

Annex 5 – Potential impact of recommendations made by other reviews of audit

In the past three years, three independent reviews have been published on elements of the statutory audit framework. Whilst the Kingman Review made specific recommendations regarding the local audit framework, the CMA Study and the Brydon Review were solely focussed on the audit of Public Interest Entities (listed companies or entities with listed debt). In addition, BEIS ministers have yet to decide whether/how to take forward all recommendations made by these reviews.

Given that local authority audit is delivered by assurance practices that undertake both public and private sector audits and conducted in accordance with a common set of quality standards, some of the recommendations made by these reviews may be relevant to the future of local audit.

This Appendix lists relevant recommendations made by all three reports and comments on how this Review has addressed them and/or how they may impact on the future of local authority audit.

Independent Review of the Financial Reporting Council (Kingman Review) – Dec 2018 https://www.gov.uk/government/publications/financial-reporting-council-review-2018	
Recommendation (local authority audit only)	Review Conclusions
<p>Recommendation 76: The Review recommends that the arrangements for local audit need to be fundamentally rethought to ensure that they:</p> <ul style="list-style-type: none"> • Deliver robust assessment and scrutiny of the quality of all local audit work, with individual reports shared with audit committees and published; • Establish a more appropriate threshold for enforcement action; and, • Bring together in one place all the relevant responsibilities, so a single regulatory body can take an overview. 	<p>This Review concurs with and has expanded on this recommendation.</p>
<p>Recommendation 77: Such a role (regarding local audit) could be taken on by the FRC or its successor body, but the Review recommends that it would be much better undertaken by a separate body that has (or could develop) a deeper expertise in the local audit world. That body should have a different and much more focused remit than the former Audit Commission. It should have a clear objective to secure quality, and should set the relevant standards, inspect the quality of relevant audit work and oversee the relevant</p>	<p>This Review concurs with and has expanded on this recommendation.</p> <p>This Review has considered whether the FRC would be an appropriate body to take on this role but has concluded that the regulator of local audit would be better as a separate body, that could focus on developing a deep expertise in local audit and which embraces the audit process from beginning to end, by including procurement and sector-wide reporting as well as quality.</p>

<p>professional bodies. It should also take on responsibility for appointing auditors for local bodies and agreeing fees.</p>	
<p>Recommendation 78: In the same spirit, the Government should review whether the arrangements now in place for other public sector audits, such as Foundation Trusts, are genuinely robust and effective. It is very unlikely that they are.</p>	<p>The audit of public sector bodies other than those classified as local authorities is outside the scope of this Review.</p>
<p>Recommendation 79: Just as the Review recommends public disclosure of AQR findings and gradings in relation to the private sector, the Review recommends that the new regulator's individual AQR reviews in relation to the NAO should be shared with the relevant audit committee and Parliament, and should be published.</p>	<p>This Review concurs with this recommendation.</p> <p>The Review recommends that the new regulator has a specific remit to publish the results of its audit quality reviews and be required to share them with Parliament.</p>
<p>Recommendation 82: The Review also recommends that responsibility for the local audit "Code of Audit Practice" should be moved to the same body that monitors the quality of local audit work.</p>	<p>This Review concurs with this recommendation.</p>

<p>Competition and Markets Authority: Statutory Audit Services Market Study - Apr 2019 https://assets.publishing.service.gov.uk/media/5d03667d40f0b609ad3158c3/audit_final_report_02.pdf</p>	
<p>Recommendation</p>	<p>Review conclusions</p>
<p>Robust regulatory oversight of the committees that run the selection process for audited companies, and oversee the audit, to make them more accountable and ensure that they prioritise quality.</p>	<p>This Review recommends that a new local audit regulator be responsible for procuring audit services for the sector and overseeing the work of those auditors with a specific remit to prioritise quality.</p>
<p>Mandatory joint audit, to increase the capacity of challenger firms, to increase choice in the market and thereby drive up audit quality.</p>	<p>The number of small number of firms active in the local authority audit market is of concern. However, audit practitioners and local authorities do not believe that joint audit is an appropriate solution for local government bodies.</p>

	<p>The Review recommends that the new regulator have a specific mandate to increase the number of practitioners in the local authority audit market through more active market management and that the statutory barriers to entry for new firms are removed.</p>
<p>An operational split between the Big Four's audit and non-audit businesses, to ensure maximum focus on audit quality.</p>	<p>CMA's declared aim in making this proposal is to enhance audit quality and end the practice of audit fees being subsidised by non-audit work.</p> <p>If this split does occur and the CMA's assertion that a subsidy does exist is proved true, then audit fees may go up across all sectors including local government.</p>
<p>A five-year review of progress by the regulator.</p>	<p>The Review recommends that the new regulator be overseen by an advisory committee comprising representatives of all key stakeholders and that it will be responsible for reporting on the effectiveness of its activities both to the panel and to Parliament.</p> <p>It will also be subject to triennial reviews as part of standard central government processes.</p>

Assess, Assure, Inform: improving audit quality and effectiveness (Brydon Review) - Dec 2019

<https://www.gov.uk/government/publications/the-quality-and-effectiveness-of-audit-independent-review>

<p>That the Audit, Reporting and Governance Authority (ARGA) together with auditors and the Plain English Campaign produce an appropriately concise guide to audit, explaining clearly what the different elements of an audit report mean as redefined in this Report, and what, just as importantly, they do not mean.</p>	<p>This Review believes that a concise plain-English guide to audit would be as valuable a reference to local authority audit as it is to public interest entity audit.</p>
<p>That auditing should provide information that is useful to present and potential investors, lenders, creditors and other users in making rational investment, credit and other decisions and assessments about the company.</p>	<p>The stakeholders in local government are different. However, this Review agrees that the purpose of an audit is to provide useful information that enables key stakeholders to make decisions and assessments about an entity. The recommendations about extending the scope of the value for money opinion and requiring the auditor to present it to</p>

	<p>full council aim to achieve this for local authorities.</p>
<p>That auditors should be free to include original information, materially useful to a wide range of users, in their audit report and at the AGM, and not be confined to commenting on that which has already been stated by directors.</p>	<p>The changes that the new Audit Code makes to the value for money opinion along with the further enhancements to that opinion recommended by this review should require the auditor to include original information in their reports.</p>
<p>That ARGA acts as the midwife to create a new profession of corporate auditing, establishing the necessary professional body, to encompass today's auditors and others with appropriate education and authorisation. ARGA would be the statutory supervisory body for that profession.</p>	<p>This recommendation has the potential to have a significant impact on the sustainability of the local authority and indeed the wider public sector audit market.</p> <p>Depending on how this recommendation is developed, Government and the local authority audit regulator may need to consider whether the proposed corporate audit profession would continue to generate skills that are transferrable for public sector audit. If not, and it develops as suggested by Brydon, there is a risk that local audit market could come under even more stress. If skills are transferrable, consideration will need to be given to how to ensure that members of the new corporate audit profession retain the skills, knowledge and expertise to deliver high quality local authority audits.</p>
<p>That an auditor's authorisation to carry out audits in particular areas of activity should flow from tailored qualifications which they have achieved.</p>	<p>This recommendation aligns to the Review recommendation that the current procedures to accredit firms and KAPs to carry out local authority audits be replaced by a qualification based on accredited training. Consideration should be given as to whether the local authority audit accredited training be treated as a tailored qualification as suggested by the Brydon Review.</p>

<p>That the Principles of Corporate Auditing should be established to form an overarching framework governing the behaviour of corporate auditors, and that standards and rules should sit within this framework.</p>	<p>The Regulator recommended by this review will need to consider whether the Principles of Corporate Auditing should also apply to audits under its remit, and if so whether they should be adapted.</p> <p>When making this assessment, the key considerations should include quality and market sustainability.</p>
<p>That the development of a specific auditor qualification, including education and training, should become a high priority for ARGA over the coming years.</p>	<p>If public sector audit remains part of a wider corporate audit profession, consideration will need to be given as to how to integrate local authority audit training into the ARGA led audit qualification.</p>
<p>That ARGA develops an agreed definition of professional judgment which builds on ISA(UK) 200.</p>	<p>Once developed, this definition is likely to apply equally to audits in all sectors.</p>
<p>That if the auditor considers there are other risks of similar or greater significance to those reported by the directors, based on its knowledge of the company, the auditor should report this fact.</p>	<p>Consideration will need to be given as to whether equivalent risk reporting should be introduced for local audit.</p> <p>The recommendation in this Review that the value for money opinion to be presented to the budget setting council or equivalent will facilitate such reporting.</p>
<p>That the Companies Act and ISA (UK) 700 be amended to replace “true and fair” with “present fairly, in all material respects”.</p>	<p>If this amendment is made for public interest entity audits, consideration will need to be given as to whether it should be replicated for local authority audits.</p>
<p>That the Government review the Companies Act to see if it could be improved to give more clarity as to what is meant by “adequate accounting records”. Given the complex requirements modern accounting creates, either through law or regulation, there should be an obligation for auditors to assess that the directors have maintained accounting records to a standard beyond the minimum level necessary for an audit to be performed. In doing so, the objective should be a High-Quality Audit as defined in this Report.</p>	<p>If the Companies Act is amended, consideration will need to be given as to whether this clarification should apply to the accounting records maintained by local authorities.</p>
<p>That ARGA promptly develop guidance for auditors around their responsibilities in relation to accounting records</p>	<p>The new local authority audit regulator will need to decide whether to implement or adapt this guidance.</p>

<p>That ARGA amends ISA (UK) 240 to make clear that it is the obligation of an auditor to endeavour to detect material fraud in all reasonable ways.</p>	<p>The FRC is consulting on an update to ISA (UK) 240, to start to address this recommendation.</p> <p>The new regulator will need to consider what application guidance will be required to help auditors of local authorities to apply the updated ISA.</p>
<p>That training in both forensic accounting and fraud awareness be part of the formal qualification and continuous learning process to practise as a financial statements auditor. In developing qualifications for auditors of other areas of activity, parallel training should be established.</p>	<p>If local audit remains part of the same profession as corporate audit, the local audit regulator will need to consider whether to mandate this training to practise as a local authority financial statements auditor.</p>
<p>That the auditor's report state explicitly the work performed to conclude whether the directors' statement regarding the actions they have taken to prevent and detect material fraud is appropriate. Furthermore, the auditors should state what steps they have taken to assess the effectiveness of the relevant controls and to detect any such fraud.</p>	<p>If this becomes mandated practice in corporate audit, the local audit regulator will need to consider the extent to which it is applicable for local authority audit.</p>
<p>That there should be an obligation on the auditors to report to both the audit committee and the shareholders on the extent to which their work has been influenced and informed (or not) by any external signals which might imply enhanced risk in the company whose financial statements are being audited.</p> <p>That ARGA should develop a menu of possible signals [regarding enhanced risk] and the auditors should report against the relevant parts of that menu.</p>	<p>The menu of enhanced signals developed by ARGA may or may not be applicable to local authority audit.</p> <p>If a menu of external signals is developed by ARGA and adopted for local authority audit, Government and the local authority audit regulator will need to give consideration as to whether something similar would be beneficial for local authority auditors.</p>
<p>That the auditor explain in each of the two succeeding audit reports what procedures have been undertaken and what conclusions reached in relation to those matters [KAMs or identified deficiencies]; the auditor should also highlight what actions have been taken by the company in response to deficiencies identified in the prior year's audit.</p>	<p>Consideration will need to be given as to whether this recommendation should be replicated for local authority audits.</p>
<p>That, in the audit report, auditors should explain the reasons for the necessity and basis of any sampling techniques used in conducting the audit.</p>	<p>Consideration will need to be given as to whether this recommendation should be replicated for local authority audits.</p>

<p>That individual statutory audit reports detail the number of hours spent in conducting the audit by grade of auditor.</p>	<p>Consideration will need to be given as to whether this recommendation should be replicated for local authority audits.</p>
<p>That audit committee minutes be published with a time-lag of 12-18 months and with approved redactions.</p>	<p>The minutes of audit committees or equivalent in local authorities are already published, typically with a lag of less than a month.</p>