see specific improvements. 16 per cent of authorities would like 'closer/better working relationship' with their auditors. One-fifth (20 per cent) would like to see 'better/more regular communication'. There was more consensus around the cost and impact of audit work. Around half would like to see the fee level (53 per cent) and time burden reduced (50 per cent), more emphasis on the 'big picture' and less on detail (44 per cent), and more proportionate/risk-based audit (44 per cent). Notable proportions of respondents would also like to see improvements in terms of continuity of auditors (41 per cent), more working together or joint approaches with other agencies (34 per cent). These all relate to the efficiency and burden of the audit process. A follow up survey and case studies would focus on whether LPBs are more satisfied in these areas.

Table 14: Changes LPBs would like to see made to improve impact of audit (selected answers)

Type and scale of work carried out	
Fee level reduced	53%
Time burden reduced	50%
More emphasis on the 'big picture' and less on detail	44%
More proportionate/risk-based audit	44%
Staffing and relationships	
Closer/better working relationship	16%
Better/more regular communication	20%
Improve continuity of auditors	41%
Working together or joint approaches with other agencies	34%

3.4.11. *Indicator 8: Measure of the technical quality of audit*

Indicator: Measure of technical quality of audit undertaken (where quality is defined as compliance with the Audit Commission's regulatory requirements and with professional standards).

134. The Audit Commission assessed the quality of the work of the firms to whom it let contracts. There were two strands – compliance with regulatory requirements for delivering audits, and assessment of the quality of work under the quality review programme. The Audit Commission stated that:

'In assessing the quality of financial statements audits, we use the work of the Financial Reporting Council's Audit Inspection Unit (AIU). The AIU reviews the firms' systems for ensuring audit quality and a sample of their audits of listed companies. It publishes public reports on each of the firms in our regime, which provide an independent view on the quality of the firms' work. In addition, we commission the AIU to review cyclically the quality of the firms' financial statement audits at a sample of Commission engagements.'⁶²

135. **Baseline position:** Overall, on their work on 2009/10 audits the Commission concluded 'We are satisfied that the risks of audit failure remain low and suppliers are meeting the Commission's regulatory requirements and standards of performance; and the requirements of professional auditing standards. However, there is scope for all suppliers to improve their work by:
- Responding to the findings of the AIU's annual inspections.
 - Ensuring compliance with our specified methodology for the certification of housing and council tax benefits subsidy claims.

⁶² Audit Commission. 2010. Quality Review Programme. Annual Report 2010. Online: <http://webarchive.nationalarchives.gov.uk/20150421134146/http://www.audit-commission.gov.uk/about-us/annual-report-and-accounts/> (accessed 1 April 2016).

136. The AIU's summary report on its inspections in 2009/10 of the work of the big four and 'other significant' audit firms, concluded that 'each firm places considerable emphasis on its overall system of quality control and, in our view, has appropriate policies and procedures in place for its size and its client base. Nevertheless, we have identified certain areas where improvements are required to those procedures.'⁶³
137. The Commission added that 'The results of the AIU reviews that we commissioned on a sample of Commission engagements for 2009/10 confirmed that the financial statements audits complied with: auditing standards; ethical standards; and the quality control standards issued by the Financial Reporting Council's Auditing Practices Board.'⁶⁴
138. The published 2011 and 2012 reports do not provide ratings, but they are available in the 2013 edition for 2011/12.⁶⁵ The data in Table 15 (below) shows that all firms were rated as Amber or Green. These ratings are not defined, although we were told in an interview with a former member of Audit Commission staff that at least 'Amber' was the expectation for an appropriate level of quality. The report states that the Commission was satisfied that the risks of audit failure were low; that firms were meeting its regulatory requirements; and that they were continuing to produce work to 'an acceptable standard' (page 4).

Table 15: Combined regulatory compliance and audit quality performance scores 2011/12

Green	Amber	Red
Deloitte	Audit Commission	
KPMG	Grant Thornton	
	PKF	
	PwC	

139. As part of its assessment of the quality of firms' work, the Audit Commission monitored compliance with its regulatory requirements. The data for delivery of audit opinions to target dates showed an average of 95 per cent compliance, and where target dates were not met, the Commission considered this was due to reasons outside auditors' control.

Table 16: Regulatory compliance 2011/12

Firm	Local Govt%	NHS%
Deloitte	90	100
Grant Thornton	98	100
KPMG	95	100
PKF	94	100
PricewaterhouseCoopers	85	93

140. These indicators cover different aspects of the **quality of the audit process**. Deterioration in performance against these indicators would raise concerns that standards of audit were not being upheld.

⁶³ Audit Commission. 2011. Quality Review Programme. Annual Report 2011, p. 5-6. Online: <http://collections.europarchive.org/tna/20121114095218/http://audit-commission.gov.uk/subwebs/publications/corporate/publicationPDF/3692.pdf> (accessed 1 April 2016).

⁶⁴ Ibid.

⁶⁵ Audit Commission. 2013. Annual Report 2012/13. Online: <http://webarchive.nationalarchives.gov.uk/20150421134146/http://www.audit-commission.gov.uk/about-us/annual-report-and-accounts/> (accessed 1 April 2016).

3.4.12. *Indicator 14: Meeting of statutory deadlines for accounts and audit*

Indicator: Number of cases:

- **Approval of accounts not done by 30 June 2010.**
- **Delays in having accounts published.**
- **Audit opinions not issued by 30 September.**

141. An important aspect of the quality of audit work is its timeliness; late accounts or delayed audits may be indicators of poor financial health or organisational stress. There are a number of statutory stages in the audit process. Meeting these deadlines ensures that audit opinions are given in a timely manner and that accounts are published, which supports transparency and accountability for use of public funds. For the baseline year, data can be obtained from Audit Commission's report 'Auditing the accounts 2009/10'⁶⁶ or individual audit letters.

142. **Baseline position:** The position against each of the stages is set out below in Table 17.

Table 17: Performance against statutory timetable for accounts

Approval of accounts not done by 30 June 2010	Six bodies did not approve their accounts by the statutory deadline (1%)
Number of delays in having accounts published	94% of councils, 97% of police authorities, 97% of fire and rescue authorities and 81% of local government bodies had published their 2009/10 accounts by 30 September 2010 as required
Audit opinions issued by 30 September	92% of councils (329) and 80% of local government bodies (77) had had their audit opinion issued by this date. The audit opinion had been issued at all police (38) and fire and rescue authorities (31) by 30 September

143. The evaluation will need to take account of changes to statutory publication dates – which will be brought forward to 31 July from the 2016/17 financial year for principal authorities. Public bodies must also publish, alongside the accounts, both a governance statement and a narrative commenting on the economy, efficiency and effectiveness of the authority. Compliance with these requirements can be considered a crucial aspect of transparency and accountability for local bodies

⁶⁶ Audit Commission.2010. Annual report and accounts 2009/10. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/247750/0124.pdf (accessed 1 April 2016).

3.4.13. *Indicator 12: Firms' satisfaction with the regulatory regime*

Indicator: Level of satisfaction of satisfaction of audit firms with new regulatory regime.

144. The Audit Commission undertook the regulation of audit firms. In April 2015, the NAO and the FRC took over aspects of the regulatory regime. The NAO will take on responsibility for the Code of Audit Practice and guidance, which sets out the ways in which auditors carry out their functions. The FRC became the overall regulator of audit standards, mirroring for local audit the arrangements under the Companies Act 2006. In addition, the FRC will specify one or more professional accountancy bodies as 'registered supervisory bodies', which will be required to have a range of regulatory roles over their membership to ensure that local audit work can only be carried out by auditors and firms with appropriate qualifications and experience. This will include inspection of a sample of local public audits. The FRC will itself review a sample of 'major public audits' each year.
145. Evidence on this indicator came from the interviews with partners of the audit firms. We asked questions about their views of the Audit Commission regime and any initial views on the new regime. The latter was generally hard to answer for firms as the impact of the changes have yet to be felt. We interviewed partners leading local audit work in seven audit firms, including those:
- Currently undertaking local government work.
 - Which had now completed their current local government contracts, having not secured work in the most recent procurement.
 - Which had returned to local government audit after a period out of the sector.
146. The firms also covered the audit of all kinds of local public bodies, both principal and smaller authorities, and in different parts of the country. In many cases, the partners had many years' experience of working with the Audit Commission. They were all members of the Local Auditors' Advisory Group, now facilitated by the NAO, and so were identified as the lead partner of local public body audit work.
147. **Baseline position:** Our interviews with audit firms give us a **mixed impression of the Audit Commission' regime**. Interviewee perceptions of the Commission's staff were generally positive. Several talked about having a **good relationship with the Commission or individuals within it**, at both senior and more day-to-day levels [3, 4, 7]. One described Commission officials as 'good people to work with, open and constructive' [3]. On the other hand, a number of interviewees also commented they felt the Commission could be **bureaucratic** and, particularly latterly, tended to afford disproportionate weight to administrative performance indicators, such as meeting deadlines [2], rather than audit quality, and required a lot of returns to be completed. Some felt their procurement and monitoring processes could be inefficient and costly [4, 5, 7].
148. Some interviewees [3, 4, 5, 7] drew a distinction between **their relationship with the Audit Commission before and after 2012**. This had moved from a more collaborative relationship (described by one partner as a 'family' approach) towards one more characterised as contract management and compliance [4]. Another firm [5] described the differences as being between being 'the eyes and ears' of the Commission and experiencing a 'micro-managing contract relationship'. It was also suggested, for example, that latterly there was inflexibility about meeting deadlines, which did not take account of the additional effort that auditors had put into helping bodies. Also, although previously

firms had competed for work, they had also collaborated a lot in what they saw as the interests of consistently applied public sector audit, and had contributed to Audit Commission projects. This had been lost towards the end of the Commission's time [4]. Two firms [4, 5] talked about the Commission 'losing its way' towards the end with its VfM and CAA work.

149. The Commission was also seen to have been **helpful in providing technical support, research and guidance** [6]. On the other hand, it was suggested that they could have done more to provide guidance on how non-financial statement audit should be done and encourage greater consistency amongst auditors [2].

3.5. Baseline views from local public bodies on the reforms

150. Our survey of LPBs also asked for their views on aspects of the reforms in order to understand whether the problems which they were designed to address were widely seen as in need of resolution. Any future evaluation would be able to repeat the questions and assess the extent to which these issues have been overcome in the view of audited bodies.
151. There was no consensus as to whether **local appointment of auditors** would be valuable for the audited organisation. **13 per cent** agreed strongly with the assertion that it would be 'valuable', whilst **23 per cent** agreed 'somewhat'. However, **one third** neither agreed nor disagreed, and **13 per cent** 'strongly disagreed'. A further 1 per cent 'did not know'. Notwithstanding these results, at the same time the majority of bodies considered they would be well equipped to make an **informed choice about their auditors**. Specifically, only **five per cent** of the respondents strongly disagreed that it would be the case, while **60 per cent** agreed with the statement.
152. Where they provided an explanation, some respondents expressed concerns about being able to select appropriately due to lack of time, experience, and/or personal capacity. In particular, they were worried that the choice would not be adequately informed as the search for more details on options would be too costly. Moreover, economies of scale in choosing auditors on the national level and simply more work for the authorities were a common reason being concerned about local appointment. In other opinions, some respondents thought that audit arrangements were best made independently of the organisation being audited, that the current arrangements were good enough and some specifically valued the fact that the auditors were appointed independently.
153. We also asked **what plans local bodies had at this stage for the new contracting arrangements**. Some **11 per cent** of respondents envisaged they would go alone in appointing the next auditor, while **33 per cent** expected to participate in a joint procurement exercise with other bodies, and a further **35 per cent** would take advantage of a sector-led body if it was established. This suggests that while many authorities felt capable of making the selection themselves, it may not be their favoured choice, with a majority favouring some form of collaborative approach.
154. The government's reforms are designed to **improve audit arrangements and reduce audit fees**. We asked local public bodies whether they expected the change to affect the **quality of the audit work that they received**. The table below shows that around half of respondents thought it would make no difference, and a quarter believed it would lead to an improvement.

Do you expect that the changes to the local audit regime will:

Improve the quality of audit of your organisation (e.g. the usefulness of the work, quality of contact with the firm)	25%
Make no difference	52%
Lead to a decline in the quality of the audit of your organisation	4%
Not sure/ don't know	19%

155. We also asked local bodies whether they expected the reforms to **affect audit fees**. The responses perhaps inevitably showed considerable variation and a degree of uncertainty. This may reflect genuine uncertainty, or could reflect the view that how the market will react to the changing demands and risks (seen in the mixed views of firms on how they might respond) is currently unknown.

Do you expect that the changes to the local audit regime will:

Lead to the audit fee charged by your auditor to your organisation going down	26%
Make no difference to the audit fee charged by your auditor to your organisation	20%
Lead to the audit fee charged by your auditor to your organisation going up	25%
Not sure/ don't know	28%

3.6. Baseline views from audit firms on other aspects of the reforms

156. Indicator 12 (paragraph 3.4.13) discussed firms' views on the previous regulatory regime. Our interviews also asked partners for observations on other aspects of the reforms.
157. Overall, there was an **acknowledgement and understanding of the rationale for the changes**, which were considered 'valid', in the words of one interviewee [1]. Another [7] stated they understood and supported the need for change, although their concern was how to maintain quality in a freer market. Some firms had contributed in writing or orally to parliamentary hearings during consideration of the legislation so they felt they had had the opportunity to contribute to the consultation process, but other firms had made no statements. Another spoke positively about the idea of local appointment [2]. At the time of the interviews there **remained uncertainty** in the local government field about the future procurement vehicle for local authorities, even if this had now been resolved for health bodies and smaller authorities. This was reflected in respondents' comments. The robustness of the new registration processes for audit firms was also an unknown at the time of the interviews [1].
158. There was also a sense from some interviewees [1, 5, 6] that the **biggest changes had already taken place** in 2012, when the Audit Commission's in-house practice was outsourced, so that more recent changes were a continuation of a programme that had been under way for some time. Firms also felt they had modernised and made more efficient the audit work previously undertaken in-house, so that **improvements to audit arrangements had been under way for several years already**.

159. There was a clear sense from firms that **local audit had particular expectations and demands** because it involved public money and accountability. Some referred to ‘the principles of public audit’ which influenced their approach [1, 2, 4], and also underlined that local government work had elements of a ‘quasi-legal role’ which made it special and interesting. This brought with it a wider sense of acting in the public interest than the audit of companies, and hence the Audit Commission’s previous role and ethos, and its expectations of them as contractors was understood against this background. As a result, reforms were judged by several interviewees in terms of whether they might run counter to long-established views on the requirements of public audit.
160. Five (out of seven interviewed) firms expressed concern at the likely **inefficiencies in terms of transaction costs** associated with multiple small procurements, rather than larger ones. There was concern that an increased amount of work would need to go into having to tailor tenders to particular local circumstances, which was not a ‘trivial matter’, according to one firm [3]. Another [5] expressed concern at ‘multiple routes to market’ emerging and hundreds of bodies all tendering over a short period of time. There was general preference for some form of framework or collective system, or geographical lots [1, 3, 4], under which firms would be able to tender more economically. On the other hand, one firm [2] was very positive about the **prospect of local body involvement in auditor appointments** and felt any risks here would be managed by the professionalism of the firms and the strong regulation of the industry.
161. **Greater transparency around fees** than under the Audit Commission regime was mentioned favourably by one firm [2]. There was, however, **some scepticism from several as to whether major additional savings would really materialise** and whether the objectives of widening the market would take place [4, 5], except perhaps for some of the recent participants returning. One firm suggested that it had previously tendered at cost in order to maintain a hold in the market [3], whilst another [5] said that fee reductions had been partly been achieved by de-scoping and that levels would not be sustainable. Interviews with these partners identified a number of potential risks facing the new audit regime (Table 18).

Table 18: Potential risks to the success of the new regime

Theme	Issues raised
1. Impact on the quality of audit	<ul style="list-style-type: none"> • Did not consider any firms would allow quality standards to drop, but main risk was to ability to 'add value' and be as flexible as in the past
2. Impact on VfM work	<ul style="list-style-type: none"> • Lowering fees could risk reducing VfM work to 'tick-box' exercise • Risk of misinterpretation both locally and nationally as to what assurance is being provided
3. New regulatory regime	<ul style="list-style-type: none"> • Alignment of regulation between local audit and companies work seen as sensible • Generally too early to comment but some concern at fragmentation with different bodies involved • NAO seen to have started effectively in new role, and sensibly recruited number of former Audit Commission staff for continuity and expertise
4. Reduced incentives to collaborate with other firms	<ul style="list-style-type: none"> • Reduced incentives to work together and share intelligence in the interests of public sector audit as a whole
5. Specialist nature of public sector audit and challenges to market entry	<ul style="list-style-type: none"> • Specialised nature of local audit made it hard – but not impossible – for firms new to the field to move into it • Significant costs associated with operating in the sector – back office expertise, etc. • Would be possible to recruit specialist staff but would need to do so before winning work and possibly at a premium to get people to move
6. Smaller bodies	<ul style="list-style-type: none"> • Audit of smaller bodies likely to be less attractive than larger ones, making it harder to find auditors and risking higher fees
7. Local accountability and transparency	<ul style="list-style-type: none"> • Potential for conflicts of interest where local appointment might influence willingness of auditors to raise concerns at risk of non-renewal of contract • Insufficient experience amongst audit panels of local public bodies to judge needs and make appropriate appointments

3.6.1. *Impact on the quality of audit*

162. Our interviewees **did not consider that any of the firms would allow standards to drop** as a result of the reforms and the changing market. In any case, all would continue to be judged by the same quality monitoring bodies and remain under the same pressures to maintain their reputations by delivering work to appropriate standards [2, 3]. Several mentioned the desirability of being able to differentiate their 'offer' in a competitive market and hoped that future procurements would focus more on quality than just price [2, 5, 6], which was seen as lacking in recent procurements. Any **risk to quality was seen in terms of their ability to 'add value' and be 'flexible'**, with additional competition and pressure on fees limiting what 'added value' could be considered as part of the service, given reduced profit margins [3]. Thus, they did not expect an impact on basic audit standards, but felt the wider benefits of engaging a large and experienced firm might be lost. Another firm [6] worried about a procurement process failing to recognise the importance of independence and the valuable role that auditors should be playing, and rather overemphasising price.

3.6.2. *Impact on value for money work*

163. Linked to this was how respondents considered fee levels could potentially affect VfM work [1,3, 4]. One interviewee [4] noted that the appropriate level of assurance needed for a VfM assessment can require a 'chunk' of fees. Lowering fees could risk reducing VfM work to a meaningless 'tick-box exercise' given the complexity of local authorities and the less prescriptive requirements of this type of work. They felt this would not help local bodies secure VfM, and risked being misinterpreted at local level (e.g. by members of audit committees) and nationally (e.g. an example was quoted of a minister referring to them in a way which placed much more reliance on this work than was merited) [3]. One interviewee [4] drew on the example of NHS trusts, where they considered that VfM was not great, but where he did not think attempts had been made by auditors and trusts to work together to remedy this. Two interviewees noted that any judgement on VfM made under such arrangements should not be conflated with a *positive* judgement on VfM. Another interviewee considered that expectations under new NAO proposals would require additional work, but the NAO guidance was seen by one firm [6] as having provided much more clarity about what was needed.

3.6.3. *New regulatory regime*

164. Under the new regime, responsibility for regulatory oversight has transferred to the FRC and the National Audit Office. A number of interviewees noted that continuity was maintained in some ways, for example, with experienced and trusted staff responsible for the Code of Audit Practice transferring from the Audit Commission to the NAO, which was seen by several interviewees to have started effectively [1, 3, 4, 6]. The **alignment of regulation between local audit work and companies' work was seen as a sensible development**, with a whole-firm review helpful. Firms were also **positive about any steps to make the regulatory regime less bureaucratic and process driven**, whilst fully acknowledging that review was essential [4]. FRC, NAO and AQRT monitoring were recognised as appropriate, rigorous and very thorough [5]. However, although it was quite early to comment, and initial signs were considered positive, one interviewee [1] spoke of **the potential for the regulatory regime to become fragmented and increasingly inefficient** where functions formerly centralised in the Audit Commission were split across several authorities. The risk was that what was formerly 'one conversation' about the work will now be held with multiple actors. Other interviewees also considered that the break-up of the Commission's responsibilities meant that the benefits of having one body with an overview would be lost, or some of the benefits of their regularly updates would be lost [6].

3.6.4. *Potential for reduced incentives to collaborate with other firms*

165. One interviewee [6] suggested that there were likely to be **reduced incentives for firms to work together and share knowledge in the interests of public sector audit as a whole**, as had been the case under the old frameworks. He noted that past coordination at a national level had lent itself to activities to develop and add value to the wider public audit sector, and the Audit Commission had required participation. This particular firm had developed a 'centre of excellence' and provided training, benchmarking and thought leadership as a way of 'adding value'. The 2012 and 2014 tenders had already led to a change in approach and mind-set, and relationships were seen by some interviewees [3, 4, 5] to have become primarily one of contract management and compliance. Some collaborative initiatives that had previously been facilitated by the Audit Commission

framework, such as study projects and review processes, the national fraud survey, and other national-level information initiatives would not necessarily be replicated under the NAO. As one firm put it, 'if you want competition, you have the effects of it as well' [6]. The interviewee was hopeful, however, that this might change going forward, and was encouraged by the position of the NAO, and was hopeful that it would use its new position to support value-added activity such as coordinated feedback.

3.6.5. Specialist nature of public sector audit and challenges to market entry

166. One objective of the reforms is to increase competition and specialised new providers to enter the local audit market. In passing it was observed by several interviewees that there had actually been a reduction of two in the number of firms operating in the field as a result of the last procurement exercise [1, 3, 4, 5]. During interviews, several firms [1, 5] suggested that the **specialised nature of public sector audit would make it hard – but not impossible – for firms new to the field and lacking the name recognition to move into it**. The work required staff with specialist knowledge able to understand and to navigate the particular needs of the public sector. It was acknowledged that public sector work was not considered attractive by many of their staff, but for others it was the only work they wanted to do because they had an interest in and cared about the public sector [4].
167. Specialist knowledge and skills could be bought by new entrants, but firms would have to do so before they had secured the work, which was a risk, and it was assumed they would probably need to pay a premium to get qualified staff to move from their existing established employers, possibly increasing audit costs. Those firms that had won in 2006 were seen as having a very dominant position in the market, although it was acknowledged that, for example, Ernst & Young had returned to the field more recently [4]. Continuing to operate in related fields such as foundation trusts or housing associations was seen as beneficial for those firms who may want to re-enter the market [7]. However, some of the firms which lost work recently were thought to be struggling to hold on to staff [5].
168. There were, however, substantial **costs associated with operating in the sector**. Firms needed some back-office technical and operational support specific to public sector audit. One interviewee listed sector and industry training, audit methodologies, procedures and software all tailored to the specific conditions of the public sector [7]. One respondent highlighted that firms not currently inspected by the FRC Audit Quality Review (AQR) team would also find the cost of entering the market was high [6]. Another interviewee [4] estimated that a minimum £2m of audit work was needed to justify the 'centre of excellence' required to develop capacity and expertise for public sector work. Another put a figure at around £5m of contracts [1]. Such expertise was also seen as a way of differentiating their offer and adding 'value' through 'thought leadership' contributions, benchmarking exercises, etc.
169. Another interviewee [3] noted that, given the uneven nature of local government spending and audit work across the financial year, a 'balanced' portfolio of work is required to sustain activity outside of peak times. However, changes coming in to bring forward the local authority audit timetable to July, meant that local government work will need to be undertaken at the same time as other work, whereas previously there peak times were different.

3.6.6. *Smaller bodies*

170. Observations were made about the **impact of local-led appointments on price and auditor choice for smaller entities**, such as district councils. Under the previous arrangements, larger firms would be allocated smaller entities for audit alongside larger entities. An interviewee [6] and the written submission by Mazars and BDO⁶⁷ noted that, if larger firms were to focus primarily on contracts for larger authorities to maximise market share and returns, smaller bodies (such as district councils) and authorities in geographically remote locations, might struggle to appoint auditors. Firms [6, 7] assumed that most would want to audit many of the same organisations. This may result in increased costs for smaller bodies, as they may have to pay more to attract larger firms, or could lead to audits of sub-standard or inconsistent quality; the written submission by Grant Thornton noted that this was suggested by the Audit Commission's experience of tendering for contracts in Cornwall and Cumbria.⁶⁸ Similarly, smaller audit practices bidding for smaller contracts or contracts for geographically isolated entities may have to increase salary levels to attract experienced staff, thereby raising operating costs. Some interviewees also raised concerns about **smaller bodies' ability to attract suitably experienced individuals** to audit committee or independent audit panels. Some examples of very poor understanding were mentioned.

3.6.7. *Local accountability and transparency*

171. A further objective of the reforms is to enhance local accountability and transparency by placing choice of auditors or selection processes in the hands of audited bodies, rather than at a central level. The new system will see authority over appointments handed to local public bodies, meaning that the local public body being audited will also be the body responsible for awarding audit contracts. If this happens, this will be overseen by audit panels at an entity-level or sector-level, of which a majority of members must be independent.
172. A concern voiced by several interviewees was that the move to local-led appointments could present **potential conflicts of interest** for firms, as raising concerns or challenging clients on points of audit could be seen as a risk to renewal of a contract and thus act as a commercial disincentive. One interviewee saw this as a risk to a fundamental principle of public audit, whilst another indicated that whether they liked it or not, firms would inevitably be aware of this possibility when considering whether to present uncomfortable messages [1, 4]. One interviewee suggested that making appointments through a larger framework contract controlled by a representative body (such as the LGA) would offer protection in this regard [4]. However, two interviewees felt professional standards and regulations were sufficiently challenging to ensure quality in audit, and firms would not risk their professional reputation by lowering their standard of audit quality [2, 3]. Another emphasised the importance of the professionalism of individual auditors [1]. Any future evaluation should seek to follow up on these issues, although they are sensitive and hard to prove.

⁶⁷ House of Commons. 2010–12. Audit and inspection of local authorities. Online: <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmcomloc/763/763.pdf> (accessed 1 April 2016).

⁶⁸ House of Commons. 2010–12. Audit and inspection of local authorities. Online: <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmcomloc/763/763.pdf> (accessed 1 April 2016).

173. Linked to this, the idea of independent local audit panels raised the issue of **experience and quality of members** for some firms. The written submissions by Mazars and Deloitte⁶⁹ highlighted the need for those making audit appointments at a local level to have sufficient experience and knowledge to make effective decisions. This was echoed in interviews; one interviewee noted that although larger public bodies (such as London boroughs) and health bodies may have people with sufficient existing expertise, smaller bodies such as district councils may require additional training. Another considered it was hard to see that they would be well equipped to handle decisions.
174. A similar concern was raised over the **exercise of auditor's powers**, which under the new regime will be recoverable from audited bodies should auditors choose to pursue public interest activity or objections. The written submission by Mazars⁷⁰ highlighted the need for transparency in how the costs of investigating complaints and producing Public Interest Reports would be covered; insufficient indemnification for costs could lead to auditors refraining from using this power, even if in the public interest to do so. If such costs are built into auditors' insurance premiums, this could in turn raise fee levels.

3.7. Issues raised by other stakeholders during the project

175. We interviewed a wide range of stakeholders including the Financial Reporting Council, LGA and the National Audit Office (see Appendix A for full list) to secure their perspectives on the reforms. In some cases the discussions were restricted to particular aspects – for which interviewees were responsible or had specialist knowledge.
176. In our interviews we got the impression that, when considering a major reform of practices, there could be an overall tendency for those involved to focus on risks rather than the anticipated benefits. A number of stakeholders nevertheless welcomed the **opportunities for efficiencies that the changes** have offered – for example, drawing local audit into the existing oversight and quality regimes for private firm audit under the FRC, or for extending the Code of Audit Practice to foundation trusts and so broadening the Comptroller and Auditor General's responsibilities around public audit as a whole [1, 2]. Some stakeholders also commented positively on the **reduced costs and increased efficiencies associated with the contracting out of audit work** since 2012 [6, 10]. And the **opportunities of sector-led bodies** were also highlighted by several stakeholders, who saw them as a way of reconciling the benefits of more local control with delivering value for money [5, 6, 10].
177. Stakeholders also set out what they considered to be risks that they (collectively or individually) would need to manage. Some of these echo those raised with us by the audit firms and we have chosen not to revisit them again in detail. In particular, stakeholders:
- **Acknowledging the different nature of public sector audit and its effect on developing a market:** A number of stakeholders [1, 3, 7] felt that the legitimate desire of government to open up the local audit market to new players did not

⁶⁹ House of Commons. 2010–12. Audit and inspection of local authorities. Online: <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmcomloc/763/763.pdf> (accessed 1 April 2016).

⁷⁰ House of Commons. 2010–12. Audit and inspection of local authorities. Online: <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmcomloc/763/763.pdf> (accessed 1 April 2016).

sufficiently recognise the unique and complex nature of public audit, nor that it was a specialist form of work. As a result, not all audit firms had the knowledge and skills to undertake it, and so there were significant barriers to entry for new firms (e.g. skills, knowledge, experience, etc.), which could limit the amount of choice that could be generated. One [4] considered a major expansion of participants was unlikely, particularly outside the top ten firms. The greater publicity associated with public audit also added to the risks for new firms, which needed to be factored in to costs. In addition, they considered eligibility criteria were a constraint for new entrants. The 2014 legislation provides the FRC with the power to determine detailed guidance on eligibility criteria, specifying for example the level of public sector experience required (currently, key audit partners auditors must have two years of post-qualification experience gained in the last six years). If these provisions remain the same and the contracts are also extended until 2020 in addition to that, then this might represent a significant barrier to market entry for firms which are currently not operating in the market.

- **The impact of a reduction in fees on quality:** Two stakeholders [3, 4] commented that driving down costs and fees could have an impact on the quality of audit. The FRC's role on quality would be very important in managing any risks here, but it was assumed that firms would be monitoring themselves carefully given the reputational risks, as will the regulatory bodies [4]. The challenges under which local public bodies are increasingly finding themselves with reduced resources could also mean their financial management was less effective, adding to the complexity and the risks for the auditors. This would make working in the sector more challenging and arguably more costly. Linked to this, despite the reduction in fees, one stakeholder [1] expressed concern that DCLG may be assuming the ability to place more weight on the work of auditors than is consistent with fee levels and the scope of audit.

178. The remainder of the major issues raised are set out here so that they can be followed up in the potential future evaluation. They are couched in terms of risks, but this does not mean that they will necessarily materialise, or if they do, that they will have any important impact on the quality of audit arrangements. They are nevertheless issues which a possible future evaluation will need to be aware of when reviewing developments.

3.7.1. Possible loss of skills in the sector

179. Some stakeholders expressed concern about a **possible loss of specialist skills and expertise** in the sector, which would become spread more thinly. The Audit Commission had a large pool of staff with considerable expertise in local audit. Many of these people moved to the private firms undertaking local audit work when the work was outsourced. The age profile means that many will retire in the coming five to ten years. It was argued that there is a risk that local public bodies could start to experience a decline in expertise, and that expertise will be (thinly) spread across the market. It was known that some firms were aware that they will have to train the next generation of local auditors, whereas they have benefited from the ex-Audit Commission field force in recent years [7].
180. On the other hand, one interviewee [2] highlighted that the legislation is drafted in a way that enables accountants who have qualified with the major accountancy bodies to carry out work both for the private and the public sector including local audits. Staff with the right competencies should therefore be able to transfer their skills to any sector. The same interviewee mentioned that it will be difficult to monitor the potential skills loss in the

market given that data from members' surveys of the accountancy bodies are voluntarily, do not necessarily distinguish between public sector and local audit, and individual data cannot be shared under the Data Protection Act (which means only broad overall numbers of how many auditors work in the public sector might be available).

3.7.2. Potential gaps in coverage in remote areas and for smaller bodies

181. A number of stakeholders [1, 7] raised the potential risk that some bodies in remote areas may struggle to secure audit coverage. Larger authorities and those closer to areas of high population will have the purchasing power for securing high-quality audit services, whereas smaller parish councils might not [5]. As a result a sector-led body was seen as sensible to secure best value [since the interview this has been set up]. Location could also be a factor that leads to a reduction in choice and, therefore, quality of audit for these bodies. Furthermore, it was suggested that while there had been a certain prestige involved for firms in working for the Audit Commission, auditing parish councils for a procurement body might not have the same level of external recognition [5].

3.7.3. Impact of different procurement routes

182. Some stakeholders expressed views on the possible procurement routes for local audits in future. Two [3, 4] emphasised that costs and fee levels will be influenced by the different procurement vehicles chosen, and that larger local public bodies or sector-led arrangements would be in a better position to influence costs. Others [5, 6] argued that national procurement or a sector-led solution was more likely to deliver reductions in costs, whilst there will be additional costs for procurement and setting up independent panels if that route is chosen [4]. There were different views on the idea of a sector-led body. Whilst several were keen, one interviewee [7] thought they sounded an easy solution but were quite hard to organise since firms' bodies would need to sign up before they knew what they could secure this way, and firms would not promise a price until they knew how much work there would be.
183. We were pointed towards recent (July 2015) research by the Local Government Association⁷¹ to ascertain the level of support/interest across the sector for extending existing audit contracts for up to three years, and also the level of support for setting up a sector-led body to procure external audit on behalf of councils and other bodies. The survey was sent to Directors of Finance (or equivalent) in 353 English local authorities, 47 Fire and Rescue Authorities, 38 Police and Crime Commissioners and 39 Police Forces. The overall response rate was 38 per cent. The key findings were:
- **Eight out of ten respondents** indicated that their organisation would support extending the current contracts for external audit by up to three years.
 - **Some 58 per cent of respondents** said that their organisation would prefer 'an opt-in sector wide body for collective procurement set up by the LGA' in the future.
 - **Three per cent** said it would prefer procurement of its own auditor, including setting up an independent Audit Appointments Panel.

⁷¹ Local Government Association.2015. 'Future of external audit survey results'.

184. Furthermore, it was reported that local appointment can potentially increase the cost of an OJEU notice, and councils might struggle to find suitable candidates for an independent audit panel, which could decrease the likelihood of councils opting for local appointment.

3.7.4. Oversight of sector development and performance

185. Under the reforms, responsibilities for monitoring and oversight of the firms and local audit arrangements are being dispersed between different organisations (see Part 1). Stakeholders identified a number of challenges with these organisational changes. In particular:

- **Ability to identify emerging problems at local level:** One stakeholder [1] advised that one of the most testing challenges for the new regime will be having the ability to know what is happening at local level and whether to intervene in the event of local failure. This includes the issue of whether there are adequate early warning signs of problems which might trigger the need for intervention.
- **Fragmented oversight will require good coordination and feedback loops:** As a result of different organisations having specific responsibilities previously held by a single body, some stakeholders [1, 3, 9] considered there was an increased risk that it becomes harder to influence the quality of work undertaken by audit teams at local level. The NAO is responsible for developing a Code of Audit Practice which is a high-level and principles-based document, but is not responsible for issuing accounting guidance and is not an auditor of local bodies. This means that the NAO has limited ability to see how its guidance is implemented on the ground. The FRC is responsible for the audit quality monitoring and review work, although one interviewee [1] said it remained a question as to how prominent a feature local audit was within the FRC's overall feedback to firms. As a result, there is a need for good feedback loops and information sharing between responsible bodies to ensure that there is shared understanding. Some of the risks were being mitigated by the creation of memoranda of understanding between bodies [1, 3], and another stakeholder [4] emphasised that many of the bodies already had a track record of coordination in other areas and talked regularly.
- **More constrained value for money role for NAO:** Although the NAO now has a value for money remit in local government, it expects to publish only about six studies a year, based on a risk-analysis. It is constrained to looking at sector-wide issues and does not have the same network of staff with direct contact with local authorities. It was therefore seen by a number of stakeholders as playing a more limited value for money role compared to the Audit Commission [3]. As a result, other sector-led sources were seen as helping to fill the gaps. One interviewee mentioned [6] the LGA's Local Government Inform benchmarking data service for councils and fire and rescue authorities. LGA had developed this with local government to try to find an approach to improvement based on the sector's own learning about what works best. It brings together key information for authorities, as well as contextual data and financial information. Users can view a wide range of data, make comparisons between authorities and other councils or groups of councils, or construct their own reports bringing several data items together. The aim is that data is updated quickly after being published at its source.⁷² Any future

⁷² LGA. 2015. LG Inform. Online: <http://www.local.gov.uk/about-lginform> (accessed 1 April 2016).

evaluator could explore with the LGA the uptake of Local Government Inform by local authorities and the type of information they seek out (or reasons for a lack of uptake the service does not provide the right type of information).

- **Monitoring and information gathering:** With the demise of the Audit Commission there is no central collection of information on different aspects of local audit, or anybody tasked with monitoring developments in the market and the overall local audit regime (for example, information on future procurement costs and fee levels). This was mentioned by some interviewees [1, 3] who feared this could lead to a lack of information required to maintain oversight of the local audit regime.

3.7.5. Benefits of consolidating audit quality within one regulator

186. The regulatory and oversight regime for local audit will mirror the systems that apply to the audit of entities under the Companies Act, and from the perspective of a firm that works across sectors, procedures will be broadly consistent across both. One interviewee [2] mentioned that there is an established and robust system of independent oversight and monitoring of the auditing profession by recognised supervisory and qualifying bodies which is well established for covering statutory audit and will be extended to cover also local audit. Existing procedures and systems will be adjusted to take note of any elements specific to local audit. FRC's Audit Quality Review (AQR) team will review a sample of audits done for the principal local public bodies as well as annual reports on each major audit firm, which will also cover their activities around local audit. This will present a major source of evidence on whether standards and quality of audit are upheld over time. FRC will also develop a register of local public auditors and a transparency report (starting when the firms have conducted their first local audits after the market has been fully opened, i.e. late 2018 at the earliest), which will look at the level of transparency of local audits focusing on the audit firms.

3.7.6. Smaller authorities

187. In keeping with comments from a number of audit firms summarised in paragraph 3.6.6., a number of other stakeholders made reference to issues relating to smaller authorities. The main issues mentioned were:

- Several stakeholders (interviewed during 2015) referred to concerns about the position of smaller authorities, particularly around a lack of purchasing power and likely levels of interest [5, 10].
- There was concern that any new arrangements should still be commensurate with the amount of public money involved, and that the lighter touch regime which had been in place since 2003 should be maintained since it was seen to work. This included a simple accounts format and self-certification.
- The challenge for the reformed regime will be how to assess the quality of audits.
- The transparency of spending by smaller authorities was seen as important and one stakeholder [5] pointed towards the £4m of new burden funding to cover the cost of improved websites for transparency purposes.

188. Subsequently, the Government announced in December 2015 the setting up of a sector-led body for smaller authorities: the Smaller Authorities' Audit Appointments Limited

(SLAA).⁷³ All bodies with an annual turnover of less than £6.5m are automatically part of the scheme unless they decide to opt out by 31 March 2016 and appoint their own external auditors. In December 2015, SLAA issued details of fee rates for bodies which were on a sliding scale dependent on income and expenditure, with the aim that they would not exceed the fees applicable for the review of accounts for 2014/15.⁷⁴

189. An interesting issue for the very small bodies – those spending below £25,000 – which decide to opt out of the sector-led arrangements, is that they still have to appoint an auditor. They are still required to follow the extant guidance. SAAA advised us that it will soon send out guidance emphasising the obligations and highlighting, for example, that if an issue arises or a PIR is required, they will have to pay. Investigation costs could be quite high.

3.7.7. Transparency and independence

190. A number of stakeholders [1, 3, 10] raised the issue of the availability and transparency of information for the wider public, and in particular the concern that public interest reports (PIRs) might decline in the future, based on evidence from the health area. Foundation trusts have been able to appoint their own auditors and the number of PIRs has dropped to none being issued. While there is a monitoring mechanism because auditors are required to report to Monitor (which is now part of NHS Improvement)⁷⁵ around some of the issues which could end up in a PIR, these issues may now be being dealt with between the foundation trust and the auditor before a PIR will be issued. However, this makes the issues transparent to Monitor, rather than to the public as a broader stakeholder. In addition to that, it is difficult to assess whether this means that the level of transparency has decreased or not without knowing the intrinsic issues for each body. The decline in PIRs can either occur because the situation of a particular body has improved, or because the relationship between the respective LPBs and the audit firm has changed because it is now based on a contractual basis and appointments of auditors are made directly by the LPBs (i.e. auditors are now less inclined to issue a PIR, a point raised in interview with one of the audit firms).
191. One interviewee mentioned that when it comes to the question of whether fee and cost structures are more transparent for LPBs after the reform, it has to be seen how much information about fees are provided by the firms and how LPBs report on costs and fees paid in the future. In general, there can always be hidden overheads in any fee, whether it is put forward by the Audit Commission or by audit firms. There are statutory requirements in place that require LPBs to disclose the fee they have paid for audit services, as well as any fees paid to the auditors for non-audit services, but whether there will be an increase in the levels of transparency can only be observed after the reform is fully implemented.

⁷³ Department for Communities and Local Government. 2015. Sector led body for smaller local authority audit appointment under the Local Audit (Smaller Authorities) Regulations 2015 – appointment announced. Online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/492898/LocalAuditNotice.pdf (accessed 1 April 2016).

⁷⁴ NALC. 2015. First letter from chairman. Online: <http://www.nalc.gov.uk/library/our-work/1856-smaller-authorities-audit-appointments-first-communication/file> (accessed 1 April 2016).

⁷⁵ Monitor is now part of NHS Improvement. NHS Improvement is responsible for overseeing NHS foundation trusts, NHS trusts and independent providers. Online: <https://improvement.nhs.uk/>

4. Further issues for consideration in a potential future evaluation

4.1. Background

192. As well as examining changes from the baseline year, a possible future evaluation will need to take account of a number of practical issues identified during the course of our research.

4.2. Timing of a potential future evaluation

193. The timing of this evaluation will be a matter for the Department for Communities and Local Government and the Department of Health, although commitments have been given to Parliament to hold such a post-implementation review within 3-5 years of Royal Assent. We assume that the relevant departments may want to commission an evaluation at a time when all aspects of the reforms have been introduced and have had time to take effect, at the very least for one year. The main influence is therefore the timing of the ending of the transitional arrangements beyond the life of the current audit contracts. It is now clear that there will be no extension for NHS and small local government audits after the 2016/17 audits are over, but the Secretary of State for Communities and Local Government announced in October 2015 of his intention to extend the transitional arrangements for principal local government bodies to 1 April 2018. Thereafter local public bodies will have the power to appoint their own auditors. New appointments will need to be made by 31 December 2017. The first year of local appointment for principal local government bodies will therefore be the 2018/19 audits.⁷⁶ Since the majority of accounts for that year will not be signed off until around September 2019, any post-implementation review would be unlikely to commence before early 2020.

194. **Given that the objective of the evaluation will be to assess the impact of new arrangements, this would suggest that an evaluation could not be finalised until early 2020, following completion of the first year's audit.** By this point, all local bodies will have experienced at least one year of audits under the new regime. In addition, some of the regulatory arrangements (e.g. NAO's role) will have been in place for more than four years. In our view, however, there is merit in undertaking some work earlier in order to bring forward the time of the final report. In particular:

- Given that implementation of local appointment will take place for health bodies and smaller authorities a year earlier, there would be **scope for the evaluators to begin work earlier** on the impact on these sectors
- **Interviews should be undertaken with, and information gathered from, PSAA** prior to the ending of the transitional arrangements.

⁷⁶ Local Government Association. 7 December 2015, 'Preparations for new appointment arrangements'. Online: www.local.gov.uk/web/guest/external-audit/journal_content/56/10180/7534520/ARTICLE (accessed 1 April 2016).

- **Validation work on the data on expenditure** in the interim years could take place early on in the research and does not need to wait until the end of the first financial year.

195. Related to the issue of timing is also the availability of certain baseline data for different points in time and whether this has an impact on the nature of the evaluation itself. In an ideal case, all the baseline data would be available for the same point in time (2009/10) but this was not possible to obtain across all indicators (see discussion and notes throughout this report). This could mean that any future evaluation will not simply be a comparison of the new status quo against the baseline as a benchmark, but more of an assessment of noticeable change at key junctures in what is a phased introduction of different reforms (with the most important changes to the system that could affect audit fees and quality likely to have happened in 2012 and 2017).

4.3. Changes in context

196. The factors influencing the timetable discussed above mean that the evaluation will look back over a ten-year period. This would be challenging in itself, but is made more so by the extent of change that will have taken place between the end of the period and the baseline year in a number of ways. The evaluation will need to acknowledge the substantially **different context** in which audit work is being undertaken. These changes discussed below, along with others which may take place in the coming years, will form the backdrop to any assessment of the impact of the audit reforms since the participants in the audit processes will be subject to a wide range of environmental changes. These contextual factors will need to be explained and taken into account in any final evaluation assessment.

197. Firstly, any future evaluation of local audit reform will also need to take account of the fact that there are likely to have been **major changes to the form and scale of local public service delivery** over the ensuing years. These changes are likely to mean that the 'landscape' in which the audit of public money is undertaken in the later years of this decade will be very different to that existing in 2010. These changes include:

- **Greater emphasis on the importance of localism**, designed to increase local decision making about how services are delivered and new developments are planned, and increase accountability at local level.⁷⁷
- **Significantly smaller budgets for local public bodies**, with reductions in government funding of local authorities by 37 per cent in real terms between 2010/11 and 2015/16, and further reductions to continue for the foreseeable future; this includes also any reductions that could come from changes in sources of local government spending (e.g. localisation of business rates).⁷⁸ There have been similar reductions in the resources of the NHS, police and other agencies.
- **Transformational change and redesign of local services**, including the development of new partnerships such as in health and social care, police bodies, fire and rescue authorities and new responsibilities such as in the field of public

⁷⁷ Department for Communities and Local Government. Policy paper: 2010 to 2015 government policy: localism. Online: <https://www.gov.uk/government/publications/2010-to-2015-government-policy-localism/2010-to-2015-government-policy-localism> (accessed 1 April 2016).

⁷⁸ National Audit Office. 2014. 'Financial sustainability of local authorities 2014'.

health, for example, under the Care Act 2014, or through the devolution of responsibilities and powers under City Deals and devolution deals, given greater effect through the Cities and Local Government Devolution Act 2016.

- **Demographic changes** including immigration and the ageing of the population, which are presenting more challenges to services.
- **Increased use of new technology** to deliver transactional services in more efficient ways, with digital forms of delivery increasingly used.⁷⁹
- **Changes to organisational cultures** and demands for new skills and responses within public sector bodies and those working with them.

198. These and other developments make it likely that local bodies will no longer undertake the same activities in the same ways as before, and will have experienced/be experiencing transformative change. There are a number of ways in which such changes may be of significance for any future evaluation of the reform of local audit. In particular:

- Under the new audit framework, **local bodies will be permitted to appoint their own auditors**, subject to the independence of the auditor being maintained, once existing audit contracts have expired, designed to increase local involvement.
- Although local authorities are generally considered to have coped well with reductions in government funding, some are showing **signs of financial stress**, which may mean that audit work uncovers weaknesses in governance and the use of public funds.⁸⁰
- **Changes in form and new delivery models** may increase the risks to the use of public money and may be more challenging for auditors.⁸¹
- There may be **pressures on the fee levels** established by the Commission's latest procurements.

199. Secondly, the evaluation will need to consider the impact of **changes in accounting requirements and audit timetable introduced over the period**, which could affect local public bodies' wider financial management and ability to prepare the accounts on time, and which may influence auditors' work and therefore, possibly fees. Particular changes mentioned include the proposed move to depreciated replacement cost for measuring local authorities' highways infrastructure assets, which will be an important change for relevant authorities but having nothing to do with the Local Audit and Accountability Act. In addition, the acceleration of local authority audit timetables may be challenging for the audit of some councils, where control environments are weaker, and will bring the audit cycle for more public sector work into line with private sector timetables, making it more of a challenge to manage peaks and troughs in workload.

⁷⁹ Local Government Association. 2014. 'Transforming local public services: using technology and digital tools and approaches'.

⁸⁰ National Audit Office. 2015. 'Short Guide to the NAO's work on local authorities'. Online: <http://www.nao.org.uk/wp-content/uploads/2015/08/A-Short-Guide-to-the-NAOs-work-on-local-authorities2.pdf> (accessed 1 April 2016).

⁸¹ National Audit Office. 2015. 'Short Guide to the NAO's work on local authorities'. Online: <http://www.nao.org.uk/wp-content/uploads/2015/08/A-Short-Guide-to-the-NAOs-work-on-local-authorities2.pdf> (accessed 1 April 2016).

4.4. Responsibilities for data collection and evidence of data gaps

200. Any evaluation depends to a great extent on the availability of data. Part 3 suggests that there is a mixed picture as regards the availability of data relevant to establishing the baseline. Some is readily available, some has been collected, and some is not available in the form required. In addition, DCLG will need to reflect on **whether, and if so by whom, certain data will be systematically collected in the coming years** in order for a national picture, for example, of fee levels, complete list of public interest reports and qualification of accounts, or number of elector objections to accounts to be understood. Responsibility for this could fall to the DCLG in its role, although it may consider that this runs counter to its localism agenda and its desire to avoid burdening local bodies. There are a number of options. An alternative would be the National Audit Office, although it is not clear that this falls within its remit and it might take the view that DCLG cannot discharge its accountability to Parliament if it does not have a well evidenced overview of developments across local public bodies.
201. In some cases, should a decision be made not to gather certain data, future evaluators may be able (or have no choice but) to gather data for themselves, but this is likely to be onerous. In addition, the reforms since 2010 (in particular, the ending of inspection and assessment work) raise questions around Government's wider ability to identify signs of local failure and poor value for money. **This suggests that a full evaluation should include consideration of gaps and consequences (including any unintended consequences) arising from the abolition of the Audit Commission's local assessment and inspection functions, and whether data gaps identified are having a significant impact on the ability to evaluate the use of public money.**

4.5. Other points to note

202. The proposed evaluation makes use of a number of different types of evidence, which are described in some detail in Part 2. A general point to be emphasised is that an important part of the evaluation will be to assess the **strength of the different types of evidence**, and reflect these assessments in the amount of reliance placed upon them.
203. Another important aspect that the evaluation will need to take into account is **unintended consequences and outcomes** arising from the reforms. One of the weaknesses of a Theory of Change approach is that it could shape the evaluation in a way that it is focussed only on how the various known activities are linked through to the stated overall policy objectives. However, with any policy initiative there may well be consequences which were not anticipated or knock-on effects that could not have been foreseen. These should be factored into the potential future evaluation approach including in interviews with stakeholders and DCLG.
204. One point raised by the reference panel was that any future evaluator might want to check to see whether there had been **additional assurance work** commissioned over the period. Although this had been on the decline under the Audit Commission, examples still exist such as the Department for Work and Pensions' requiring assurance on housing benefit subsidy claims. In the NHS, NHS England, Monitor and TDA require assurance work on certain quality reporting. On the other hand, the example was given of the two per

cent maximum precept on council tax for social care spending, where no assurance work has been requested.

205. Any future evaluator might also want to take into account research insights and data from additional studies on the local audit regime, in particular an ESRC-funded programme of research into public sector audit and accounting at the University of Bath. Dr Margaret Greenwood is leading a large programme focused on local authorities. The data collected throughout the studies will provide a basis for analysis by institution, year and other factors such as geographical location. The programme consists of three projects⁸²: Study no.1 aims to estimate the effect of the new local audit regime under which local authorities and NHS Trusts appoint their own auditors and in which the monitoring of audit quality is transferred to the Financial Reporting Council (FRC). The study will focus on audit fees and audit quality of NHS Foundation Trusts and NHS Trusts. Study no.2 will use pre-audit financial statements to investigate the relationship between audit adjustments and audit fees for local authorities in England. The aim is to estimate the potential savings from an improvement in pre-audit financial reporting quality. Study no.3 will look at the impact of recent pressures on audit fee levels on the financial reporting quality of local authorities and NHS Trusts.

⁸² Bath Centre for Healthcare Innovation. 2015. Public Sector Audit in a Period of Austerity and Reform. Online: <http://www.bath.ac.uk/chi2/project/public-sector-audit/> (accessed 1 April 2016).

5. Methodology for a potential future evaluation

5.1. Background

206. This section of the report summarises the proposed methodology for any future evaluation of local government reforms. The methodology section assumes that the evaluation will take place in about three years' time. It is also assumed that the key research questions to be addressed remain as set out in the original Research Specification (paragraph 1.1.). The remainder of this part discusses each element in sequence, explaining the rationale for the work. It is worth emphasising that the approach set out below is designed based on the assumption that adequate evidence will be available. We recommend that any future evaluator carries out an initial evaluability assessment to agree with DCLG as the client whether there are sections of the research which may not be possible in the absence of suitable evidence.

5.2. Documentary review

207. As explained in Part 1, the reform of local audit is being introduced in stages over a number of years. It will therefore be important that the evaluator is familiar with developments. In order to take into account new policy developments related to the reforms and how they were implemented, the evaluator will want to conduct a short document review, mainly of policy documents and research papers in the topic area. Key points to take into account are:

- As the policy lead, the **Department for Communities and Local Government** will be able to direct the future evaluator to any new policy documents and other related documents which are of importance. The **Department of Health** will be able to point out the additional policy documents relevant for the audit of health bodies.
- A second key source is a list of **other organisations**, whose websites can be used as a starting point for looking for other documents that describe the implementation of the reforms as well as any other changes. Organisations of particular importance are the Local Government Association, CIPFA, ICAEW, ICAS, the National Audit Office, and the Financial Reporting Council, NALC and SLCC. Additional information could also be retrieved from other bodies such as the Home Office and the Department for Environment, Food and Rural Affairs. The new sector-led bodies will also be essential.

208. **Rationale:** The document review will enable the evaluator to identify key changes from March 2016 onwards (the date of the submission of the final report of the scoping project). This will be essential for developing an understanding of how audit arrangements, participating bodies and other stakeholders, and the wider environment have or have not changed since the baselining work. The importance of being clear about audit arrangements by 2019/20 and the wider environment was discussed in Part 1. The document review will help provide an updated narrative at the time of the evaluation. The document review can also be used to support a brief review of the Theory of Change (summarised at the start of Part 2), which was developed to help understand how the

variety of initiatives and actions undertaken were designed to lead to securing the overall policy objectives. Continuing use of the Theory of Change should be seen as central to the continuing evaluability of the reforms, rather than an optional extra.

209. There are a number of different types of document:

- **Official documents from DCLG** will highlight any policy changes or amendments to the overall strategic direction. These developments will need to be taken into account in any consideration of whether the reforms met their objectives, which may have been amended over the course of what may be nearly ten years after the announcement of the abolition of the Audit Commission. Whilst we would expect an evaluation to refer back to the original policy objectives, it should also pay close attention to subsequent adjustments which mean the original objectives cease to have validity.
- **Third party documents** will provide information on the contribution made by organisations such as the NAO and the (FRC), which have specific responsibilities under the Act. Both are likely to use their websites to publish relevant material on their roles, activities and the performance of organisations subject to their specific forms of regulation. The NAO will also issue guidance to auditors at various points in the coming years.
- We would also expect the evaluation to draw on **material prepared by representative or professional bodies** over the period. For example, the Healthcare Financial Management Association (HFMA), LGA and CIPFA have issued guidance or commentary on local audit matters. ICAEW issued a guide to local audit regulations in November 2015.⁸³ Similarly, an evaluation will want to take account of material issued by NALC and SLCC on smaller bodies. Furthermore, the transitional body PSAA will be issuing annual reports as will any sector-led bodies for procurement, e.g. the Smaller Authority Audit Appointments Ltd (SAAA) for smaller bodies.

5.3. Review of administrative data and data trends

210. **Rationale:** The evaluator will also need to capture and assess administrative data for a number of the indicators. Part 2 discussed the sources for each indicator but the future evaluator will need to first review the availability of equivalent contemporary data. Where there are gaps or data has not been collected in the interim period, the evaluator will need to discuss with DCLG as policy lead how to obtain the data.

⁸³ For example:

ICAEW. 2015. Local Audit Regulations. Online: <https://www.icaew.com/~media/corporate/files/technical/audit%20and%20assurance/local%20public%20audit%20in%20england/annex%201%20local%20audit%20regulations.ashx> (accessed 1 April 2016).

LGA. 2015. Preparations for new appointment arrangements. Online: http://www.local.gov.uk/web/guest/external-audit/-/journal_content/56/10180/7534520/ARTICLE (accessed 1 April 2016).

HFMA. 2015. Auditor panels: guidance to help health bodies meet their statutory duties, September 2015. Online: <https://www.gov.uk/government/publications/auditor-panels-for-nhs-trusts-and-clinical-groups> (accessed 1 April 2016).

CIPFA. 2015. Guide to auditor panels. Online: <http://www.cipfa.org/policy-and-guidance/publications/g/guide-to-auditor-panels-pdf> (accessed 1 April 2016).

211. At the current time, PSAA will report on the findings from audits covering many of the same issues as the *Auditing the Accounts* reports produced by the Audit Commission. A report for the health audits for 2014/15 was published in July 2015 and a report on local government accounts appeared in December 2015. Once PSAA is no longer operating the transitional arrangements, it is unclear how this data will be collected. One view is that individual government departments will need to collate the information as part of their assurance frameworks. Data on audit quality and the quality of the firms will be available from the Financial Reporting Council through its inspection reports.
212. Where possible the evaluation should include an analysis of annual data for each indicator to identify any particular trends or developments which merit deeper examination. It is clear, for example, from the Audit Commission's unpublished report 'In the public interest' that there can be significant changes within different aspects of audit work over time. Thus, there has been a noticeable fall in the number of PIRs since 2009/10 (p28), while over the same time period, there has been a significant improvement in the proportion of principal and small bodies receiving an audit opinion by 30 September (p33). Undertaking a trend analysis will help to inform the overall conclusions. Table 19 summarises the administrative data sources.

5.4. Local public body survey

5.4.1. Purpose of the survey

213. A key element of the methodology is a survey of local public bodies. This was designed to capture the views of senior finance officers within the principal public bodies on aspects of audit reform. The Theory of Change work made it clear that the reform could only be considered a success if certain quantitative and qualitative changes took place, and if the quality of audit was deemed to have been maintained. It would be hard to argue that the policy change had met its objectives if, for example, finance professionals were reporting a decline in the quality of audits conducted at their organisation and they were experiencing less choice in audit provider, or (amongst audit firms) if the replacement regulatory regime was considered more onerous than that which it replaced, or if the cost of audit had increased substantially.
214. In a number of cases, therefore, we identified the need to supplement quantitative data collection with capturing the views of participants in the audit process through a survey of senior finance officers in local public bodies. This has helped us to establish the baseline position against a number of key indicators (Table 20).

Table 19: Future sources of administrative data

Type	Indicator	Source
Number of audit firms registered and local audit in	1	Register of auditors maintained by professional bodies
Cost of local audit regime	2	See separate section below
Number of objections by local electors	3	Not collected centrally in the future; may need to be created.
Qualification of audit opinions	4	Currently PSAA / not collected centrally in the future. May need to be created
Health of audit system	5	Financial Reporting Council
Number of Public Interest Reports	6	Currently PSAA and DCLG /ISA 260 reports/auditors will be required to send PIRs to the Secretary of State once PSAA closes
Quality of audits performed	8	Financial Reporting Council Annual Inspection Reports
Number of NAO reports on local issues	13	National Audit Office website for publication list
Timeliness of publication	14	Currently PSAA, CIPFA in the future

Table 20: Future sources of survey data

Type	Indicator	Source
Satisfaction with audit services	7	Repeated survey of LPBs
Local public bodies' views on composition of fees	10	Repeated survey of LPBs

5.4.2. Survey sections and type of information collected

215. The questions for the survey were designed to gather stakeholder views on existing audit arrangements and initial views on the impact or likely impact of the changes to the local audit regime.

5.4.3. Development of the questionnaires and piloting

216. The questions in the survey instrument were developed based on our understanding of the main issues from the earlier stages of the project work (our literature review, the development of the Theory of Change and stakeholder interviews). They also built on, or have sought to replicate, some of the questions included in the 2008 Ipsos MORI stakeholder survey mentioned in Part 2. We took account of the views of DCLG and the

DoH, as well as CIPFA, ICAEW, PSAA and NAO, which all provided useful feedback and suggestions for changes in order to make the survey more targeted and accessible.

217. In addition, we were conscious that a survey instrument needed to be meaningful to those who would be completing it and make use of appropriate terminology. We therefore arranged with CIPFA to expose the draft document to members of its Accountancy Panel. We sought feedback on whether there were any issues with the type of questions included and any practical issues when using the survey online (e.g. clarity and flow of the questionnaires; appropriateness of language used; accuracy of all routings, and time taken for completion). The draft was also shared with HFMA.

Table 21: Survey section and data collected

Local public bodies survey		
Survey section in questionnaire	Area on which information is collected	Use of survey results underpinning indicator and research questions
1. Background information	Respondents' organisation and role in it	Not applicable
2. Satisfaction with current audit arrangements	Respondents' views on existing/recent audit arrangements.	Indicator no.7: Level of satisfaction with quality of audit services amongst LPBs Indicator no.10: Extent to which LPBs are clear about the composition of the audit fees
3. Views on the importance of areas covered by the local audit reforms	Respondents' views on the importance of areas covered by the 2014 Local Audit and Accountability Act	Research questions – accessible markets, quality of audit regime
4. Views on changes to audit arrangements in the future	Respondents' views on the anticipated implications of the changes brought in by the 2014 Local Audit and Accountability Act	Research questions – accessible markets, quality of audit regime
5. Accountability and transparency for public spending	Respondents' views on implications for accountability and transparency for public spending brought in by the 2014 Local Audit and Accountability Act	Research question – audit standards
6. Final thoughts	Final thoughts/any remaining issues respondents want to add	Overall

218. **Rationale:** To gauge whether there has been a change in the views of local public bodies on aspects of the audit process and practice, the possible future evaluation should repeat the survey. The survey instrument used in 2015 should be broadly replicated in order to ensure that interviewees answer the same questions. This will ensure that the data is comparable over time (this applies in particular to Section 2 of the survey). However, before use, we recommend that the survey is reviewed in cooperation with the above mentioned stakeholders in order to assess whether the questions are still relevant or need to be changed in the light of developments. The understanding coming out of the proposed

document review should also be used to assess whether the survey questions are still valid or need to be adjusted or dropped.

5.4.4. Target audience and sampling strategy

219. The survey covered all principal local public bodies in place during 2015/16 and was sent out to senior financial officers. It is worth noting that some of these bodies (such as CCGs) would not have been in existence in the baseline year of 2009/10. Smaller bodies were excluded from the survey in order to make the survey manageable in size, avoid overburdening organisations with limited resources, but also to focus on bodies which spend the most public money. We recommend the possible future evaluation should follow the same approach.

5.4.5. Distribution, response rate and statistical significance

220. In order to try to secure a high response-rate, the survey questionnaire for both baseline surveys was deliberately kept short (average time to fill in the survey was estimated at 15 to 20 minutes) and was clearly structured. The online format of the surveys was designed using RAND Europe's online survey platform SelectSurvey. However, the survey can be replicated with any suitable software that provides a secure web interface for creating, administering, and deploying the survey.
221. The survey should be also repeated in a way that allows for testing statistical significance of changes over time between the results of the 2015/16 survey and the survey undertaken for the potential future evaluation. From a methodological viewpoint (subject to sample sizes) t-tests would probably be suffice for this, but ensuring that this can be done would add another layer of rigour for the potential future evaluation. It should be also noted that the data obtained does not (strictly speaking) represent panel data but rather repeated cross-sectional data from the same type of organisations. While the survey will be sent out to the same types of organisations when being repeated, it will not necessarily be sent out to the same people (since people will switch positions, jobs, etc.). While this approach represents probably the only way to get a sufficient response rate overall and surveying the same people in the future will not be feasible from a logistical point of view, panel data would be the only reliable way to chart change over time since this would map real changes in perceptions of the same individuals (while in the other case changes in perception could be more related to overall differences in views between different individuals).

5.4.6. Limitations of the survey design and elements that could be added when the survey is repeated

222. The survey mainly covers the views of local audit bodies on audit arrangements as they existed up to and including 2015, and their views on the pros and cons of the reforms that begun in 2010 and were implemented through the Local Audit and Accountability Act 2014. However, depending on whether DCLG or other stakeholders collect relevant information on the different aspects of the local audit regime in the future, the survey might have to be extended to cover more aspects. In particular, it could be used to gather a data sample on the various annual costs of local audit regime (in total and by local body) which are needed to underpin indicator no.2 (see list of indicators above) in case no central collection of this type of information will take place over time. The survey could also be extended by questions around:

- Procurement costs.
- Costs of setting up and running independent audit panels (where established).
- Costs of setting up and running other procurement vehicles (collective procurement/sector-led bodies).
- Other costs incurred by LPBs related to compliance with the new regime.

223. Another important difference between the 2015 survey and the repeated version is that respondents should be asked about the form of procurement they used – e.g. individual procurement, sector-led body, other form of group procurement. This will allow for comparative analysis of views based on the route taken. The survey should also specifically request the fee paid. In addition, the repeat survey could include a question on whether audited bodies felt better/worse informed about comparative performance than in the past, given the ending of the Audit Commission’s role in this area. The evaluator would be interested in whether the new role of the NAO and the sector-led information gathering provide adequate comparative data.

224. However, consideration will also need to be given to whether this would be overly burdensome for local bodies at a time of reduced budgets, and whether alternative sources, such as an annual accounts may need to be used, whatever the limitations of this source.

5.5. Interviews with partners of audit firms

225. A key group of stakeholders in the reform of local audit are the audit firms themselves. Given that the Government’s objectives include ‘to develop a diverse audit market, maintain competitive fees and maintain high standards of audit’, it would be hard for the reforms to be seen as effective if the firms were put off undertaking local audit work and/or could be shown to be delivering a poorer quality service. Securing the views of the audit firms was therefore another element of the scoping and baselining work, and will need to be replicated for the evaluation.

Table 22: Future sources of interview data

Type	Indicator	Source
Audit firms’ views on fee levels	11	Repeated interviews with stakeholders
Firms’ satisfaction with the regulatory regime	12	Repeated interviews with stakeholders

226. In considering how to gather the views of audit firms, we opted to undertake semi-structured interviews with the partners/directors leading the audit of local public bodies’ work. These individuals were identified with the assistance of (David Aldous, Director at) the NAO, and the Local Auditors’ Advisory Group (LAAG) of firms carrying out these audits. As such they were deemed the people most likely to be able to provide an authoritative firm perspective. Interviews as a means of gathering the views of firms were chosen as an alternative to a written survey, as RAND Europe considered the latter would generate less substantial evidence and that there would be less opportunity to discuss issues arising out of the individual circumstances of each firm (e.g. location, scale of local audit work).

227. The interviews with the audit firms help to examine how they have responded to the changing environment since the announcement of the abolition of the Audit Commission in 2010 and the introduction of the Local Audit and Accountability Act 2014. The structure for the interviews is at Appendix E. Any future evaluator will need to identify with DCLG who are the participating firms and who, within them, are the key contacts. Assuming that the NAO remains as the coordinator of the Local Auditors' Advisory Group, its Director responsible for local audit work could be a suitable starting point again.

Table 23: Participating audit firm contacts 2015

Stakeholder	Potential contact person
Deloitte	Craig Wisdom
Ernest & Young	Karl Havers
Grant Thornton	Jon Roberts
KPMG	Trevor Rees
Mazars	Gareth Davies
BDO	David Eagles, Malcolm Thixton
PwC	Lynn Pamment

228. The audit firm interviews were broadly aligned with the survey along the topic areas covered and the format was informed by the document review and development of the ToC. It was also informed by the subjects raised by audit firms during parliamentary enquiries into audit reform and in written submissions. These were reviewed as part of the baselining work.⁸⁴ The topic areas covered are:

- **Background information** – to understand the size of the firms, the geographical areas operating in, history of participation in local audit, etc.
- **Existing and recent audit arrangements** (pros and cons) – to gain the firm's overall perspective on the adequacy of pre-reform arrangements, including views on the Audit Commission's regime
- **Views on the importance of areas covered by the local audit reforms** – to assess whether the issues addressed in the audit reforms were/are considered significant to the firm and hence, worth change
- **Views on changes to audit arrangements in the future and assessment of anticipated market responses to the changes** – to assess whether the firms consider the reforms are likely to address these issues, whether they consider there are risks/downsides, etc.
- **Barriers to entry to the market/sustainability of participation in the market** – views on the ease with which firms can equip themselves for local audit, barriers to entry, specialist nature of the work etc.
- **Regulatory regime** – views on the changes to the regulatory regime, including views on Audit Commission approach, introduction of NAO/FRC, etc.

⁸⁴ See, for example, written submissions at: House of Commons Communities and Local Government Committee. 2010. 'Audit and inspection of local authorities. Fourth Report of Session 2010–12 Volume II'. Online: <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmcomloc/763/763vw.pdf> (accessed 1 April 2016).

229. **Rationale:** Any future evaluation would replicate the semi-structured interviews with relevant firm partners, amending the focus to take account of changes in the environment, but seeking to gather similarly authoritative views of the participating firms. The aim would be to gather a new snapshot at the time of the evaluation, particularly on:

- **Adequacy of the procurement arrangements for audit** – whether they consider the arrangements that developed are efficient and effective.
- **Incentives in the reformed regime** – relating to fee levels, the ability to deliver a quality service and add value, relations with local public bodies, etc.
- **Efficiency of the regulatory regime** – how it operates, the demands placed on firms, pros and cons of new arrangements, etc.

230. The evaluation could draw on evidence from the firm interviews to cross-refer to the information coming out of the analysis of the indicators using the administrative data, in particular when it come to the market development and the different supply/demand factors in the market. The information coming out of the interviews underpin the analysis indicators 11 and 12. In addition, they would be a chance to follow up on the issues raised by audit firms in 2015 about the conduct of local public audit. This will provide the opportunity to see whether the risks identified have materialised.

5.6. Stakeholder interviews

5.6.1. Contacts for the baselining and scoping study

231. In considering whether the government's objectives have been met, it will be necessary to take account of the views of a variety of stakeholders in a possible future evaluation. Whilst there are a number of objective measures for assessing outcomes, it is also clear that participants in the audit process or other stakeholders and observers of it have views which need to be captured and assessed as evidence. It will, for example, be hard to consider reforms a success if many of the major participants such as the professional and representative bodies, or the new regulators, consider that audit standards have declined, or if there is a widespread belief that there has been a decline in levels of accountability and transparency.

232. **Rationale:** As part of the evaluation, therefore, interviews with a wide range of stakeholders affected by, or with an interest in, the reforms should be conducted. This will help to:

- Provide informed insights into developments since the beginning of the reforms.
- Draw attention to relevant documentation or other contacts available since the baselining study.
- Triangulate the information coming out of the analysis of the indicators using the administrative data and the cost-benefit analysis.
- Provide insights into potential problem areas which could guide the wider analysis of whether the reform aims have been achieved (or are about to be achieved).

233. These interviews will also help provide information on whether the local audit regime and market have developed along the line of the policy goals, whether regulators are seen to be coordinating effectively, and whether the new regulatory bodies are seen to be operating well. Table 24 summarises the list of stakeholder bodies interviewed in 2015 along with the focus of the interviews. The individual contacts at the time of the evaluation

are likely to be different but this list of organisations can be regarded as a suitable starting point.

Table 24: Stakeholder contacts

Stakeholder	Focus of interviews
1. Financial Reporting Council	New regulatory role
2. National Audit Office	New regulatory role
3. ICAEW	Professional body role
4. Society of Local Council Clerks	Arrangements for smaller bodies
5. Local Government Association	Overview of reforms
6. Public Sector Appointments Ltd	Audit Role of PSAA, Audit Commission data
7. CIPFA	Professional body role
8. Department of Health	Impact of reform on NHS
9. Centre for Public Scrutiny	Accountability and transparency
10. HFMA	Arrangements for NHS
11. Smaller Authorities' Audit Appointments Ltd	Arrangements for smaller authority audits

5.6.2. Issues raised during 2015 interviews

234. In the course of the interviews with stakeholders conducted in 2015, a number of key issues were mentioned. These included challenges and opportunities of the new arrangements, as well as areas of development for the future. These issues could be used as a starting point for conducting a new set of interviews for the post-implementation evaluation in order to establish whether they have changed or remained the same, or whether new issues have emerged. This list of issues (together with the risk/challenges section from the ToC) can be also used in order to corroborate the review of the ToC indicators and the results of the cost-benefit analysis review. If there are gaps between stakeholder perceptions and the results of the quantitative analysis (e.g. around the perceived quality of audit and objective measures) these gaps will be worth exploring further. Significant disparity between different stakeholder views will also be worth pursuing to understand varying perspectives.

5.7. Case studies of the audit of local bodies

235. We suggest that local case studies could supplement the data collection, particularly around costs and quality of audit. These will enable any future evaluator to probe the reasons for changes that are observed in the data, as well as the extent to which they are due to changes in public audit as opposed to factors specific to the local public body itself or the wider environment. This will allow the evaluator to assess in more detail specific developments over time in selected organisations which might be representative for a wider set of bodies.

5.7.1. Which bodies should be included?

236. The choice and number of case studies would be guided by a discussion with DCLG about the main issues which they would like the evaluation to explore. This will be influenced in

part by the issues which are identified from the survey and the changes which have taken place since the baseline year. Other guiding criteria might be:

- Size, type of body, remit, location, varying local context, etc.
- Procurement vehicle chosen (individual appointment, joint procurement, sector-led body).
- Previous issues arising from audit and transparency of local spending (objections, PIRs, etc.).

5.7.2. How should the case study be conducted?

237. The research approach would be decided by the potential future evaluator but we suggest the following steps to be included in the case studies:

- Mapping the context for local audit of the body.
- Interviews or focus groups with selected key informants.
- Document review and data collection.

Mapping the context

238. This step should help to identify the varying factors that affect how the audit has been conducted in order to isolate whether particular developments can be seen as a major outcome of the reforms or whether other factors and changes in context play a larger role (for example, financial health of the body, capacity of finance function to prepare high quality accounts). Consideration may also need to be given to any broader changes such as reorganisations or mergers. This mapping exercise will not only describe the type, size budget and remit of the body, but also describe briefly recent changes. It will also include a brief description of any issues around the market for audit services in which the body is located (e.g. in a remote area).

Interviews or focus groups

239. The exact selection of the candidates for interview would be decided by any future evaluator. We suggest including at least a Financial Director or a Financial Officer on senior level for the interviews. A focus group could be considered to bring together a number of staff in one discussion, and could include staff conducting the day to day financial management and staff preparing the accounts as well as senior staff. The interview template and the template used for the focus groups could involve similar topic areas. These could be around:

- Current vehicle for procuring the audit.
- Reasons for choosing the vehicle as compared to others.
- Procurement costs, staffing.
- Satisfaction with current audit arrangements.
- Type and scale of audit work carried out.
- Quality of audit work.
- Fee levels and transparency of fees.
- Level of transparency of public spending, PIRs and objections.
- Wider impact of audit reforms.

Document review and data collection

240. The document review and data collection will be focused mainly on grey literature, administrative and policy documents from the audited body.

Draft outline of the case studies

241. The case studies should be written up using a common template/structure in order to be able to compare findings across cases and to draw out common themes or specific differences between the cases. We suggest the following draft structure which reflects similar thematic areas which are also covered by other parts of the suggested evaluation methodology, and therefore ties in with the wider evaluation framework (however, this serves as a starting point that can be also adjusted by any future evaluator):

- Local socio-economic context
- Challenges faced by the body and recent developments that could affect the audit
- Audit arrangement and procurement vehicle
- Quality of audit
- Costs for procurement
- Audit market and transparency of fees
- Wider transparency of public spending.

5.8. Cost analysis

242. A key objective of the reform of local audit is the reduction in the overall costs of auditing. In order to consider the costs systematically, DCLG prepared an Impact Assessment (IA).⁸⁵ This provides an authoritative overview of forecast costs between 2009/10 and 2019/2020. The figures presented in the IA can be put into the following categories:

- Past baseline data known with certainty at the time of the IA, often drawn from audited accounts.
- Transitional/new framework data estimated based on assumptions given in the report.

243. To assess one of the main objectives of the reform, saving £1.35bn, all relevant costs in the old and the new framework are to be transformed into the same base year prices and compared.

5.8.1. Expenditure trends to 2019 to 2020

244. The anticipated reduction in expenditure over the period comes from several different developments. These are:

- Ending of certain activities
- Reductions in audit fees
- Reduced regulatory costs.

⁸⁵ Department for Communities and Local Government. 2014. Local Audit and Accountability Bill: 'Local audit impact assessment'. Last updated 1 September 2014. Online: <https://www.gov.uk/government/publications/local-audit-and-accountability-bill-local-audit-impact-assessment> (accessed 1 April 2016).

245. Significant reductions in expenditure resulted from the **ending of activities** undertaken by the Audit Commission, in particular, ending of assessment and inspection work, other Commission statutory responsibilities, support and overhead costs. The Government made a clear policy choice to end this particular approach to scrutinising the use of public money through these mechanisms. This means that a comparison between expenditure at the start and end of the period of the evaluation needs to be very clear about what activities were being funded at each point.
246. A major reduction in expenditure is through **reduction in audit fees**. The tendering exercise in 2012, with the ending of the Commission's in-house practice and transfer of staff to private firms, led to a reduction of about 40 per cent in fee levels for 2012/13 audits for five years. In 2014, the remaining 30 per cent of audit work already carried out by private firms was retendered, leading to further savings. The Audit Commission has estimated savings from this of £440m from 2012 to 2020.⁸⁶ As a result, DCLG estimates that the total financial benefit of the reforms will be £1.35bn over ten years, with £759m realised between 2012 and 2017. It adds that 'The monetised benefits are largely avoided costs arising from the various elements of the reforms.'

5.8.2. Elements of the evaluation of costs

247. An important element of the potential future evaluation will therefore be to examine whether or not the predicted reduction in expenditure on audit has materialised. There are a number of elements to this work. They are:
- **Scrutiny of the continuing robustness of the framework** in the IA, in particular, its completeness in terms of capturing all the costs, and whether any developments have taken place during the period which underline the assumptions made.
 - **Validation of the figures** contained within the IA, drawing on authoritative sources including relevant audited accounts.
 - **Capturing of additional data**, where not already available.
 - **Discussion and clarification** of numbers with stakeholders, where appropriate.

5.8.3. Scrutiny of the Impact Assessment

248. RAND Europe has considerable experience of impact assessments and as part of the baselining work we have examined the DCLG IA for local audit reform. Overall, following the technical guidelines for IAs (both from the European Commission and BIS: <https://www.gov.uk/government/publications/impact-assessment-template-for-government-policies>), we consider that it has been conducted in a sound and appropriate manner. The assumptions are clearly stated and sound plausible. In our view, the main area for focus will need to be around the transitional and compliance costs, which are estimates, based on limited evidence, and the fee levels, which will not be known for some time.
249. Nevertheless, the IA is a sound assessment of the costs as at 2009/10 and thereafter, based on anticipated changes to the audit arrangements. It should therefore be used as a starting point for the possible future evaluation. In terms of completeness, the evaluation will need to check that there have been no developments in the course of the period since the IA was prepared. Such developments might result in additional relevant cost elements which should be taken into account. Evidence of any relevant changes will come from the

⁸⁶ 'In the public interest', p. 5.

document review (particularly, official DCLG or DoH documents) and interviews with departmental officials. Additional information could be also retrieved from other government bodies such as the Home Office and the Department for Environment, Food & Rural Affairs (Defra).

5.8.4. Examination and validation of costs in the framework

250. The IA includes a detailed framework of costs for local audit work between 2009/10 and 2019/20. This extends from the baseline year, through the transition period, to the new arrangements. The framework provides a breakdown of costs incurred by different agencies. Any future evaluation will include an examination and validation of the costs for each year. The main areas of expenditure which will need to be examined are set out in Table 25, along with details of sources of information.

Table 25: Expenditure relating to local audit regime 2014/15 to 2019/20

Cost element	Sources of evidence
Costs incurred and income generated by the Audit Commission until 2014/15, at the end of which it was abolished.	The Audit Commission's accounts have been audited and published, including the final year of account, 2014/15, in July 2015. This information is in the public domain in verified form.
Transitional framework costs incurred by Public Sector Audit Appointments Limited from 2015/16 to 2017/18.	Costs incurred by PSAA will be included in their annual audited accounts. The first year of account will be 2015/16. This information will be in the public domain when the accounts are audited and published in 2016.
Fees paid by local bodies directly to their auditors 2017/18 onwards. [Health bodies and smaller bodies will be paying fees from 2017/18, other principal bodies will start from 2018/19.]	Fees paid by local bodies to their auditors will show in their accounts. Unless there is a requirement to collect this information centrally, it will be necessary to collect them individually from accounts.
Local body compliance costs from 2015/16 onwards.	The IA defines these as the cost to local bodies of procuring their auditors, and the cost of establishing and taking advice from an independent audit panel. It is possible that some local bodies will collect this information (although probably not consistently), but an alternative will be for the repeat of the RAND survey to include a question on this. Costs for procuring auditors need to be distinguished by type of procurement and could be also compared (sector-led body, joint procurement, own procurement).
NAO transition costs between 2012/13 and 2014/15.	These are not separately identified in the NAO's accounts. Information will need to be requested from the NAO.
NAO value for money costs from 2012/13 onwards.	The cost of individual NAO value for money studies are not published and it is unlikely that the NAO will separately report the costs of VFM studies on local issues. Relevant data will be held internally by the NAO and we suggest could be obtained on request.
NAO regulatory costs from 2015/16 onwards.	The NAO's published Strategy '2015-16 to 2017-18' states that the NAO's resource proposal includes an element of £1.5m for additional responsibilities under the Local Audit and Accountability Act 2014. It also states that whereas this was shown separately before, following passage of the legislation it is now considered part of the NAO's ongoing work. It is therefore not separately identified. ⁸⁷ They may be available from the NAO directly.

⁸⁷ NAO Strategy. December 2014. '2015-16 to 2017-18'.

5.8.5. Capturing costs

251. There are a number of aspects of local audit where it is not clear at this time whether certain cost data will be collected centrally from local public bodies. In the table above we specifically refer to fees paid by individual bodies and compliance costs.
- **Fee levels:** It may be that DCLG and other departments have yet to decide whether they need to capture a complete national picture of fee levels at each local body for their own monitoring purposes. This is a policy choice, but there is an argument that suggests it is necessary as part of their overall accountability for the use of public funds.
 - **Compliance costs:** It is questionable whether local bodies will collect this information themselves and, as the IA suggests, data is likely to be lacking. A decision will need to be made as to whether local bodies should be expected to collect and report it.
252. As a result, the future evaluation team may need to gather primary data. The most significant figure in the forecast expenditure total for 2019/20 is the amount of **audit fees paid**. These fees will appear in their accounts. Unless there is an expectation that this data will be collected centrally, it will therefore be necessary to collect it by reviewing each set of accounts, which will be an onerous task. During our baselining work we examined 378 sets of accounts in three to four days.
253. For **compliance costs**, the evaluation team may wish to consider including a question in the repeat survey asking for estimated costs associated with appointing their own external auditors and taking advice from independent auditor panels. This would help to secure at least an estimate of the sums involved.

5.8.6. Discussion and validation with stakeholders

254. Given the different components of the schedule of costs, and the variety of sources of varying degrees of reliability, we suggest that the evaluation team discusses and validates them with the relevant stakeholders.

5.9. Comparisons with other nations' local audit arrangements

255. Although the focus of our work is England, there may be value in the potential future evaluation seeking to draw some comparisons with arrangements in Scotland, where the Accounts Commission continues to oversee local government spending, and in Wales, where the Auditor General for Wales is the statutory external auditor of most of the Welsh public sector. These are directly comparable environments, where similar audit work is undertaken to the same standards. However, it should be noted in this context that Scotland and Wales are considerably smaller in size as compared to England. This would need to be taken into account when comparing systems and the respective audit markets.
256. In **Scotland**, the Commission's specific statutory responsibilities remain similar to those of the Audit Commission and include to secure the audit of all accounts of local authorities and associated bodies by appointing either Audit Scotland or firms of accountants as the auditors; to secure the performance by local authorities of their Best Value and Community Planning duties and the performance by fire and rescue and joint police boards of their Best Value duties; to consider reports made by the Controller of Audit on matters arising

from these audits, to investigate all matters raised and to conduct hearings where appropriate; to make recommendations to Scottish ministers and to local authorities, as appropriate; to undertake and promote performance audits, which examine value for money issues across the bodies for which it is responsible; to give directions to local authorities on the performance information they should gather, and publish information about how councils perform.

257. The **Auditor General for Wales** audits the accounts of county and county borough councils, police, fire and rescue authorities, national parks and community councils, as well as the Welsh Government, its sponsored and related public bodies, the Assembly Commission and National Health Service bodies.
258. Work to understand arrangements in Scotland and Wales would provide some form of counterfactual for developments in England during a period of change. Areas for comparison might be trajectories of audit costs, satisfaction levels with audit services, etc.
259. Whilst a detailed comparison would add to the cost of an evaluation, there could be value in undertaking interviews with representatives from both bodies and reviewing documentary evidence on developments in Scotland and Wales, including any survey evidence or information on audit quality. More extensive work in this area would be probably not part of any future evaluation but covered by academic research funded by, for example, a research council.

Appendix A: Methodology for the project

The methodology for this scoping and baselining project is described below. Furthermore, at the end of the work, RAND Europe will deposit interview guides, the survey instrument and database of responses with DCLG, along with any other relevant material.

A. Document review

We undertook a focused literature review relating to the reforms. The rationale behind the changes to the local audit regime have been set out in a number of policy documents since the announcement was made in August 2010 to abolish the Audit Commission, and to transfer the audit of local public bodies to the private sector. We have identified some of these below.⁸⁸

Our literature review provided a clearer understanding of:

- The background and context for the reform of local government audit.
- The objectives of the policy change.
- The forecast impacts, when they are expected to materialise, and to which bodies.
- The assumptions made about what is needed for different elements of the reform to have the expected impact.

Given our need to understand the official rationale for the policy, particular attention was paid to documents published by the DCLG after 2010, including in particular, the impact assessment published in 2014.

In addition, we reviewed relevant third party literature (e.g. practitioner literature, academic coverage, etc.) in order to develop a sound understanding of different perspectives of the reforms, and the risks and challenges that other parties considered existed for the delivery of the reform's objectives. This included material produced by the Audit Commission itself, the LGA, CIPFA, ICAEW, NAO and PSAA. This helped to shape our thinking and ensure that our work was alive to a wide range of perspectives.

B. Stakeholder interviews

Stakeholder interviews: Semi-structured interviews were conducted between July 2015 and February 2016 with a number of stakeholders affected by, or with an interest in, the reforms. These were (listed alphabetically):

⁸⁸ Literature includes the Government consultation paper *Future of Local Public Audit Consultation Paper* (March 2011); *A summary of responses and Government response* (January 2012); Local Audit and Accountability Act 2014: Local audit impact assessment (2014); report of the Communities and Local Government Select Committee: *Audit and Inspection of Local Authorities* (July 2011) and *Government response* (October 2011) at: <http://www.publications.parliament.uk/pa/cm201012/cmselect/cmcomloc/763/763.pdf> (accessed 1 April 2016); *Regulatory Compliance and Quality Review Programme annual reports, Audit Commission*; *Local Audit and Accountability Bill: A Plain English Guide, DCLG* (May 2013); House of Commons Library, *Local Audit and Accountability Bill Research paper 13/56*

- Shazia Ahmad (Financial Reporting Council)
- David Aldous (National Audit Office)
- Mike Attenborough-Cox (Smaller Authorities' Audit Appointment Ltd)
- John Connell (Department for Communities and Local Government)
- Anna Green (Healthcare Financial Management Association)
- Ed Hammond (Centre for Public Scrutiny)
- Keeley Lund (Chartered Institute of Public Finance and Accountancy)
- Keith Morton (Department of Health)
- Paul Rowsell (Department for Communities and Local Government)
- Sumita Shah (Institute of Chartered Accountants in England and Wales)
- Dennis Skinner (Local Government Association)
- Mike Suffield (National Audit Office)
- Steve Parkinson (Society of Local Council Clerks)

We were unable to secure an interview with the National Association of Local Councils.

The subject matter varied but in general interviews covered the following subjects:

Audit quality

- Standards of audit and how they can be maintained.
- Accountability and transparency.
- Confidence in the local audit system.
- Identified risks to audit quality.

Auditor regulation

Given that a government objective was to replace an organisation – the Audit Commission – with a new regulatory framework, we discussed:

- The new arrangements for regulation.
- Coordination.
- What gaps, if any, have emerged in oversight and reporting on issues across local public bodies.
- The NAO's role in reporting to Parliament on local audit issues.
- Alignment of regulatory regimes for audits of different types of body.

C. Theory of change workshop

On 8 June 2015, we held a workshop with key DCLG officials to develop the Theory of Change which underpins the local audit reform. A draft Theory of Change diagram, based on our initial literature review, was used as the basis for workshop. A total of eight members of DCLG officials were involved, including a number who had been involved in discussions about the policy reform throughout its life.

A Theory of Change approach helps an organisation to identify what it wants to achieve through a given initiative, and the steps it needs to take in order to achieve it. The theory of change, then, sets out the building blocks needed to deliver a programme goal and specifies the range of assumptions about the underlying logic which can lead to desired results. To do this, **logic modelling** is used as the evaluation and learning tool. Logic

modelling maps sequences of activities that connect actions to intended consequences. The logic models can be accompanied by rich, narrative accounts of the intervention logic to explain the implementation pathways and reasoning behind selected approaches.

The workshop was designed to:

- Gain a better understanding of the original purposes of the changes and the assumptions DCLG used to inform its reform programme.
- Clarify the strategic vision for the future, both short-term and long-term, of the audit of local public bodies.
- Identify how the reforms can achieve this vision, and how the evaluations will help to support putting this framework in place.
- Specify very clearly on which organisations the impact falls, as well as the likely timing of the impacts in the coming years.

The workshop generated the diagram at Figure 1 in Part 2, which was considered an accurate reflection of the anticipated outcomes from the reform and how they would be achieved.

D. Survey of local public bodies

To complement existing secondary/administrative data we developed a baseline survey of local public bodies to gather information on their recent audit arrangements, and their views on the pros and cons of changes. This was designed to help us establish a baseline position for local public bodies' views on their audit arrangements prior to the changes. Whilst these views were not gathered during the baseline year, in many cases the current auditors had been in place for some years.

Our survey was drawn up based on our literature review and following a number of interviews with stakeholders. We included a number of statements per subject area arising from this work. Questions asked were also informed by the proposed questions for the potential future evaluation. We worked closely with DCLG to develop the content of the survey. In order to pilot the survey we made use of CIPFA's Accounting Panel to review the draft document. We used a five-point Likert scale to provide some granularity amongst the responses and help us to analyse differences in perceptions.

Our survey was sent to 427 principal bodies from a list provided by DCLG – 354 in local government, 42 police bodies, and 31 fire and rescue authorities. It was sent by link in an email to a named senior financial officer. In addition, a slightly amended version of the survey was sent to 211 Clinical Commissioning Group (CCG) Finance Leads via the NHS England Finance Portal and to 90 Directors of Finance and Deputy Directors of Finance in NHS Trusts via TDA (including four part-year NHS trusts in 2015/16).

The survey was launched in November 2015 using RAND Europe's SelectSurvey tool. The survey was finally closed on 28 February 2016. In total, we received 168 completed responses (a response rate of 23.2 per cent). It should be noted that it was difficult to secure a higher response rate from NHS bodies, in particular from NHS Trusts, which is reflected in the overall lower response rate for NHS bodies. A full breakdown by category of body is shown in Table 26.

For a potential rerun of the survey we suggest achieving a response rates around 30% (per cohort and overall) which should be sufficient in order to create a dataset that is comparable to the baseline survey. Particular effort should be invested in securing a higher response rate for the health bodies. This could be for example done by drawing in

more representatives from the health sector to support the survey (who could be also part of the Advisory Panel) and send internal messages about the survey to their particular organisations to generate more buy-in from staff members. Another option would be to send out the survey to a specified list of professionals with an individualised email so that the sample of people can be more targeted. This could generate more awareness of the survey as for example posting a link to the survey via an internal information system (however systems like the NHS England Portal could be also used as an additional distribution channel).

Table 26: Response to local body survey

Type of body	Total surveyed	Respondents	Response rate
Local authority	354	103	29.1%
Fire and rescue authority	31	10	32.3%
Police bodies	42	15	35.7%
Clinical Commissioning Groups and NHS Trusts	301	41	13.6%
TOTAL	728	169	23.2%

RAND Europe made considerable efforts during the period when the survey was open to secure a high response rate. The survey was kept to a minimum and the covering letter made it clear that it could be completed within 15 to 20 minutes. We also explained clearly the background to the survey and the importance of gathering baseline data for the purposes of assessing the impact of local audit reform and ensuring that the quality and effectiveness of audit arrangements were maintained.

We also worked closely with a number of agencies to raise the profile of the survey and to raise the response rate. In particular:

- RAND Europe sent out three reminders to recipients of the survey and extended the deadline for completion on three occasions.
- A reminder about the survey was posted three times on the NHS England Portal.
- The NHS Trust Development Authority (TDA) sent out three emails regarding the survey which was circulated to NHS Trust Directors of Finance and copied to Deputy Directors of Finance.
- DCLG included text about the survey in the Permanent Secretary’s regular update to local authority Chief Executives.
- The Local Government Association (LGA) included a reminder about the survey in its Finance Bulletin, and subsequently via its finance e-bulletin.
- DCLG’s fire and rescue policy team sent out a reminder about the survey to its Fire Finance Network communities list.
- The Police Resources Policy Team, Efficiency and Resources Unit, Crime and Policing Group at the Home Office mentioned the survey at the meeting of the Police and Crime Commissioners Treasurers Society (PACCTS).

E. Interviews with audit firms

In considering how to gather the views of audit firms, we opted to undertake semi-structured interviews with the partners/directors leading the audit of local public bodies' work. These individuals were identified with the assistance of David Aldous, Director of Local Government at the National Audit Office, who chairs the Local Auditors' Advisory Group (LAAG) of firms carrying out these audits. They were deemed the people most likely to be able to provide an authoritative firm perspective. Interviews as a means of gathering the views of firms were chosen as an alternative to a written survey because we considered the latter would generate weaker and less substantial evidence, and that there would be less opportunity to discuss issues arising out of the individual circumstances of each firm (e.g. location, scale of local audit work).

Audit firm	Contact person
Deloitte	Craig Wisdom
Ernest & Young	Karl Havers
Grant Thornton	Jon Roberts
KPMG	Trevor Rees
Mazars	Gareth Davies
BDO	David Eagles, Malcolm Thixton
PwC	Lynn Pamment

The interviews with the audit firms help to examine how audit firms have responded to the changing environment after the announcement of the abolition of the Audit Commission and the introduction of the 2014 reforms. The structure for the interviews is at Appendix E: 'Interviews with audit firms'.

F. Advisory Panel

An Advisory Panel of interested parties was established by DCLG. The purpose of the Advisory Panel was to provide a forum for key external organisations to comment on the scope of the project, the research design, the core outputs, to help signpost to relevant data, evidence and sources of information; rather than being a discussion of policy.

The members of the Advisory Panel were:

- Shazia Ahmad (Financial Reporting Council)
- David Aldous (National Audit Office)
- Margaret Greenwood (University of Bath)
- Keeley Lund (CIPFA)
- Keith Morton (Department of Health)
- Dennis Skinner (Local Government Association).

Meetings were attended by officials from DCLG and the RAND Europe team. The group met in June and November 2015, and in February 2016, to discuss the aims and objectives of the project, as well as interim and draft final outputs from the research.

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Appendix C: Detailed Theory of Change description

1. Long-term policy objectives, related outcomes and activities

This section describes the stated policy objectives, the expected mid- and long-term outcomes that need to be achieved in order to secure the objectives, and the agreed activities being carried out (and the relationships between them), as well as relevant indicators that are shown in the ToC diagram. First, those policy objectives and related outcomes linked to the conduct of audit within LPBs will be described; second, those policy objectives and related outcomes linked to the regulation of the auditors and the audit regime will be described.

2. Policy objectives and outcomes related to local public bodies (LPBs)

2.1 Policy objectives and long-term outcomes related to the conduct of audit within LPBs

Policy objective 1: Develop a diverse and competitive market for local audit service providers. This objective, while not explicitly listed in the reform plan, is implicit in various documents describing the local audit regime change and appears of high importance.⁸⁹ The achievement of such a state is conditional on a set of **long-term outcomes** (see ToC diagram): opening up the local audit market to a wider range of providers (including smaller, local firms) so that LPBs have more choice of auditors on the market; increasing the transparency around the cost of audit services so that there is greater visibility as to what is included in fees (which may prompt discussions about reductions); and ensuring the presence of incentives for the reduction of the costs by auditors (for example, through innovation in audit approach and elimination of unnecessary work). To fulfil this objective, it is also important that the market is capable of meeting the specific needs of different categories of public body and that work can be tailored to different sectors.

Policy objective 2: Maintain competitive audit fees (or reduce audit fee levels). To achieve this objective the government considers there needs to be a set of **long-term outcomes**: increased transparency around the costs of local audit services, and the removal from the audit fees of costs associated with non-audit activities which individual LPBs have not commissioned. Audit fees previously covered the cost of the actual audit service but also a top slice to pay for Audit Commission corporate costs and the cost of its other work. Furthermore, there will need to be incentives for auditors of LPBs to reduce the costs of their audits through greater competition and innovation and greater exposure of their costs to LPB scrutiny so that bodies can see what work auditors are doing for the purposes of giving an opinion.

⁸⁹ For example, the 'Local audit impact assessment for the Local Audit and Accountability Act 2014', which states that: 'Ending state provision of audit services and increasing competition in the market will drive better value for money for the taxpayer.'

Policy objective 3: Save £1.35bn as part of the overall local audit reform programme under way. The DCLG has estimated that the introduction of the new local audit regime will result in saving a total of £1.35bn over the course of ten years from 2009/10. The **long-term outcomes** required to help secure this policy objective are similar to those for the first objective stated above. Savings will be secured by further reductions in audit fees, which are expected to be generated by greater transparency of costs of local audit services, incentives provided for auditors to reduce costs of local audits, and the ending of non-audit activities. In addition reforms to the oversight of the public audit regime is expected to generate a more efficient regulatory system for all audit work. This will be in addition to the reduction secured as a result of the ending of inspection and assessment work.

2.2 Related medium-term outcomes

In order to achieve the above stated long-term outcomes (which in turn are designed to secure the fulfilment of the three key policy objectives related to the conduct of audit within LPBs) certain **outcomes also need to be accomplished in the medium-term.**

In particular, LPBs having an enhanced choice on the market depends on local appointment of auditors for LPBs from a competitive market and having the possibility to request non-audit assurance services, within the boundaries of what is appropriate work.

An increase in the transparency of costs of local audit services depends on the same medium-term outcomes as well as LPBs paying only for actual audit services which no longer include costs for any other Audit Commission activities.

Furthermore, whether incentives for LPB auditors to reduce costs are created will depend on the responsiveness of the auditors of LPBs to the audit needs of the sector. The expectation is that auditors will be more responsive if they come under greater pressure from LPBs. This pressure may be generated from LPBs by greater awareness of the costs of their audit service and thus greater interest in securing value from it. This may arise from LPBs directly incurring costs themselves relating to the procurement and management of audit contracts, which were previously incurred by the Audit Commission, as well as paying for the actual audit services only.

2.3 Activities undertaken to achieve mid- and long-term outcomes

There are a number of activities included as part of the reforms designed to yield the aforementioned outcomes and in turn achieve the policy objectives. Following outsourcing in 2012, all local government audit work is now undertaken by private sector firms with staff with suitable qualifications and experience. Under the reforms, responsibility for commissioning auditors is being transferred to local appointment by LPBs. They will have the option to go it alone and procure themselves, procure jointly with other LPBs or use a sector-led collective procurement body. Where they decide to go alone, they will be expected to establish an independent audit panel to be consulted on the appointment. Furthermore, LPBs with an annual turnover not exceeding £25,000 are exempt from external audit, while those with a turnover between £25,000 and £6.5m are subject to a proportionally smaller regulatory regime. Finally, wider reforms have already put an end to the routine inspections and assessments (including CAA) which were undertaken by the Audit Commission.

2.4 Indicators used to assess the policy objectives and mid- and long-term outcomes

The extent to which these three policy objectives are met will be measured both directly and indirectly using a set of key indicators. Each indicator is likely to be supported by other qualitative and quantitative evidence in future evaluations. The list of indicators and the way these are assigned to the ToC are illustrated in section 2.2 above (see ToC graphic and table listing indicator).

Policy objective 1 can be measured by looking at the number and type of audit firms participating in the market at the baseline year (2009-10) and post-reform (indicator 1). Another element that needs to be taken into account is also the number of people gaining a qualification to do public audits, without whom an expanded market will be impossible given the specialised nature of local audit (indicator 16)

Policy objective 2 can be measured directly by comparing the pre- and post-reform fee levels; we propose treating the fee levels in the 2009/10 financial year as the baseline; the information on the fee levels are subsumed as a part of the indicator on the annual costs of the audit regime (indicator 2).

Policy objective 3 can be measured directly by comparing the total annual costs of the audit regime (indicator 2) before and after the implementation of the reforms. Consideration of the change would need to take account of any major alterations in the nature of the work undertaken by auditors as well as major changes in the organisation of local service delivery.

An indirect assessment of the extent to which the policy objectives are met can be made by looking at indicators related to whether the **long- and medium- term outcomes** are achieved. With regards to the key long-term outcomes:

- Whether LPBs have enhanced choice of auditors through the market and whether the different sector needs are being met can be assessed by looking at the number and characteristics of audit firms registered and undertaking local public audit (indicator 1), as well as the number of people seeking a qualification to do public audits (indicator 16). Furthermore, survey evidence will provide some evidence on the level of satisfaction among LPBs with the quality of the audit services and value received (indicator 7).
- The increase in the transparency of costs can be measured by surveying LPBs on the extent to which they are clear about the composition of audit fees (indicator 10).
- Evidence on whether the reforms provided incentives for fee reductions will include data on fee levels at baseline year and subsequently (indicator 2), as well as survey evidence from audit firms on whether they consider they were provided with incentives to reduce their audit fees (indicator 11).

The medium-term outcomes can also be tracked through a number of indicators:

- The ability of LPBs to appoint their own auditors locally from a competitive market which better suits their needs, can be measured by looking at the numbers and characteristics of audit firms operating in the market (indicator 1). This will be supported by evidence on the extent to which audit firms feel they were provided with incentives to reduce audit fees (indicator 11).

- The level of satisfaction with the audit services provided, as reported by LPBs, can be used to assess how well LPB auditors responded to various sectors' needs (indicator 7).
- Data on whether, and to what extent, LPBs incur internal costs for procurement of audit and for complying with the new audit regime, and whether they only pay for actual audit services, can be identified from the costs data (indicator 2).
- The number of qualified audit firms conducting public audit (indicator 1), as well as the level of satisfaction of LPBs with the audit services (indicator 7) can serve as indicators for the extent to which LPBs have the possibility of choosing different audit services and those which are most suitable for them.

3. Policy objectives and outcomes related to the regulatory bodies

3.1 Policy objectives and long-term outcomes related to the regulation of the auditors and the audit regime

Policy objective 4: Deliver greater local accountability and transparency. Public audit provides detailed information on how public funds have been spent and allows a range of stakeholders including residents to know how money entrusted to public bodies has been used. Where they have concerns it provides the basis for holding public bodies and their representatives to account. This policy objective is linked to four main **long-term outcomes** which government wants to see achieved through the reforms. These outcomes are:

- Continuing the use of audit to provide assurance to elected members and paid officials that funds have been spent appropriately.
- Maintaining the local accountability and quality of audit services.
- Continuation of the ability of the audit regime to identify financial problems within local bodies.
- Increasing the transparency around the cost of local audit services.

Policy objective 5: Uphold high standards of auditing. The quality of audit is related to adherence to technical standards set by the audit and accounting professions, as well as timeliness in undertaking and reporting the work, which ensures that the outputs are useful to decision makers and assurance on the use of public funds given in a timely manner. In the particular context of the audit of public funds, high standards of audit also require a broader assessment of the value for money and propriety with which funds are used. Fulfilment of this objective is conditional on the achievement of four long-term outcomes. These are:

- Maintaining the local accountability and quality of audit services.
- Having a more efficient regulatory system for all audit work.
- Ensuring that data and knowledge of sector performance issues continues to be gathered by the NAO, but at a lesser cost than under the Audit Commission regime.
- Maintaining the ability of the audit regime to identify financial problems.

3.2 Related medium-term outcomes

In order to achieve the above-mentioned long-term outcomes (which in turn are designed to secure the fulfilment of the key policy objectives) certain medium-term outcomes also need to be accomplished.

Elected members and the public will continue to receive assurance on the appropriate use of public funds if the auditors of LPBs continue to conduct independent audits which are undertaken in adherence to the auditing and ethical standards, and continue, where necessary, to issue 'reports in the public interest'.

The maintenance of local accountability and quality of audit services depends on the achievement of the following set of mid-term outcomes: the public needs to continue to be able to raise objections on specific items of expenditure and the arrangements for doing this need to be simple and transparent so that they are easily exercised. Furthermore, local auditors must continue to be able to conduct their work independently, applying applicable auditing and ethical standards. Where they have cause for concern about the way public funds have been spent they must be able to report publicly without fear. In addition – where in place – auditor panels need to be seen to be working effectively and making recommendations which are acted upon in a transparent way.

The desired long-term outcome of efficiency gains in the regulation of local audit arises from LPB auditors being subject to the same regulation as that of the private sector, which will allow for the exploitation of efficiencies as a result of merging regulatory regimes through the FRC, given that the firms involved in both are often the same.

Maintaining sector wide knowledge about performance (but at a lesser cost than under the Audit Commission regime) is contingent on the NAO undertaking suitably targeted studies of themes across local public bodies, and publishing a number of reviews on cross-sector themes within the agreed budget.

The continuation of the ability to identify financial problems depends on the local auditors continuing to conduct independent audits, as well as auditors applying auditing and ethical standards to public audits.

3.2.1 Activities undertaken to achieve mid- and long-term outcomes

The above-mentioned outcomes are expected to be achieved by a set of activities which are primarily undertaken by the new regulatory bodies (although some of the activities related to the LPBs also feed into the achievement of the respective policy goals). In addition, the wider public can play a role by lodging objections to items within an account (albeit increased discretion has been given to auditors regarding the investigation of the objections).

The set of activities related to the regulatory bodies (the Financial Reporting Council (FRC), NAO and professional bodies) includes the transfer of local audit regulation to the FRC. Currently, audit firms have to meet requirements laid out by the Companies Act 2006 before they can be a statutory auditor for a listed company, and they also needed to meet a separate set of requirements set by the Audit Commission to act as a statutory auditor of a local public body. Monitoring of audit quality and the work of the firms is also undertaken under the Companies Act 2006 by recognised supervisory bodies (the professional institutes) and the FRC, and under the Audit Commission Act 1998, local public audit quality was assessed by the Audit Commission. Moving the regulation of the local public

audit regime to the FRC and professional audit bodies is designed to remove the duplication and rationalise arrangements.

In order to uphold high (and consistent) standards of audit the NAO has taken over the role of preparing and updating the Code of Audit Practice and related guidance. The NAO has also taken on the role of preparing value for money studies in the local government field which will ensure that sector-wide performance information and analysis is still available, albeit on a limited number of topics. The same broad scope of public audit will continue to be undertaken by auditors of local public bodies. Together these measures are designed to achieve the overall objective of upholding high standards of auditing.

3.2.2 Indicators used to assess the policy objectives and mid- and long-term outcomes

Fulfilment of the above described policy objectives as well as long- and mid-term outcomes which will contribute to meeting the objectives can be measured using several indicators. Each indicator is likely to be supported by other qualitative and quantitative evidence in future evaluations. The list of indicators and the way these are assigned to the ToC are illustrated above (see ToC graphic and table).

Policy objective 4 – the extent to which greater local accountability and transparency have been delivered – can be measured using proxies which reflect the importance of opportunities for local spending to be challenged/problems publicised, and the quality and conduct of audit work to be scrutinised. In particular:

- The number of cases in which local electors lodged an objection to items within the accounts and the number of cases in which auditors decided to investigate (indicator 3).
- Number of cases where accounts were qualified (indicator 4).
- The health of the audit system (indicator 5) which entails: the number of cases in which local bodies failed to appoint an auditor (both principal bodies and smaller bodies); the number of violations of the FRC Auditing Practices Boards ethical standards; number of removals or resignations of auditors.
- The number of PIRs issued (indicator 6).
- The number of small LPBs complying with the newly introduced transparency standards (indicator 9).

Changes over time in these indicators will need to be interpreted with care. For example, a reduction in the number of Public Interest Reports issued could be seen as a sign of an improvement in local financial management or might be a sign that auditors were reluctant to raise concerns. Several of these indicators are also likely to be nil returns or a very small number of cases.

Policy objective 5 – upholding high standards of auditing – can be assessed by looking at two measures reflecting different perspectives on quality. These are:

- The levels of satisfaction with the quality of audit services (indicator 7) as reported by LPBs.
- The technical quality of audit work as assessed by the FRC (indicator 8).

In terms of **long-term outcomes**, the extent to which elected members and other stakeholders continue to receive assurance on the appropriate use of public funds can be measured by looking at:

- The number of cases where accounts were qualified (indicator 4).
- The number of PIRs issued (indicator 6).
- The timeliness of the delivery of audited accounts (indicator 14).

The degree to which local accountability and quality of audit services are maintained can be assessed by looking at trends in the exceptions to the smooth running of the audit process:

- The health of the audit system (indicator 5) which entails: the number of cases in which local bodies failed to appoint an auditor (both principal bodies and smaller bodies); the number of violations of the FRC Auditing Practices Boards' ethical standards; the number of removals or resignations of auditors.
- The more subjective views on the quality of the audit services as derived from the survey of LPBs (indicator 7).
- The technical quality of audit work as assessed by the FRC (indicator 8).
- Evidence that independent auditor panels are working effectively, gained by identifying extent to which recommendations are adhered to (indicator 15).

The efficiency of the regulatory system will be assessed by:

- Looking at the annual costs of the local audit regime (indicator 2).
- Looking at the satisfaction levels of audit firms with the new regime (indicator 12).

An assessment of the extent to which knowledge of sector performance issues is maintained (but at a lower cost than before) can be done by:

- Annual costs of local audit regime in particular the costs associated with regulatory oversight (indicator 2).
- Information on VFM reports by the NAO related to LPBs (indicator 13).

Finally, continuation of the opportunities for local financial problems to be identified can be tested using:

- The number of cases in which local electors lodged an objection to items within the accounts and the number of cases in which auditors decided to investigate (indicator 3).
- The number of cases where accounts were qualified (indicator 4).
- The number of Reports in the Public Interest issued (indicator 6).
- The number of relevant VFM reports produced by the NAO which highlight financial management issues (indicator 13).

With regards to **medium-term outcomes**, the extent to which auditor panels are in place and work in an effective and transparent way could be tracked by the proxy measure of LPBs following the auditor panel recommendations (this would at least show some consistency in the coordination between panels and LPBs which could be perceived as panels working effectively if the majority of LPBs follow the recommendations). The extent to which the ability of the public to raise objections to spending is maintained can be

estimated by looking at the number of cases in which local electors lodge an objection to items within the accounts and the number of cases in which auditors decide to investigate the issue (indicator 3).

The issue of whether the regulation of LPB auditors becomes more efficient through merger of arrangements with those applied to the private sector will be answered by reviewing arrangements and FRC costs, and by assessing the level of satisfaction of audit firms with the new regulatory regime (indicator 12).

Assurance that the audits are conducted independently will draw on a number of proxy indicators:

- The number of cases in which local electors lodged an objection to items within the accounts and the number of cases in which auditors decided to investigate (indicator 3).
- The number of cases where accounts were qualified (indicator 4).
- The number of Reports in the Public Interest issued (indicator 6).

Evidence on whether auditors continue to apply auditing and ethical standards to public audits will be derived from proxy indicators around the health of the audit regime (indicator 5):

- The number of cases in which local public bodies failed to appoint an auditor.
- The number of cases of violations of the FRC Auditing Practices Boards' ethical standards in local audits.
- The numbers of cases where LPBs remove their auditors or they decide to resign.

Finally, whether or not sector-wide performance reviews take place can be determined by looking at the number of reports relating to LPBs issued by the NAO (indicator 13).

4. Underlying assumptions and potential risk areas

Articulation of the Theory of Change is underpinned by a set of assumptions – both general (e.g. about the political environment) and specific (e.g. about particular behavioural reactions to the reforms). These assumptions were made implicitly and explicitly by DCLG officials in the course of designing the reform of local audit, based on the evidence available to them and their judgement of how particular stakeholders are likely to react to changes in the audit regime. The purpose of this section – which draws on discussions with DCLG officials – is to be as explicit as possible as to what the main assumptions are, and what are the potential risks associated with them, should the actual outcomes deviate significantly from one or more assumptions.

There are two main (sets) of questions that can be explored in this context:

- What are the underlying assumptions of the ToC?
- What will happen if these assumptions do not hold? If things are not developing as planned, what would we expect to see?

Table 6 in Part 2 of this report maps out the potential risks and the possible impact if outcomes are only partly achieved, not achieved, or occur in an unexpected way. The risks relate to three key areas which were identified in discussion with DCLG officials:

- **Market development**, i.e. the market for local audit does not develop as assumed
- **Public and regulatory oversight**, i.e. accountability arrangements put in place do not maintain or develop a robust audit regime, and the quality of audit work declines
- **Political context**, i.e. the new audit system put in place does not meet the needs of the changing context in which LPBs operate, leading to a decline in confidence in the arrangements.

Appendix D: Survey instrument for local public bodies

SURVEY INSTRUMENT

Welcome

Background

This survey is part of a research project, funded by the Department for Communities and Local Government and supported by the Department of Health, designed to capture baseline data for a future evaluation to assess the impact of changes to the local audit regime. These changes have been introduced since 2010 including under the Local Audit and Accountability Act 2014. They include the abolition of the Audit Commission (which took place in 2015), changes to the appointment of auditors (which will take place after the transitional arrangements overseen by PSAA end), and changes to the regulatory framework (which were initiated in 2015).

Use of the survey results

This survey is a key data source for a future evaluation and is designed to gather your views on the impact of the changes to the local audit regime. Your responses will help to ensure that a future evaluator will have access to a sound evidence base in order to understand whether reforms have improved the efficiency of the local audit regime and the quality of audit. It is therefore important that we secure the views of a wide range of local public bodies in different sectors across the country.

Data protection

While individual survey responses are identifiable to the RAND Europe research team in order to allow matching outcomes with later surveys, the data will be treated in confidence and will be reported only as part of aggregated data. The responses will be kept for the duration of the evaluation project.

RAND Europe adopts good industry practices regarding the protection of personal data as part of its obligations as a Data Controller under the Data Protection Act 1998 and takes appropriate technical and organisational measures conformant with ISO 27001 to protect personal data. Respondents to this survey have the right to oppose, have access to, rectify, or remove personal or sensitive personal data held by RAND Europe.

Target audience

The survey should be completed by, or on behalf of, the senior finance officer in the organisation and be considered as a definitive statement of the organisation.

Completing the survey

The survey consists of six sections in which we ask you about the following:

- I. Your organisation
- II. Your existing audit arrangements
- III. Satisfaction with current audit arrangements
- IV. Views on the issues behind the local audit reforms

- V. Views on the implications of the changes brought in by the reforms
- VI. Accountability and transparency for public spending

We estimate that it will take you in total 10-15 minutes to complete the survey. **Please note that draft answers cannot be saved – the survey needs to be completed in one sitting.**

If you have any queries related to the survey or the project, please do not hesitate to contact us using the following email address: [an email alias].

I. – Your organisation – background information

In this section, we ask you for basic information about your organisation and your role in it.

Please provide the name of the local public body you represent:

Please specify the category your local public body belongs to:

- Local authority
- National Health Service body
- Police bodies (including police and crime commissioner)
- Fire and rescue authority
- National park body
- Combined authority
- Other (please specify).

What is your role within the organisation?

- Chief Executive or equivalent
- Finance director
- Other senior management not covered in a) or b)
- Finance team staff member
- Other (please specify)

Are you the main audit contact?

Yes/No (please specify)

Please specify the annual revenue of your local public body:

- Up to £6.5m
- £6.5m-£24.9m
- £25m-£49.9m
- £50m-£74.9m
- £75m-£100m
- More than £100m.

Please specify the outward code of the postcode (the part before the single space in the middle) of the area in which your local public body is based/operates):

II. – Your existing audit arrangements – background information

Please specify your current external auditor

- Deloitte

- Ernst & Young
- Grant Thornton
- KPMG
- Mazars
- BDO
- PwC
- PKF Littlejohn

Please provide the year when your current external auditors were appointed

[Drop-down menu]

- Pre-2012
- 2012
- 2013
- 2014
- 2015

III. – Satisfaction with current audit arrangements

The Government’s reforms are designed to improve the responsiveness and value for money of the external audit service received by local public bodies. In this section we ask about your CURRENT external audit arrangements so that a future evaluation can assess whether these objectives are met.

1. How satisfied are you with:

	Completely satisfied	Mostly satisfied	Partially satisfied	Not at all satisfied	Don't know
...the ease with which audit firms can provide staff and capacity to conduct the audit in a timely manner?					
...the ease with which you were able to get an earlier involvement of the auditor when preparing the accounts?					
...the ease with which you are able to contact and communicate with your audit firm?					
...the extent to which your last audit plan was tailored to focus on key risks and priorities faced by your organisation?					
...the timeliness of reports?					
...the practicality of report recommendations?					
...the usefulness of reports?					
...the impact of audit reports on the operation of your organisation?					

...the extent to which external auditors place appropriate reliance on internal audit					
...the effectiveness of your organisation in reducing the costs of external audits?					

2. Do you agree with the following statement in relation to your most recent audit:

	Yes, it was completely appropriate	It was acceptable	No, it was not appropriate	Don't know
'My initial audit fee was appropriate'?				

3. Do you agree with the following statement in relation to your most recent audit:

	Yes	No	Don't know
'Any revisions to the fee were clearly communicated and explained'?			

4. Which of the following actions has your auditor undertaken in the course of recent audits? (select all that apply)

Approach taken to the work

<input type="checkbox"/> Provided advice/guidance/helped to address important issues
<input type="checkbox"/> Been a true 'critical friend'/developed a good working relationship with us
<input type="checkbox"/> Been good at communicating/keeping in touch
<input type="checkbox"/> Been available to discuss/listen to issues about the operation of this organisation
<input type="checkbox"/> Demonstrated good knowledge and understanding of this body

Focus of the work

<input type="checkbox"/> Helped improve our management arrangements
<input type="checkbox"/> Helped demonstrate/highlight best practice/share information from elsewhere
<input type="checkbox"/> Encouraged my organisation to prioritise/provided action plan
<input type="checkbox"/> Provided benchmarking/comparative data
<input type="checkbox"/> Given honest and constructive feedback on our performance

- Helped improve financial management and governance

5. Which of the following changes would you like to see made to improve the overall impact of your audit? (select all that apply)

Type and scale of work carried out

• More proportionate/risk based audit
• Reduce the fee level/charges
• Be less burdensome in terms of time/effort
• Provide more regular reports/more up to date/ better quality reports
• Focus more on the 'bigger picture' and less on detail

Staffing and relationships

• Closer/better working relationship with organisation/relationship manager
• Improve the quality of staff
• Improve the continuity/consistency of staff
• Better/more regular communication/feedback
• Working together/joint approach with other agencies

IV. – Views on the issues behind the local audit reforms

The Local Audit and Accountability Act 2014 was introduced to tackle a number of perceived problems with the conduct of the audit and inspection of local bodies. These included fee levels, the ability to influence the choice of auditor and the coverage of work undertaken by external auditors. In this section we ask for your views on the issues covered by the 2014 reforms.

6. How far do you agree with the following statements?

	Strongly agree	Somewhat agree	Neither agree nor disagree	Somewhat disagree	Strongly disagree	Don't know
"To date, my organisation has been concerned that we have been paying too much for our audit over the last three years."						
"To date, my organisation has not						

been clear what our audit fee has included.”						
“To date, my organisation has been concerned at arrangements for the appointment of auditors.”						

V. – Views on the implications of the changes brought in by the reforms

The Local Audit and Accountability Act 2014 is bringing in a series of CHANGES IN THE FUTURE to the arrangements for local public audit. In this section we ask for your views on these changes.

7. How far do you agree with the following statements?

	Strongly agree	Somewhat agree	Neither agree nor disagree	Somewhat disagree	Strongly disagree	Don't know
'Local appointment of auditors will be a valuable change for my organisation.'						
'My organisation is well equipped to make an informed choice about its auditor.'						

Where you have disagreed with either or both of the above statements, please could you explain briefly your reason.

[Open question]

For your first contract procurement, currently do you envisage:

[Drop down menu – one option only possible]

a) Going alone in appointing your auditor
b) Participating in a joint procurement exercise with other bodies
c) Taking advantage of a sector-led body if they are established
d) Undecided

Do you expect that the changes to the local audit regime will:

[Drop down menu – one option only possible]

a) Improve the quality of audit of your organisation (e.g. the usefulness of the work, quality of contact with the firm)
--

b) Make no difference
c) Lead to a decline in the quality of the audit of your organisation
d) Not sure/don't know

Do you expect that the changes to the local audit regime will:

[Only one option possible]

a) Lead to the audit fee charged by your auditor to your organisation going down
b) Make no difference to the audit fee charged by your auditor to your organisation
c) Lead to the audit fee charged by your auditor to your organisation going up
d) Not sure/don't know

VI. – Accountability and transparency for public spending

Objectives of the reforms include delivering greater local accountability and transparency and upholding standards of audit. The Government also considers that greater transparency in the appointments process and of audit outputs will increase the ability of the public to hold local decision-makers to account. In this section we ask for your views on how the 2014 reforms will help to deliver these objectives.

8. How does your authority/NHS body currently disseminate information on spending to help local residents and service users understand how public funds have been spent?

[Drop down menu for these options – multiple options possible]

Press conference
Announcements on own billboard
Announcements on own website
Social media
Email newsletter
Handouts/flyers/printed newsletter
Newspaper announcements
Radio announcements
Public hearings
Other (please specify)

9. In the last financial year (2014/15), how many (if any) objections to accounts have there been from electors?

10. Final thoughts

Is there anything else about your external audit service and the reforms to local audit arrangements that you would like to share with us?

[Open question]

Thank you very much for your time.

The results of this survey will feed into the final report that RAND Europe will prepare for the Department for Communities and Local Government in early 2016. The report will include the description of a method for a future evaluation of the reforms set out within the Local Audit and Accountability Act 2014, as well as a set of baseline metrics and analysis from which a subsequent evaluation might measure impact. The survey results will form part of the baseline metrics and analysis.

Please do not hesitate to contact us if you have any questions or would like to raise any issue, at [\[email\]](#).

Appendix E: Interviews with audit firms

Section	Question
Background information	<ol style="list-style-type: none"> 1. What is your role within your firm? 2. What types of local public bodies does your firm conduct audits for and in which regions are you active? 3. How many LPB audits do you have? Where can we find what is your overall annual revenue annually from doing local audits?
Existing and recent audit arrangements (pros and cons)	<ol style="list-style-type: none"> 4. How satisfied were you with the arrangements under the Audit Commission? What was good and what less good about it? 5. What difference has the establishment of PSAA made? 6. How satisfied are you with the procurement process for local audit services? What are the pros and cons? 7. How satisfied are you with the current fee levels? 8. How satisfied are you with the current contract conditions and contract volume compared to the risks involved and the quality requirements to the work?
Views on the importance of areas covered by the local audit reforms	<p>The objectives of local audit reform were set out by the government: develop diverse and competitive market, maintain competitive audit fees or reduce fees, save £1.35bn, deliver greater accountability and transparency, uphold standards of audit</p> <ol style="list-style-type: none"> 9. Does your firm have any views on the significance of these objectives? Have these views been publicly articulated? 10. Do you consider that there is a need to develop a diverse and competitive market for local audit service providers? 11. Do you have any views or concerns about accountability, transparency and standards of audit under current arrangements?
Views on changes to audit arrangements in the future and assessment of anticipated market responses to the changes	<ol style="list-style-type: none"> 12. Do you believe the changes to the local audit regime – particularly changes to appointment – will have an impact on fee levels? If so, how? 13. What do you consider are the opportunities and risks of alternative arrangements – local appointment, sector-led body? 14. Will the changes to the local audit regime have an impact on the attractiveness, risks and requirements for doing local audits? If so, how? 15. Will the changes to the local audit regime have an impact on the type of work you undertake for LPBs? If so, how?
Barriers to entry to the market/sustainability of participation in the market	<ol style="list-style-type: none"> 16. Looking at the current eligibility criteria (resources, staff post-qualification experience in doing local audits), how do you consider these affect firms' ability to enter the market (in case contracts are extended until 2020)? 17. To what extent do you agree/disagree with the following statement: 'Firms have to make high upfront investments to enter the market'

18. How do you expect the market to develop?
- How will the amount of work develop?
 - Will there be enough staff qualified for doing local audit in the future?
 - Will smaller firms be in the same position to bid for work as compared to bigger firms?
 - What is the likelihood that firms discontinue local audit services to be able to provide consultancy services?

Regulatory regime

19. What do you consider were the pros and cons of the previous regulatory regime?
20. What views do you have about the changed regime – with NAO and FRC responsibilities?
21. What impact (if any) have these changes had so far? If too early, what impact do you expect them to have?
22. Do you consider the regulatory regime in place after the 2014 reform will be sufficient for safeguarding the overall quality of local audits?
23. Do you expect the changes to regulation will have any impact on the regulatory expectations for carrying out local audits?
24. Do you consider the regulatory framework to be appropriate or a burden?

Other roles

25. How significant is the responsibility for reporting in the public interest?
26. Do you expect there will be any significant changes to your obligations around this in the future?

Appendix F: Theory of Change diagram and overview of indicators

Table: List of indicators

No	Theme	Indicator
1	Number of participating audit firms	Number of audit firms registered and undertaking local public audit work, including information on size/turnover of audit firm; market share; and value of contracts held with local public bodies.
2	Annual cost of local audit regime	Annual cost of local audit regime including procurement costs, fees paid, regulatory oversight, etc.
3	Local elector objections to accounts	Number of cases in which local electors lodge an objection to items within the accounts/number of cases in which the auditor decided to investigate.
4	Qualification of audit opinions	Number of cases where the audit opinion on local public body accounts is qualified.
5	Health of the audit system	Number of cases in which local bodies failed to appoint auditor by principal bodies and smaller bodies; number of cases of violations of the FRC Auditing Practices Board's ethical standards in local audits; number of cases where local public bodies removed their auditors/auditor resigns.
6	Public Interest Reports	The number of Public Interest Reports issued.
7	Satisfaction with audit services	Level of satisfaction with the quality of audit services amongst local public bodies.
8	Measure of the technical quality of audit	Measure of technical quality of audit undertaken (where quality is defined as compliance with the Audit Commission's regulatory requirements and with professional standards).
9	Small local public bodies' compliance with transparency expectations.	Number of small local public bodies not complying with transparency standards.
10	Local public bodies' views on composition of fees	Extent to which local public bodies are clear about the composition of the audit fees.
11	Audit firms' views on fee levels	Extent to which firms feel incentivised/encouraged to reduce audit fees.
12	Firms' satisfaction with the regulatory regime.	Level of satisfaction of audit firms with new regulatory regime.
13	Data and knowledge of sector maintained.	Number of NAO reports published relating to local public bodies and existence of broader, sector-led data sources.
14	Meeting of statutory deadlines for audit	Number of cases where: Approval of accounts not done by 30 June 2010 Number of delays in having accounts published Audit opinions issued by 30 September
15	Role of auditor panel	Number of local public bodies that did not follow auditor panel recommendations.

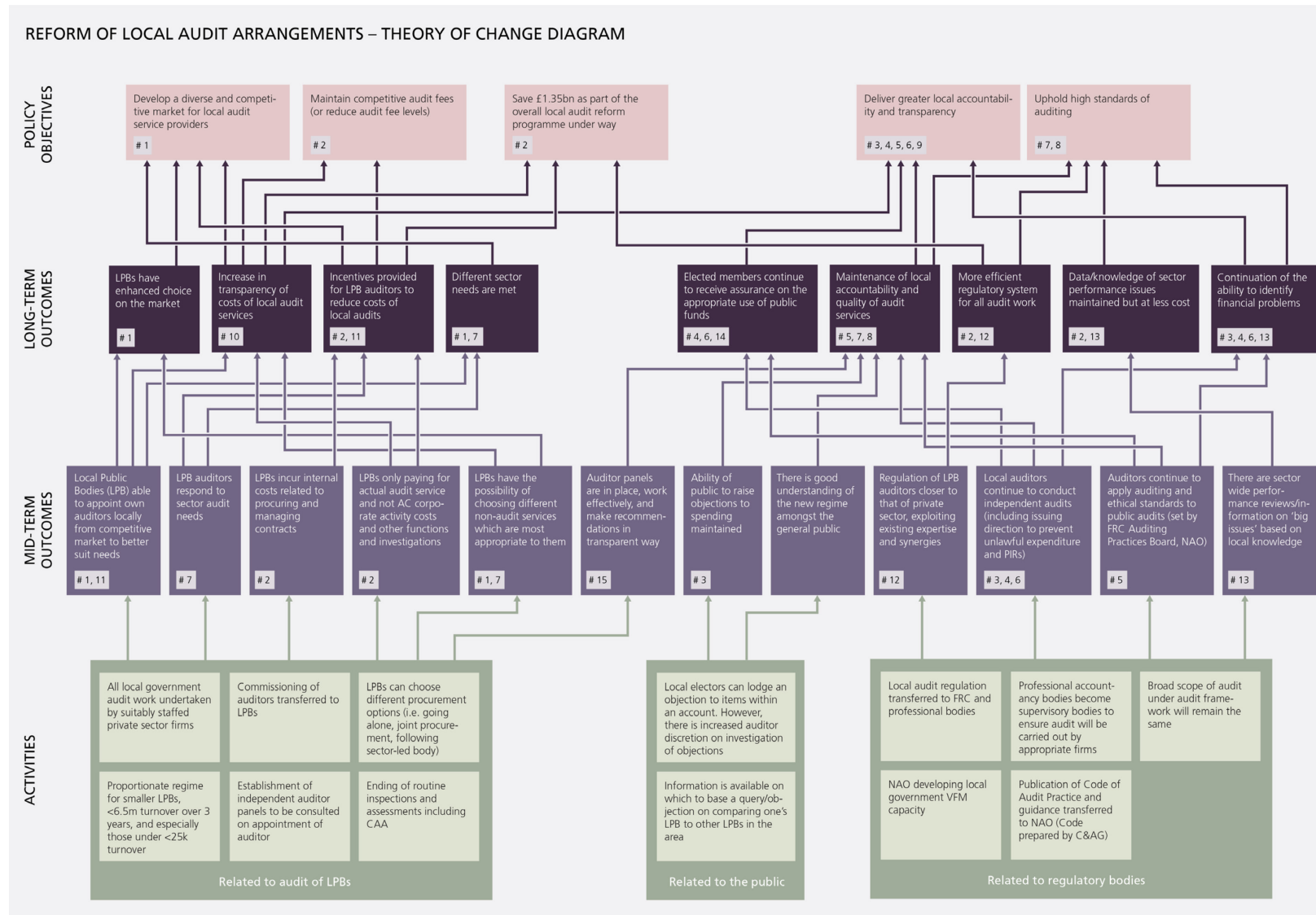
Table: Indicators and report section that describes baseline data

No	Indicator theme	Type of evidence	Responsibility for data collection in interim period and/or at time of evaluation		Report section describing baseline data
			<i>Local government</i>	<i>Health bodies</i>	
1	Number of firms in local audit work	Official data	PSAA Sector-led bodies	NHS England NHS Improvement NAO	Section 3.4.1
2	Cost of local audit regime	Official data	PSAA Sector-led bodies Regulatory bodies	NHS England NHS Improvement	Section 3.4.2
3	Number of objections by local electors	Official data	Sector-led bodies	N/A	Section 3.4.5
4	Qualification of audit opinions	Official data	Sector-led bodies	NHS England NHS Improvement	Section 3.4.6
5	Health of audit system – e.g. violations of ethical standards, removal of auditors, etc., plus shortcomings in the procurement and appointment processes	Official data	FRC Sector-led bodies	NHS England NHS Improvement	Section 3.4.7
6	Number of Public Interest Reports	Official data	Sector-led bodies	NHS England NHS Improvement	Section 3.4.8
7	Local public bodies' satisfaction with audit services	Survey data; qualitative evidence	Evaluator will repeat survey	NHS England NHS Improvement	Section 3.4.10
8	Quality of audits performed	Official data	FRC	FRC DoH	Section 3.4.11
10	Local public bodies' views on composition of fees	Survey data; qualitative evidence	Evaluator will repeat survey	NHS England NHS Improvement	Section 3.4.3
11	Audit firms' views on fee levels	Qualitative evidence	Evaluator will repeat interviews	Evaluator will repeat interviews	Section 3.4.4
12	Audit firms' satisfaction with the regulatory regime	Qualitative evidence	Evaluator will repeat interviews	Evaluator will repeat interviews	Section 3.4.13
13	Number of NAO reports on local issues as well as existence of broader, sector-led data sources	Official data/qualitative evidence	Evaluator review of NAO/other sources (such as LGA etc.)	Evaluator review of NAO/other sources (such as LGA etc.)	Section 3.4.9
14	Meeting of statutory deadlines for audits	Official data	PSAA Sector led bodies	NHS England NHS Improvement	Section 3.4.12

Indicators for which there is currently no baseline data



















No	Indicator theme	Reason
9	Number of small local public bodies not complying with transparency standards	Too early, this information will only be available at a later point in time
15	Number of local public bodies that did not follow auditor panel recommendations	This process is not yet in place before this project will be concluded

FIGURE: REFORM OF LOCAL AUDIT ARRANGEMENTS - THEORY OF CHANGE DIAGRAM



Appendix G: Overview of survey results









Table: Summary descriptive statistics of the survey responses.

Local Public Bodies Survey					
Respondents:	169 displayed, 540 total	Status:	Open		
Launched Date:	10/21/2015	Closed Date:	11/19/2016		
1. LPBname					
Total Respondents					169
2. LPB_Category					
		Response Total	Response Percent	Points	Avg
Local authority		102	60%	n/a	n/a
National Health Service body		40	24%	n/a	n/a
Police bodies (including police and crime commissioner)		15	9%	n/a	n/a
Fire and rescue authority		10	6%	n/a	n/a
National park body		0	0%	n/a	n/a
Combined authority		0	0%	n/a	n/a
Other, please specify		2	1%	n/a	n/a
view					
Total Respondents					169
					100%
3. Role					
		Response Total	Response Percent	Points	Avg
Chief executive or equivalent		1	1%	n/a	n/a
Finance director		99	59%	n/a	n/a
Other senior management not covered in (a) or (b)		37	22%	n/a	n/a
Finance team staff member		23	14%	n/a	n/a
Other, please specify		9	5%	n/a	n/a
view					
Total Respondents					169
					100%
4. Main_Contact					
		Response Total	Response Percent	Points	Avg
Yes		140	83%	n/a	n/a
No		29	17%	n/a	n/a
Total Respondents					169
5. LPB_Revenue					
		Response Total	Response Percent	Points	Avg
Up to £6.5 million		1	1%	n/a	n/a
£6.5 million-£24.9 million		12	7%	n/a	n/a
£25 million - £49.9 million		18	11%	n/a	n/a
£50 million - £74.9 million		20	12%	n/a	n/a
£75 million - £100 million		12	7%	n/a	n/a
More than £100 million		106	63%	n/a	n/a
Total Respondents					169
					100%

6. Postcode									
							Total Respondents	169	
7. LPB_Auditor									
						Response Total	Response Percent	Points	Avg
Deloitte						6	4%	n/a	n/a
Ernst & Young						31	18%	n/a	n/a
Grant Thornton						64	38%	n/a	n/a
KPMG						48	28%	n/a	n/a
Mazars						5	3%	n/a	n/a
BDO						4	2%	n/a	n/a
PwC						11	7%	n/a	n/a
PKF Littlejohn						0	0%	n/a	n/a
Total Respondents							169	100%	
8. Auditor_Appointment_Year									
						Response Total	Response Percent	Points	Avg
Pre-2012						46	27%	n/a	n/a
2012						69	41%	n/a	n/a
2013						35	21%	n/a	n/a
2014						8	5%	n/a	n/a
2015						11	7%	n/a	n/a
Total Respondents							169	100%	
9. Audit_Satisfaction									
	Completely satisfied	Mostly satisfied	Partially satisfied	Not at all satisfied	Don't know	Response Total	Points	Avg	
The ease with which your audit firm can provide staff and capacity to conduct the audit in a timely manner?	27.11% (45)	48.8% (81)	19.28% (32)	3.01% (5)	1.81% (3)	166	n/a	n/a	
The ease with which you were able to get an earlier involvement of the auditor when preparing the accounts?	38.55% (64)	41.57% (69)	11.45% (19)	6.02% (10)	2.41% (4)	166	n/a	n/a	
The ease with which you are able to contact and communicate with your audit firm?	59.64% (99)	34.94% (58)	3.01% (5)	1.2% (2)	1.2% (2)	166	n/a	n/a	
The extent to which your last audit plan was tailored to focus on key risks and priorities faced by your organisation?	41.57% (69)	42.17% (70)	11.45% (19)	0.6% (1)	4.22% (7)	166	n/a	n/a	
The timeliness of reports?	36.75% (61)	44.58% (74)	13.25% (22)	2.41% (4)	3.01% (5)	166	n/a	n/a	
The practicality of report recommendations?	31.93% (53)	50% (83)	14.46% (24)	1.81% (3)	1.81% (3)	166	n/a	n/a	
The usefulness of reports?	28.31% (47)	51.81% (86)	15.66% (26)	2.41% (4)	1.81% (3)	166	n/a	n/a	
The impact of audit reports on the operation of your organisation?	24.7% (41)	50.6% (84)	16.87% (28)	3.61% (6)	4.22% (7)	166	n/a	n/a	
The extent to which external auditors place appropriate reliance on internal audit	32.53% (54)	40.36% (67)	17.47% (29)	4.82% (8)	4.82% (8)	166	n/a	n/a	
The effectiveness of your organisation in reducing the costs of external audits?	28.31% (47)	38.55% (64)	18.67% (31)	6.63% (11)	7.83% (13)	166	n/a	n/a	
Total Respondents							166		
(skipped this question)							3		
10. Audit_Fees									

	Yes, it was completely appropriate	It was acceptable	No, it was not appropriate	Don't know	Response Total	Points	Avg
'My initial audit fee was appropriate?'	24.55% (41)	68.86% (115)	4.79% (8)	1.8% (3)	167	n/a	n/a
Total Respondents					167		
(skipped this question)					2		
11. Do you agree with the following statement in relation to your most recent audit:							
	Yes	No	Don't know	Response Total	Points	Avg	
'Any revisions to the fee were clearly communicated and explained?'	83.23% (139)	5.99% (10)	10.78% (18)	167	n/a	n/a	
Total Respondents					167		
(skipped this question)					2		
12. Auditors_Actions_Approach							
				Response Total	Response Percent	Points	Avg
Provided advice/guidance/helped to address important issues				120	72%	n/a	n/a
Been a true 'critical friend'/developed a good working relationship with us				119	71%	n/a	n/a
Been good at communicating/keeping in touch				121	72%	n/a	n/a
Been available to discuss/listen to issues about the operation of this organisation				131	78%	n/a	n/a
Demonstrated good knowledge and understanding of this body				119	71%	n/a	n/a
Other, please specify				6	4%	n/a	n/a
view							
Total Respondents					167		
(skipped this question)					2		
13. Auditors_Actions_Focus							
				Response Total	Response Percent	Points	Avg
Helped improve our management arrangements				22	13%	n/a	n/a
Helped demonstrate/highlight best practice/share information from elsewhere				90	54%	n/a	n/a
Encouraged my organisation to prioritise/provided action plan				41	25%	n/a	n/a
Provided benchmarking/comparative data				32	19%	n/a	n/a
Given honest and constructive feedback on our performance				117	70%	n/a	n/a
Helped improve financial management and governance				70	42%	n/a	n/a
Other, please specify				4	2%	n/a	n/a
view							
Total Respondents					167		
(skipped this question)					2		
14. Changes_Wanted_Scale							
				Response Total	Response Percent	Points	Avg
More proportionate/risk							

auditors will be a valuable change for my organisation.'	12.5% (21)	23.21% (39)	33.33% (56)	16.67% (28)	13.1% (22)	1.19% (2)	168	n/a	n/a
'My organisation is well equipped to make an informed choice about its auditor'	25.6% (43)	33.93% (57)	19.64% (33)	14.88% (25)	5.36% (9)	0.6% (1)	168	n/a	n/a
							Total Respondents	168	
							(skipped this question)	1	
19. Disagreement_Reason									
							Total Respondents	59	
							(skipped this question)	110	
20. Next_Contract									
							Response Total	Response Percent	Points Avg
Going alone in appointing your auditor							18	11%	n/a n/a
Participating in a joint procurement exercise with other bodies							55	33%	n/a n/a
Taking advantage of a sector-led body if it was established							58	35%	n/a n/a
Undecided							37	22%	n/a n/a
							Total Respondents	168	100%
							(skipped this question)	1	
21. Expected_Changes									
							Response Total	Response Percent	Points Avg
Improve the quality of audit of your organisation (e.g. the usefulness of the work, quality of contact with the firm)							43	26%	n/a n/a
Make no difference							87	52%	n/a n/a
Lead to a decline in the quality of the audit of your organisation							6	4%	n/a n/a
Not sure/ don't know							32	19%	n/a n/a
							Total Respondents	168	100%
							(skipped this question)	1	
22. Changes_Fees									
							Response Total	Response Percent	Points Avg
Lead to the audit fee charged by your auditor to your organisation going down							44	26%	n/a n/a
Make no difference to the audit fee charged by your auditor to your organisation							34	20%	n/a n/a
Lead to the audit fee charged by your auditor to your organisation going up							42	25%	n/a n/a
Not sure/ don't know							48	29%	n/a n/a
							Total Respondents	168	100%
							(skipped this question)	1	
23. Information_Dissemination									
							Response Total	Response Percent	Points Avg
Press conference							24	14%	n/a n/a
Announcements on own billboard							5	3%	n/a n/a

Announcements on own website		150	89%	n/a	n/a
Social media		74	44%	n/a	n/a
Email newsletter		31	18%	n/a	n/a
Handouts/flyers/printed newsletter		62	37%	n/a	n/a
Newspaper announcements		68	40%	n/a	n/a
Radio announcements		33	20%	n/a	n/a
Public hearings		45	27%	n/a	n/a
Other, please specify		40	24%	n/a	n/a
view					
Total Respondents		169			
24. In the last financial year (2014-15), how many (if any) objections to accounts have there been from electors?					
					Response Average
					0.07
Total Respondents					169
25. Final thoughts					
Total Respondents					49
(skipped this question)					120