

Quality review programme

Annual report 2010

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

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On Friday 13 August, the DCLG announced that the Audit Commission will be abolished in 2012/13. This report was completed before that announcement. The messages in this report remain relevant.

Introduction

1 The Audit Commission appoints external auditors from either its own staff (the audit practice) or private firms of auditors,ⁱ to 900 principal local government, criminal justice and health bodies in England. The Commission also appoints external auditors to some 9,500 parish and town councils and other bodies such as internal drainage boards, referred to as smaller bodies in this report. These bodies are subject to a separate limited assurance audit regime by a mainly different group of audit suppliers.ⁱⁱ

2 Appointed auditors' responsibilities are set out in the Audit Commission Act 1998. They must carry out their work and exercise their powers in accordance with the Commission's statutory Code of Audit Practice (the Code).

3 The Commission assesses the quality of the work of its in-house audit practice and the firms to which it has let contracts (suppliers). We define audit quality as compliance with professional standards and our regulatory requirements. Our objectives are to:

- provide assurance the Commission's audit suppliers have put in place systems and processes to deliver audit work of an appropriate quality; and
- inform the audit appointments we make.

4 This report summarises the results of the quality review process for 2010 for our stakeholders, which include audited bodies, government departments, the wider accountancy and auditing profession, and other interested parties.

ⁱ Deloitte, Grant Thornton, KPMG, PKF and PricewaterhouseCoopers.

ⁱⁱ In addition to the audit practice these are Mazars, BDO, Clement Keys and Moore Stephens.

Background

5 There are two main strands to our monitoring. First, we report quarterly on suppliers' compliance with our regulatory requirements for delivering audits. Secondly, we apply our annual quality review programme (QRP), which assesses the quality of suppliers' work.

6 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 on a cyclical basis the quality of the firms' financial statement audits at a sample of Commission engagements.

7 We also commission the AIU to review the quality of the financial statements audits carried out by the Commission's own audit practice.

8 We place reliance on suppliers' own quality control and monitoring arrangements so far as possible, but also obtain independent assurance through a programme of reviews of specific aspects of auditors' work. In 2010 we carried out reviews of:

- auditors' value for money (VFM) conclusions;
- written reports to audited bodies;
- certification of claims and returns for grant-paying bodies; and
- limited assurance audits.

Regulatory requirements

9 We monitor whether auditors comply with our regulatory requirements. These include the target dates for issuing audit opinions on the financial statements and VFM conclusions; giving opinions on the whole of government account (WGA) returns; producing annual audit letters and sending us specified information and returns.

10 Mostly auditors met our target dates with only a few instances where there were delays, for reasons that were within the auditor's control.

QRP results

- 11** The risks of audit failure remain low and suppliers are:
- meeting the Commission's regulatory requirements; and
 - continuing to produce work to a good or acceptable standard.
- 12** However, there is scope for all suppliers to improve their work by:
- responding to the findings of the AIU's annual inspections;
 - improving the quality of evidence and documentation supporting their VFM conclusions;
 - ensuring greater consistency in the quality of written reports;
 - improving compliance with our specified housing and council tax benefits methodology; and
 - more timely completion of limited assurance audits.
- 13** The rest of this report summarises the results of our work on each of the main parts of the QRP.

Financial statements audit work

14 Auditors of listed companies have a statutory duty to produce an annual transparency report, giving information about the firm's governance and its arrangements for ensuring the quality of its work. All the firms in our regime are covered by this requirement. The Commission's audit practice complies with the requirement on a voluntary basis and publishes an annual quality report.

15 The AIU's public reports on the firms provide an objective reality check on the self-assessments included in the firms' transparency reports. The AIU's summary report on its inspections in 2008/09 of the work of the big four and 'other significant' audit firms concluded that 'the overall quality of audit work [is]... fundamentally sound'. The AIU was satisfied with the basis on which significant audit judgements were made on the individual audits it reviewed. It considered that audit procedures had been performed to a good or acceptable standard. However, the AIU identified certain areas at each major firm where improvements were in its view needed to enhance audit quality. (*AIU 2008/09 Audit Quality Inspections – An Overview* (December 2009)).

Value for money conclusions

16 Auditors are required by the statutory Code of Audit Practice to give a conclusion as to whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness (VFM) in its use of resources.

17 For each audit supplier we reviewed a sample of auditors' VFM conclusions. The aim of these reviews was to assess whether the evidence on the audit file was sufficient to support the auditor's judgements.

18 Our overall conclusion is the evidence on the audit files was sufficient to support auditors' VFM conclusions. However, there is scope for:

- clearer recording and cross-referencing of the evidence supporting auditor's judgements; and
- documenting more fully the thought process in reaching judgements.

Audit reporting

19 This part of the QRP reflects the importance we attach to good-quality report writing, which is essential if audit work is to have impact and secure worthwhile change. We asked a group of readers (Commission Board members, the Chief Executive, Managing Directors and other senior staff) to assess a selection of different types of audit report. We reviewed a sample of audit plans, governance reports, annual audit letters and public interest reports. We asked readers to address whether the reports were clear, concise and likely to have impact and to score the overall presentation of the reports.

20 While most reports were fit for purpose and the quality of written reports has improved, all suppliers need to secure greater consistency in this area.

Certification of claims and returns for grant-paying bodies

21 Government departments, agencies and the European Commission pay billions of pounds of grants and subsidies each year to local authorities. Grant-paying bodies often ask for certification by a suitably qualified auditor of the claims and returns sent to them. Certification work is not an audit but a different type of assurance engagement. This involves applying prescribed tests that are designed to give reasonable assurance that claims and returns are fairly stated and agree with specified terms and conditions.

22 Over the past year we have taken action to improve the quality of certification work. We published an auditor briefing '*Raising the Profile of Certification Work*' (December 2009) and introduced a new requirement for auditors to report yearly on the results of certification work to those charged with governance.

23 For each supplier we reviewed a sample of grant claims work to assess whether the auditor had followed properly our prescribed tests. We found good practice and high levels of compliance with our requirements at all suppliers. But we did find scope for improving compliance with our housing and council tax benefits methodology.

Limited assurance audit regime

24 The limited assurance audit regime for small bodies is running as intended. All suppliers have developed internal quality monitoring that is robust enough for us to place reliance on.

25 The date for publication by audited bodies of their audited accounts has progressively moved forward. For 2008/09 the specified date was 30 September 2009, compared to 31 October in 2008. There is scope for all suppliers to improve the timeliness of completing these audits by the target date.

Responses to QRP findings

26 All audit suppliers have made arrangements to report the QRP findings to a suitable top management group. Action plans are in place to address both organisation-wide and audit team issues. We will follow up significant recommendations as part of next year's QRP.

27 Next year we propose to:

- rely more on suppliers' systems for ensuring compliance with our regulatory requirements;
- continue to rely on the work of the AIU; and
- target risk-based file inspections on a sample of VFM conclusions and certification work.

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This document is available on our website.

If you would like to know more about the Commission's QRP or would like to discuss our auditors' or the Commission's work, please write to us at the following address:

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