

CIPFA Better Governance Forum

The Draft Local Audit Bill - comparison to the key statements in the published Government Response (January)

In January 2012 the Government published its response to the consultation carried out in 2011 on the future of local public audit. DCLG also held regional engagement workshops to explore key issues with local government practitioners. The draft Bill was published on 6 July for further consultation, with a closing date of 31 August.

The aim of this analysis is to trace how the key areas outlined by the Government in its response published in January 2012 have been developed into the draft Bill. The draft Bill was published along with explanatory notes and a policy overview to explain the Government's intentions in the draft Bill.

The analysis does not aim to be a comprehensive summary of the entire draft Bill but features the main areas of interest. Some clauses vary according to organisation type and this analysis focuses on the main provisions rather than listing all variations in application.

As a general comment the key principles have not significantly changed since the Government's response in January. It should also be noted that a significant number of areas will be subject to further regulations from the Secretary of State. Until these are published the detailed application of the new legislation may not be fully apparent.

This briefing has been produced by the CIPFA Better Governance Forum to help inform its subscribers in their reading of the draft Bill. It does not constitute any part of CIPFA's formal response to the consultation.

If you have any queries arising from this analysis please contact Diana.Melville@cipfa.org.uk

| Key Area | Government Response | Draft Bill | Points to note |
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| Regulation | | | |
| Code of Practice | <p>Government intention was for the National Audit Office to produce the Code of Practice.</p> <p>NAO provide annual and in-year guidance to achieve consistency.</p> <p>Guidance should be principles based and not prescriptive.</p> | <p>The Comptroller & Auditor General will prepare a code or codes if more than 1 is required for different bodies.</p> <p>There will be a requirement to consult representatives of the bodies being audited, the auditors and professional accountancy bodies.</p> <p>A new code must be produced at least once every 5 years.</p> | |
| Regulation of auditors | <p>The Financial Reporting Council to be the overall regulator.</p> <p>The Secretary of State to have powers to authorise professional accountancy bodies to act as Recognised Supervisory Bodies for local public audit. In practice, the Secretary of State will delegate these powers to the Financial Reporting Council.</p> <p>For monitoring and enforcement the response recommended that Responsible Supervisory Bodies would be mainly responsible. With Audit Inspection Unit of FRC playing a role for bodies of Significant Public Interest.</p> <p>All eligible local public auditors will be placed on a register, which will be kept by the Recognised Supervisory Bodies.</p> <p>No specific regulations mentioned to ensure that firms registered for local audit work would meet specific criteria e.g. experience.</p> | <p>The Draft Bill provides for the delegation of functions from the Secretary of State to a new or existing body. Schedule 4 of the Bill requires an annual report on the discharge of its functions to be made to the Secretary of state and published to Parliament.</p> <p>Using their delegated powers the FRC will be able to authorise professional accountancy bodies to be recognised supervisory bodies in respect of local public audit.</p> <p>The draft Bill creates an offence of acting as a local auditor when not eligible to do so.</p> <p>The draft Bill sets out independence requirements so that an officer or member of an authority cannot be appointed as its auditor. This also applies to holders of corporations sole such as Police & Crime Commissioners. Partners and employees of officers & members are also proscribed from acting as</p> | <p>The overview of the Bill makes plain the Government's intentions to delegate overall regulation to the Financial Reporting Council.</p> <p>Auditors need to be seen as independent so the content of the regulations will be interesting.</p> <p>In particular will the independence requirement apply solely to the nominated auditor responsible for the audit</p> |

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| | | <p>auditor. The Secretary of State will have powers to make regulations that may define other 'connections' that could be deemed to compromise independence.</p> <p>The Register of those individuals and firms eligible to act as local auditors will be based on the possession of a recognised qualification. Schedule 3 to the Bill outlines the requirements on the Recognised Supervisory Bodies to ensure that those registered are competent to undertake local audit and are fit and proper persons to do so. The Bill does allow for the register to contain other information - to be specified in regulations. The Secretary of State will also have power to make regulations over the disclosure of controls over the quality and independence of local audit work.</p> <p>Arrangements for monitoring and enforcement are set out in Schedule 3 also. These include an inspection at least once every 6 years of their local audit work. An annual report on inspections is to be provided to the Secretary of State. Inspections of a firm with a quality assurance policy will cover all the eligible auditors employed by that firm.</p> <p>The policy overview accompanying the bill states that the FRC will have responsibility for monitoring the quality of 'major audits'. Which bodies will have their audits defined as 'major audits' will be defined by regulations by the Secretary of State.</p> | <p>or will it also apply to all audit staff engaged on the contract?</p> <p>Apart from ensuring professional competence through qualification and professional membership, Recognised Supervisory Bodies will need to have regard to the regulations.</p> <p>The definition of what constitutes a major audit is one of the specific questions in the consultation.</p> |
| Scope of the audit | <p>The Government proposed keeping the current requirements for auditors to satisfy themselves that:-</p> <ul style="list-style-type: none"> the accounts have been prepared in accordance with the necessary directions or regulations and comply | <p>The draft Bill stipulates the continuation of the following 3 requirements of the audit scope.</p> <ul style="list-style-type: none"> It requires the auditor to be satisfied that the relevant authority's statement of accounts have been prepared in accordance with the relevant legislative requirements; | <p>The draft bill does not show any change to the Government's thinking about the scope of the audit but it does not set out how the assessment of value for money in a 'risk based and proportionate approach' will be</p> |

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| | <p>with relevant statutory requirements;</p> <ul style="list-style-type: none"> proper practices have been observed in the compilation of the accounts; and the body has made proper arrangements for securing economy efficiency and effectiveness (value for money) in its use of resources. <p>The Government commented that it considered that the value for money component of the audit could be delivered in a more risk based and proportionate way. This would have the potential for a consequent decrease or increase on the level of audit work some local public bodies might see as a result. This issue was explored further by the National Audit Office at the Engagement Workshops hosted by DCLG in the Spring.</p> | <ul style="list-style-type: none"> that proper practices have been observed in the compilation of the statement of accounts; and that the relevant authority has made proper arrangements for securing economy, efficiency and effectiveness in the use of its resources. <p>In the Policy Overview published alongside the draft Bill the Government states that the National Audit Office will set out more detailed requirements within the code of audit practice and related guidance.</p> | <p>achieved in practice.</p> <p>Clearly every public body should be ensuring that it does have proper arrangements for securing value for money, the issue is how the auditors will be able to satisfy themselves that this is the case in order to give an opinion in accordance with the code.</p> <p>This is an area where further detail will emerge as the National Audit Office start to prepare the code.</p> |
| Commissioning Local Audit Services | | | |
| Duty to appoint, rotation of auditors and failure to appoint | <p>The Government proposed that all local public bodies with income/expenditure over a threshold (currently £6.5m) will be under a duty to appoint an auditor from the register of local auditors.</p> <p>The original consultation included a proposal to limit the appointment to a maximum of 10 years. This did receive majority support although some concerns were raised that it would be a barrier to new entrants. The Government therefore proposed not to introduce this requirement.</p> <p>The proposals suggested that authorities</p> | <p>The appointment must be made by 31 December the preceding year to which the audit relates.</p> <p>The appointment may be for more than 1 year but a further appointment must be made at least once every 5 years. The authority may re-appoint the auditor.</p> <p>The relevant authority must publish a notice within</p> | <p>The FRC is currently consulting on changes to the UK Code of Corporate Governance. This includes a new requirement that FTSE350 companies should put the external audit contract out to tender at least every 10 years.</p> <p>The merits and issues around the rotation of auditors is</p> |

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| | <p>should publish details of their appointment of an auditor and also the recommendations of the panel. If the local public body did not follow the advice of the Panel in making its appointment, it would be required to publish on its website a statement setting out the reasons why it had chosen not to follow that advice.</p> <p>The Government proposed that an authority would be required to advise the Secretary of State where they have failed to appoint an auditor and the Secretary of State would then have powers to either direct them to make the appointment or to appoint an auditor for them. The response also suggested that there might be a sanction for failing to appoint.</p> | <p>28 days of the appointment that it has made the appointment, identifies the appointed auditor, the advice given by the Panel and reasons if the authority has not followed the advice. The notice is to be published on the website.</p> <p>The draft Bill gives the Secretary of State the power to direct and authority to appoint or to make an appointment if the body has failed to do so.</p> | <p>currently a hot topic so it will be worth following developments in this area as changes in the UK code may influence future legislation.</p> <p>There is no provision for a sanction in the bill.</p> |
| <p>Auditor Panels - role</p> | <p>The Government proposed that authorities would appoint their auditor through Full Council taking into account the advice of an Auditor Appointment Panel.</p> <p>The Government proposal was to provide for a limited set of functions on the Independent Audit Appointment Panel in legislation, around advising on auditor appointment, independence, removal and resignation, and in relation to public interest reports.</p> <p>The Government also proposed to allow flexibility for local public bodies to suit their own circumstances, and facilitate joint working and joint commissioning between local public bodies.</p> | <p>The Bill requires each relevant authority to have an auditor panel to exercise the functions of an auditor panel under the Bill.</p> <p>The functions of the Panel are:</p> <ul style="list-style-type: none"> • To advise the authority on the maintenance of an independent relationship with its auditor; • To advise the authority on the selection and appointment of an auditor to audit its accounts. <p>Both of these duties must be carried out when requested by the authority or if the Panel itself chooses to make the advice.</p> <p>In addition the Panel can be requested by the auditor to advise on the authority's proposal to enter into a liability limitation agreement or a proposal to make a public interest report.</p> <p>Advice from the Panel should be published locally.</p> | <p>Guidance / regulations will support their interpretation of the statutory functions and also determine how they can be combined with other functions required by the authority.</p> <p>The bill does not specifically refer to the role of the panel in the removal or resignation of the auditor but this may fall within the broad responsibility to advise on the maintenance of an independent relationship.</p> <p>The policy overview states that the draft Bill does not replicate the Company's Act requirements around the rotation of the key</p> |

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| | | <p>The Secretary of State will have powers to make regulations on the role of the Panels and authorities and Panels will be required to follow it.</p> | <p>audit partner or the provision for the auditor to report on issues surrounding their independence to the body's audit committee. The Government envisage the Panel undertaking this role through its duty to advise on the maintenance of an independent relationship. Further details will be set out in regulations.</p> <p>The Bill allows a reasonable amount of flexibility in the use of Panels including joint arrangements. There are also minimum safeguards in the independence of its membership.</p> |
| <p>Auditor Panels – appointment & powers</p> | <p>The Government proposed that the Independent Audit Appointment Panel should be independently chaired, with a majority of independent members. Where the body already has an independent audit committee, they may wish to use that committee to meet this requirement.</p> | <p>A suitable Auditor Panel can be appointed by an authority or appointed jointly with other authorities. It may also be a committee of the authority if it complies with the requirements of the Panel. It may also be a committee of another authority if that committee fulfils the requirements of a Panel.</p> <p>The Panel must have a majority of independent members and must be chaired by an independent member.</p> <p>The definition of independent is:</p> <ul style="list-style-type: none"> • not been a member or officer of the authority within the period of 5 years; • not at that time a relative or close friend of a member or officer of the authority; <p>Further details of the makeup of the panel and provisions for appointment, term of office, remuneration etc. may be set out in regulations by</p> | <p>In taking forward the establishment of a Panel then the authority will need to ensure not just compliance with the legislation and any subsequent regulations but also how to ensure the Panel is effective in fulfilling its functions and how it will operate alongside other governance arrangements – notably existing audit committee arrangements. Another factor will be whether the Panel is seen to be sufficiently independent by the public and stakeholders.</p> |

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| | | <p>the Secretary of State.</p> <p>The draft Bill also sets out some of the powers of the panel. These include:</p> <ul style="list-style-type: none"> • The authority must provide to the panel any documents or information the panel requires to exercise its functions. • The panel can require any member or officer to come to its meetings to answer questions • The member or officer should comply with the panel requirement except where they would be entitled to refuse to answer in a court of law. | |
| <p>Resignation and removal of auditors</p> | <p>The government proposals for either the resignation or removal of the auditor were:</p> <ul style="list-style-type: none"> • Issue of 28 days' notice (by authority for removal or by auditor for resignation) to the other party and to the Panel. • Preparation of a written response which would also be sent to the Panel. • The Panel would have a role to investigate the response and in the case of proposed removal to advise the authority. • The resigning auditor's statement would be published on the website and the regulatory bodies informed. • Removal of auditors would require consideration of the Panel's comments and a decision by Full Council. • The decision would need to be published on the website. | <p>The draft Bill states that the Secretary of State may make regulations about the resignation or removal of the auditor.</p> <p>The regulations may cover the:</p> <ul style="list-style-type: none"> • The steps to be taken • Timescales • Role of the panel or for recognised Supervisory Body <p>The regulations will also cover steps that need to be taken before a new auditor is appointed.</p> | <p>More regulations are required to set out the detail of the process to follow.</p> <p>However, in the policy overview the Government does say in the case of resignation, the auditor would need to make a statement to the authority, the panel and its supervisory body. The authority would then need to publish its response to that statement.</p> <p>In respect of removal the authority would need to give the auditor and the panel the notice including a statement of reasons. The auditor's response would also be considered by the panel. The body's decision to terminate would be subject to the advice of the panel.</p> <p>As the bill does not contain full details it is not clear if the</p> |

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| | | | regulations will require the removal to be by Full Council as originally proposed. |
| Auditor Liability | The Government considers that auditor liability should be an issue to be dealt with in the contractual negotiations between the auditor and audited body. The Government will also consider the feasibility and necessity of a supporting statutory framework which could set out the process for agreeing liability limitation agreements. | The Secretary of State will make regulations to cover the terms of Liability Limitation Agreements and any agreement negotiated must comply with the regulations. A relevant authority must consult and take into account the views of its auditor panel before entering into an agreement. | Although the advice of the panel is to the authority, section 13.5 seems to suggest that only the auditor can request that the panel gives advice in respect of the LLA. |
| Public Reporting & Transparency | | | |
| Public Interest Reporting and other recommendations | Government intends to retain the duty for auditors of all local public bodies to undertake Public Interest Reporting under the new framework. | <p>Key points to note are:</p> <ul style="list-style-type: none"> • The auditor must consult the auditor panel before making the public interest report. • Auditors making public interest reports on connected entities will supply them to the 'parent' body for consideration. • The auditor will need to send a copy of the report to the Secretary of State. • A new requirement to publish the report on the website along with details of a meeting held to consider the report. • A copy of the public interest report (PIR) must be sent to the audit panel. Note this responsibility lies with the body receiving the report not the auditor making it. • The audited body must advise the auditor of decisions taken in relation to the report and also to publicise them. <p>Section 64 refers to written recommendations by the auditor following the completion of audit. Such recommendations have to be reported to the Secretary of State also and considered at a meeting of the authority within 1 month of the date of receipt.</p> | <p>Although the panel must be consulted by the auditor before issuing the PIR and the authority must inform the panel of the PIR, the panel itself does not have any decision making role in relation to the PIR or direction of action to take in response to the PIR.</p> <p>The Secretary of State has powers to make regulations in this area and this may provide some clarification of the auditor recommendations this clause</p> |

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| | | Clause 69 prevents the delegation of functions in relation to PIR or written auditor recommendations to an executive or other committee. | relates to. For example would it apply to all recommendations contained in the ISA260 report? |
| Non audit services | The Government considers that the current ethical standards provide sufficient safeguards for auditor independence. We therefore propose to enable auditors to provide non-audit services to the audited body, subject to adhering to the ethical standards produced by the Auditing Practices Board and gaining approval to undertake the work from the Independent Auditor Appointment Panel. | The draft Bill does not specifically mention non-audit services and appropriate safeguards. | Regulations to be issued by the Secretary of State may include guidance on non-audit services as part of the Panel's responsibility to advise on the maintenance of an independent relationship. |
| Public Interest Disclosure | The Government envisaged transferring the Audit Commission's PIDA responsibilities as designated persons to the appointed auditor and the panel. | | There is no mention of this in the draft Bill. This may come through in further bills or in other legislation. |
| Transparency and inspection of accounts | The Government proposed to retain the right to object to the accounts but to provide a power to give the auditor discretion to reject vexatious, repeated or frivolous objections. | The draft Bill retains the right to inspect the accounts and auditor reports in the form of a new duty on the local authority to make them available. During the audit any interested person has the right to inspect supporting accounting records and documents. A local elector will be able to raise objections to the account in relation to a matter that could lead to public interest disclosure or lead to an auditor notice. The local auditor can consider whether to take action in response to the objection but will have the power to not consider the objection if it is frivolous, vexatious or repeats an objection previously made | |

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| | | & considered by the auditor. | |
| Freedom of Information | Following on from its consultation the Government said it would not be including auditors within the remit of the FOIA. | There is no provision to include auditors within the remit of FOIA but in delegating powers to regulate the supervision of auditors the Secretary of State brings the delegated body within the remit of FOIA. | This would apply for powers delegated to the FRC. |
| Other functions of the Audit Commission | | | |
| Grant certification | The response document stated that 'Following the Audit Commission's closure, grant paying bodies for new grants will need to develop separate arrangements, either in the form of free-standing tripartite agreements (between the grant paying body, the payee and its auditor) or self-certification.' | There are no provisions in the draft Bill but the Government has repeated their intention to phase out existing certification requirements. | Where there is a need to procure external audit certification to meet the assurance requirements of a grant then this will need to be identified and procured as an external audit service. |
| National Fraud Initiative | The Government confirmed its support for the continuation of the NFI and stated it would develop proposals for delivery. | <p>The draft Bill transfers the Audit Commission's data-matching powers to the Secretary of State who will then delegate them to an operational provider. Three candidates are identified in the policy overview:</p> <ul style="list-style-type: none"> • National Fraud Authority • Department for Work & Pensions • Cabinet Office. <p>Local public bodies will continue to be required to provide data for data matching purposes through a new duty. The policy overview states that it will be up to individual bodies to follow up their matches.</p> <p>The Secretary of State will be required to draw up a code of data matching practice.</p> | <p>The draft Bill does not contain any sanctions for failure to follow up the data matches.</p> <p>Question 14 in the consultation response form asks for views on who the owners of the NFI should be.</p> |

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| <p>Inspections & national studies</p> | <p>The government response commented: ‘We consider that there is scope for rationalisation in the number of value for money studies published relating to the local public sector compared to the number previously undertaken. We would like to see a coherent and complementary programme of offerings across providers including the National Audit Office, central Government and the Local Government Association.’</p> | <p>The draft Bill contains an amendment to the Local Government Act 1999 giving the power to the Secretary of State to appoint an inspector for an inspection of compliance with best value duties. The policy overview comments ‘We envisage that this power would be rarely used, only where there are concerns about significant governance failure in a local authority.’</p> <p>Part 7 clause 93 amends the National Audit Act 1983 to provide a new power to the Comptroller and Auditor General to undertake studies regarding the economy, efficiency and effectiveness with which the English local government sector has used resources in undertaking its functions.</p> | <p>The explanatory notes say that the intention of thematic reviews across local authorities is to enhance the assurance work the NAO provides to Parliament and support learning across the sector.</p> |
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Additional matters:

Matters not included in the Government’s response document published in January but included in the draft Bill, include the following:

- Right of access to information. The draft Bill retains the right of auditors to access document and information, including rights of access to connected entities. It will be a criminal offence to prevent the local auditor from having access to any information required. Set out in Part 5 clauses 61-62.
- Auditor’s power to issue Advisory Notices & have an item of account declared unlawful. Auditors will retain the right to apply to the court if they believe an item in the accounts is unlawful. The auditor can also issue an advisory notice if the auditor thinks the body is making a decision or taking a course of action that is unlawful. Full details are in Part 5 clauses 76-80.

Key areas that will be covered by regulations from the Secretary of State:

- Role, make up and appointment of the auditor panel;
- Independence in the appointment of auditors;
- Resignation & removal of auditors;
- Liability Limitation Agreements
- Definition of ‘major audits’ for enhanced monitoring by the regulator;
- Public interest reports and auditor recommendations.