



<b>AUDIT AND GOVERNANCE COMMITTEE</b>	<b>AGENDA ITEM No: 14</b>
<b>27<sup>th</sup> September 2019</b>	<b>PUBLIC REPORT</b>

## **NATIONAL AUDIT OFFICE CONSULTATION ON CHANGES TO THE CODE OF AUDIT PRACTICE**

### **1.0 PURPOSE**

- 1.1 To provide the Committee with an overview of the proposed changes to the Code of Audit Practice.

<b><u>DECISION REQUIRED</u></b>	
<b>Lead Officer:</b>	<b>Robert Emery (Chief Accountant)</b>
The Audit and Governance Committee is recommended to note the proposed changes to the code of audit practice, and the potential impact on reporting to the Committee for local audit work.	

### **2.0 BACKGROUND**

- 2.1 The Code of Audit Practice is a key document which sets out the principles which govern how local auditors in England meet their responsibilities when auditing Local Authorities. The Code must be reviewed at least every five years and the deadline for the new Code to come into force is 1<sup>st</sup> April 2020.
- 2.2 The National Audit Office (NAO) have completed phase one of the consultation on changes to the code, including key stakeholders such as Local Authorities, audit firms, NHS bodies and Central Government.
- 2.3 Based on the responses received a draft of the revised Code has been published and the period for phase two of the consultation, on the published draft, lasts until the 22<sup>nd</sup> November 2019.

### **3.0 SUMMARY OF PROPOSED CHANGES**

- 3.1 As the Code covers all types of Local Authority, and the NHS, this report focusses on the changes which have an impact on the Combined Authority; a full list of changes, and the full text of the draft Code, can be found on the NAO's website as linked to in the source documentation table at the end of this report.

## **Value for Money**

- 3.2 While the responsibility held by auditors of Local Authorities in respect of Value for Money (VfM) has not changed, that is to “*satisfy themselves that the audited body has made proper arrangements for securing VfM in its use of resources*”, specific reporting criteria have been introduced: financial sustainability, governance, and improving economy, efficiency and effectiveness.
- 3.3 For each of these criteria, there will be statutory guidance which sets out the procedures which auditors must undertake, and the auditor’s report must include a commentary on each criteria. The NAO have indicated that this change is not expected to increase the work required by local auditors but instead to extract more value from, and maximise the impact of, work already being undertaken. This should result in the 2019-20 auditors report providing a greater insight into the VfM arrangements in place at the Combined Authority.
- 3.4 The draft Code introduces the expectation that, where work identifies significant weaknesses in arrangements, the auditor will issue a recommendation to the body, setting out the auditor’s judgements clearly along with a summary of the evidence on which those judgements are based. The auditor should also explain the impact the judgement has on the body itself and set out clearly the actions the body should take in response. The draft Code also expects that, when they identify significant weaknesses in arrangements, the auditor considers whether to make their recommendation immediately, rather than wait until the end of the audit. This gives the Committee assurance that, were a significant control weakness be identified during the year, the auditors would not have to wait to complete an annual audit to report their findings.

## **Audit Reporting**

- 3.5 The proposed revised Code specifies that to maximise clarity, and value, for the public the auditor’s reporting will consist of two elements: The report on the financial statements, which covers only the work undertaken on the statements, and the auditor’s annual report.
- 3.6 The revised Code maintains the clear expectation that local auditors will complete their work and issue their opinion on the financial statements in time to allow local public bodies to meet their statutory deadlines for publication of audited accounts. This is not a change from the previous Code and, 40% of Local Authority’s 2018-19 accounts were not audited in time for the statutory deadline, however a separate review of local audit arrangements is being undertaken by MHCLG, led by Sir Tony Redmond and, given the delays experienced in the 2018-19 audit, the Combined Authority will be engaging with this.
- 3.7 The annual report should cover all audit work undertaken throughout the year and include the commentary on the specific VfM arrangements as set out in 3.2 and 3.3. The report will be intended to provide a clear, readily understandable commentary on the auditor’s findings and highlight any issues that the auditor wishes to draw to the attention of the body or the wider public. The auditor’s annual report should include details of any recommendations issued during the course of the year to ensure that all recommendations made by the auditor are accessible and reported publicly.

- 3.8 The annual report does not have to be published alongside the report on financial statements, but must be published by the 30<sup>th</sup> September following the end of the financial year.

### **General**

- 3.9 The expectation that audit firms need to ensure that their teams have the necessary skills and knowledge of the relevant financial reporting and regulatory frameworks to enable them to deliver their audit work has been clarified, this should ensure that the auditors assigned to the Combined Authority's audit are well versed in Local Authority audit, rather than only having experience in company auditing.
- 3.10 The NAO have also clarified expectations that their reporting to, and communications with, Local Authorities, and the wider public, are effective and transparent – that language should be chosen to ensure reader comprehension reflecting that the auditor's report is for the benefit of the public as well as the Local Authority.
- 3.11 The Code is based on generally accepted auditing standards however some sectors require auditors to report their findings in more detail than is required by GAAP, this is known as enhanced auditor reporting. While this is not currently required for Local Authorities, the NAO observed that this is becoming more widespread and have thus updated the Code to allow for this to come forward in future. If enhanced auditor reporting is put in place for Local Authorities a report will be presented to the Audit and Governance Committee with further details.
- 3.12 The draft Code emphasises the need for auditors to consider the impact of exercising their powers in relation to objections to the draft accounts and the issuing of an advisory notice, including proportionality, to what extent the issue is already known to the public and whether it is in the public interest for the auditor to publish their independent view on the matter. As there were no objections to the Combined Authorities accounts, we would not expect this change to have an impact.

## **4.0 SUMMARY**

- 4.1 While the revised Code does not represent a fundamental change in the approach the Authority's auditors will take, their annual reporting to the Audit and Governance Committee will now take the form of two separate reports, with a greater focus on value for money.
- 4.2 Officers are supportive of the proposed changes and welcome the greater focus on value for money, the increased requirement for specific Local Government expertise, and the re-assertion of the clear expectation that auditors will issue their opinion in line with the statutory timescales required of Local Authorities
- 4.3 We would welcome any steer from the Committee in relation to the Combined Authority's feedback to the proposed draft.

## **5.0 FINANCIAL IMPLICATIONS**

- 5.1 The NAO has identified that any change to the work of local auditors, particularly the increased requirement for specific expertise, may impact the fee required to fund auditor's work and are working with key stakeholders to understand the potential

impact of the proposed changes.

## **6.0 LEGAL IMPLICATIONS**

6.1 There are no direct legal implications

## **10.0 EQUALITIES IMPLICATION**

10.1 None

<b><u>Source Documents</u></b>	<b><u>Location</u></b>
<b>National Audit Office Code of Audit Practice Consultation documentation</b>	<a href="https://www.nao.org.uk/code-audit-practice/code-of-audit-practice-consultation/#">https://www.nao.org.uk/code-audit-practice/code-of-audit-practice-consultation/#</a>