

# Audit Contract Monitoring Arrangements from 2023/24

## Introduction

PSAA is committed to working with all parties to achieve the aim that the audits that we commission meet the standard required by the local audit system, whilst recognising that our role is limited to being the specified appointing person for relevant local government authorities under the Local Audit (Appointed Person) Regulations 2015.

We work within the local audit system arrangements, so on audit quality we liaise closely with the FRC as both incoming system leader of the local audit system and as the regulator that oversee the quality of auditors' work to deliver Code of Audit Practice compliant audits.

Our approach to audit contract quality monitoring is grounded in the International Auditing and Assurance Standards Board's (ISAAB) framework for Audit Quality.

We have taken the attributes the IAASB framework expects to be present in a quality audit and distilled them into three areas:

1. adherence to professional standards and guidance (where we will draw on the assessments carried out by FRC and the ICAEW's QAD);
2. compliance with contractual requirements; and
3. relationship management.

While responsibility for providing a quality audit rests ultimately with an auditor, audit quality, efficiency and effectiveness are shared responsibilities. They are key concerns for appointed auditors and audit firms; for chief finance officers (CFOs) and audit committees; for regulatory and supervisory bodies; for the Comptroller & Auditor General (C&AG) and the National Audit Office (NAO); and for Government. The FRC as regulator has the role of monitoring and enforcement aligned to its purpose to serve the public interest by promoting high standards of financial reporting, governance and audit.

The IAASB framework notes that all parts of the financial reporting supply chain have a role in contributing to and encouraging an audit environment that supports provision of an audit service of the expected quality.

Quality of service delivery formed a core part of the evaluation of tenderers' responses in our audit services procurement, with tenderers encouraged to have regard to the IAASB framework.

Ongoing contract monitoring arrangements have the dual purpose of reporting for opted-in bodies and ensuring that we meet our statutory requirements under the Local Audit (Appointing Person) Regulations 2015 to monitor compliance of auditors against the obligations in the audit contracts.

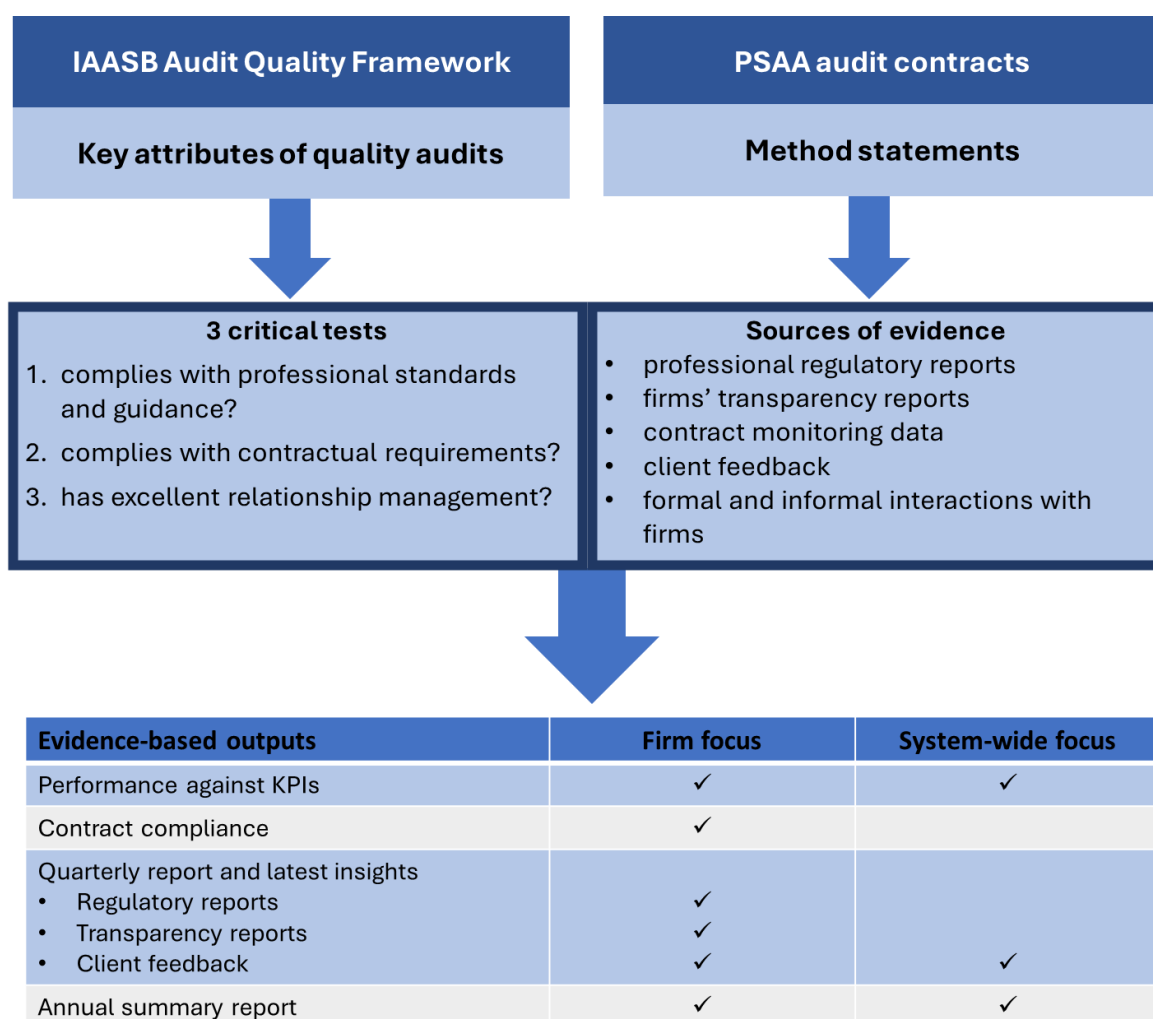
## An overview of our approach

With the IAASB framework as the starting point, we worked with our Advisory Panel and other key stakeholders to develop our approach to audit contract quality monitoring the services provided to opted-in bodies from 2018/19. We have recently refreshed our approach to reflect changes in the audit services contracts for the audits from 2023/24, including seeking feedback from the Advisory Panel.

These principles provide the drivers of our approach to monitoring audit contract quality, which seeks to be:

- **holistic** – includes a range of actions (encouraging, monitoring, reporting);
- **engaged** – links with all parts of the financial reporting supply chain including audit committees and regulators;
- **informed** – brings together intelligence from a variety of sources;
- **transparent** – information is shared openly where possible;
- **drives continuous improvement** – recognises progress will be made by small gains;
- **proportionate** – arrangements should not be unduly bureaucratic or place undue burdens on audit firms; and
- **timely** – encourages action to be taken when required.

The IAASB framework recognises there is a complex interplay of many factors in audit quality and notes the need for a rounded approach. We have set out below the sources we will use to monitor audit quality for the three tests to provide a rounded view. The diagram below summarises our approach.



## **Our approach in more detail**

We hold formal quarterly contract monitoring meetings with each contracted audit firm, in addition to having regular dialogue on specific matters. We publish information on the quality of services delivered under our audit contracts to promote transparency and to report on contract compliance.

### **1. Adherence to professional standards and guidance**

Information on the audit firms' adherence to professional standards and guidance will come from the results of professional regulatory reviews completed by the Audit Quality Review Team (AQRT) for the Financial Reporting Council and the Quality Assurance Department (QAD) for the Institute of Chartered Accountants in England and Wales, the principal RSB for local audits in England. The regulators will be reviewing a sample of local audits. Our contract monitoring of audit quality is based on the work and the reports of the regulators.

We will triangulate the work of the regulators with information on audit quality provided by audit firms in their transparency reports and from their own internal quality monitoring reviews (iQMRs).

### **2. Compliance with contractual requirements**

Information on an audit firm's compliance with contractual requirements will come from a range of sources including:

- Complaints both formal and informal.
- An assessment of a compliance with our Terms of Appointment covering a range of areas such as use of auditors' specific powers, objections, fee variations rotation of key staff, non-audit services work, and data confidentiality.
- An assessment of a compliance with its Method Statements. Each audit firm in its tender response provided details of its approach covering audit delivery (in terms of quality assurance, capability, resourcing and capacity), communications and social value. The Method Statements are incorporated within the contract. Annually firms must provide evidence of their delivery and compliance. Where practicable we will test and triangulate the evidence provided with information from other sources e.g. client feedback.
- An assessment against key performance indicators within the contract.
- Other assurances such as information assurance, economic and financial standing, and modern slavery.

### **3. Relationship Management**

Information about an audit firm's relationship management will come from monitoring the delivery of the communication commitments contained within their Method Statements, reviewing audited bodies' ad hoc enquiries and any complaints, and an annual survey covering all audited bodies. We will issue a survey to each audited body's representatives of both management (typically the s151 Officer) and those charged with governance (typically the Chair of the Audit Committee or equivalent).

## **Reporting on audit contract quality**

We will report on the three tests (compliance with professional standards and guidance, compliance with contractual requirements and relationship management).

We will produce a quarterly monitoring report and an annual report that reflects on the delivery of audits for the year. We discuss any areas of concern identified in the quarterly or annual report with each audit firm. We will publish all reports on our website and provide audit firms' quality and assurance partners with each annual report.

## **Taking action where audit delivery concerns arise**

PSAA has contracted with audit firms to deliver audit services to audited bodies in accordance with:

- the 2014 Act, the 2015 Regulations and any other relevant Law or arrangement;
- the Code of Audit Practice;
- any Supplementary Guidance;
- the Contract;
- Good Industry Practice; and
- any requirements contained in the Terms of Appointment or Supplementary Guidance including reporting requirements.

Where our audit contract quality monitoring arrangements find that an audit firm may not have met a contractual requirement, there are both informal and formal mechanisms through which we can seek rectification by the audit firm.

We would meet with the audit firm to understand and discuss:

- the reason for the issue including the effect on any audited body and PSAA;
- the steps which the audit firm proposes to take to rectify the issue including timescales; and
- any dependencies of the audit firm on PSAA or any audited body to enable resolution.

Where an audit firm does not take action, or that action is inconsequential, there are contractual escalation mechanisms that we can apply.

Ultimately, our audit services contracts require audit firms to follow our monitoring arrangements. The contracts provide for termination where there is a material breach or persistent failure such as consistently failing to substantially deliver its obligations would be viewed as persistent failure.

We would expect that, recognising their professional registration requirements, audit firms will take action to address problems as they are identified.