The role and responsibilities of external audit

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Appointment

- Appointed by the Audit Commission under a framework contract after consultation with Audited and Inspected Bodies
- Key statute is the Audit Commission Act 1998 (ACA 1998)
- Overriding principle is independence:
  - Limits on non-audit work
  - Avoidance of potential conflicts
  - Rotation of partner/manager every 5 years
  - Annual declarations (in the Audit Plan)
Responsibilities

• Main Code Audit
  – Independent auditor
  – Opinion on Accounts and on BVPP
  – Conclusion on adequacy of Value for Money arrangements

• Use of Resources Assessments – Key Lines of Enquiry (KLOE)

• Certification of grant claims
  – Agent of the Audit Commission and methodology is prescriptive
Responsibilities

• Special powers
  – report in the public interest, under the terms of Section 8, ACA 1998;
  – application for a declaration that an item of account is unlawful under Section 17, ACA 1998;
  – declaration on the recovery of an amount not accounted for under Section 18, ACA 1998;
  – issue of an advisory notice under Sections 19A to 19C, ACA 1998 (brought about by Section 91 of the Local Government Act 2000); and
  – application for judicial review under Section 24, ACA 1998.
What do auditors actually do?

- Our opinion is not an absolute statement – it’s a view:
  - *We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement*

- Do not aim to find every error or misstatement that might exist
What do auditors actually do?

• We adopt a risk-based approach:
  – Identify areas of risk
  – Determine which of those risks impact on our audit
  – Identify arrangements/controls the Council has in place to mitigate relevant risks
  – Assess the strength of those controls
  – Determine if there are any residual audit risks (i.e. risks not completely covered by controls)
The Code of Audit Practice

• Approved by Parliament at 5-yearly intervals
• Prescribes how auditors carry out their statutory functions
• Compliance with the Code is itself a statutory requirement
A New Audit Model (from 2005/06)

Audit of accounts (including review of SIC)

Risk-based, integrated audit

Use of Resources and Conclusion on VFM arrangements
VFM work under the new Code

• Stronger focus on corporate performance and financial management arrangements

• Positive conclusion whether audited body has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness (3Es), in its use of resources, accordance with criteria specified by the Audit Commission

• Reliance on work of other inspectorates
Use of Resources Assessments and KLOE

• “Key Lines of Enquiry” work is mandated by the Audit Commission
• Annual process that links to Direction of Travel
• 5 themes:
  – Financial Reporting (2 sub-themes)
  – Financial Management (3 sub-themes)
  – Financial Standing (no sub-themes – stand-alone)
  – Internal Control (3 sub-themes)
  – Value for Money (2 sub-themes)
• Scored 1 (inadequate) to 4 (performing strongly – i.e. exceptional)
• Some sub-elements weighted higher – e.g. accounts
Link between KLOE and VfM conclusion

- VfM conclusion has 12 criteria set by the Audit Commission:
  - 8 are based on KLOE assessments
  - 1 is based on assessment of “data quality” arrangements
  - 3 are based on the latest Audit Commission CPA Corporate Assessment, updated for recent knowledge

- Inadequate areas are reported as exceptions (i.e. “unqualified, except for . . .”)

- If things are really bad, could result in an “adverse” opinion
Audit outputs

• Audit reports/opinions/conclusions:
  – Financial statements “presents fairly” opinion
  – Value for money conclusion
  – Best Value Performance Plan opinion

• s.8 reports / s.11 recommendations
Audit outputs

• Annual Audit and Inspection Plan

• Accounts report to those charged with governance including matters to be reported under ISA260

• Use of resources reports:
  – Use of resources assessments (KLOE)
  – Data quality & BVPIs
  – Other risk based work

• Annual Audit and Inspection Letter
  (prepared and published by the Audit Commission)
Fees

• Annual fees and work programme document
  – Consultation with Audited and Inspected Bodies
  – Sets out scope of Code work for the year and any mandated work (e.g. KLOE)
  – Provides benchmarks of *likely* fee levels

• Actual fee based on the level of work required to address the audit risks identified from the risk based planning
Other issues

• Inspection
  – We do not carry out inspections
  – We do work very closely with the Audit Commission RM and his team

• Internal Audit
  – Our joint working approach seeks to minimise duplication of work – but the overall scope of Internal Audit’s work is for the Council to determine
  – Our review of Internal Audit is solely to:
    • Determine what we can or cannot rely on for opinion purposes
    • Feed in to KLOE assessments (particularly 4.2 re Internal Control)
  – Our review is not a review of effectiveness (as is now required by the very recently updated Accounts and Audit Regulations)
Other issues

• Fraud / corruption
  – It is *not* external audit’s role to seek out fraud or corruption
  – We do consider the strength of anti-fraud arrangements

• Levels of reserves
  – It is not external audit’s role to tell the Council what is or what is not an adequate level of reserves
  – We do assess the robustness of arrangements by which the Council sets reserve levels
Questions

• Any questions?

• Thank you for listening