

Local Audit Backlog – Rebuilding Assurance during the Recovery Period

Background

Local authorities and other local bodies, including police, fire, transport and waste authorities, as well as national parks, provide vital public services to local communities. Timely, high-quality financial reporting and audit is vital for supporting decision-making and accountability of those local public bodies. External assurance gives local taxpayers and elected representatives confidence in the financial management of their local public body.

On 31 July 2024 the Ministry of Housing, Communities and Local Government (MHCLG) issued a **Statement** that set out measures to be applied to clear the significant backlog of unsigned audit opinions of English local public bodies.

This announcement came after only 1% of local public bodies published audited accounts on time for 2022/23. Without decisive action, it was widely acknowledged that the backlog would continue to grow and undermine local accountability and governance.

In September 2024, the Financial Reporting Council (FRC) published a briefing: **Local Audit Backlog Rebuilding Assurance**. The briefing explains how the recovery period may operate in practice for local public bodies that receive disclaimed audit opinions primarily because of statutorily imposed backstop dates limiting the scope of the audit. It has been prepared so that finance teams, elected members and other interested parties can understand what the recovery period may look like in practice.

This paper summarises the main messages from the FRC's briefing.

The overarching objective of the measures is to clear the backlog of outstanding audit opinions and reduce the likelihood of this position returning.

Measures to address the backlog

The Government's approach to clear the backlog of local audits and embed timely audit comprises two parts:

- **Reset measures** - clearing the backlog of historical audit opinions up to and including financial year 2022/23.
- **Recovery period** - a period that reduces the likelihood of the backlog re-emerging through the implementation of backstop dates.

The measures have been developed collaboratively by all organisations involved in regulation and oversight of local public body financial reporting and audit ('system partners') to clear the backlog of outstanding audit opinions.

On 30 September 2024 **The Accounts and Audit Regulations 2015** (which set out the approval and publication requirements for LG audits in England) were amended via **The Accounts and Audit (Amendment) Regulations 2024**, to introduce backstop dates by which point local public bodies must publish audited accounts.

Exhibit 1: Backstop dates

- For years up to and including 2022/23 – 13 December 2024
- 2023/24 – 28 February 2025
- 2024/25 – 27 February 2026
- 2025/26 – 31 January 2027
- 2026/27 – 30 November 2027
- 2027/28 – 30 November 2028

A new draft **Code of Audit Practice** (the Code) has also been published¹ by the National Audit Office (NAO) that requires auditors to give their opinion in time to enable local public bodies to comply with the backstop date. The Code will apply to audits which have not been certified complete at the time it comes into effect, and to the audits of local public bodies from 2024/25, until it is replaced after five years. The Code also requires auditors to carry out full scope audit of Value for Money (VFM) arrangements for 2023/24 onwards.

¹The new draft Code of Audit Practice was laid in Parliament on 9 September 2024 and will take immediate effect once it has received Parliamentary approval.

Rebuilding assurance

The backstop dates enable auditors to rebuild assurance over multiple years rather than performing all work in a single year. Auditors will make prioritisation decisions to issue audit opinions ahead of backstop dates and, as a result, they may not be able to obtain evidence over all balances. This means it could take several years for disclaimed opinions to be lifted.

A local public body's financial statements include the following:

- Opening balances brought forward from the prior year, including, for example, cash, general fund and ringfenced reserves, property valuation and pension liability / asset valuations;
- Closing balances;
- In-year expenditure, income, reserves and cash-flow movements;
- Comparative figures from the prior year; and
- Explanatory notes to the financial statements.

The objective of the auditor is to obtain sufficient evidence to conclude that they have reasonable assurance that the financial statements, as a whole, are free from material misstatement.

Where an auditor is unable to gain enough evidence or is unable to reach this conclusion based on the evidence gathered, they will issue a modified opinion, or a disclaimed opinion where the issues are pervasive.

Where the opinion on the prior year audit has been disclaimed, the auditor will not have assurance over:

- Opening balances brought forward from the prior year (the prior year closing balance); and
- Comparative figures.

It is also unlikely that the auditor will be able to obtain sufficient evidence to conclude they have reasonable assurance over the in-year expenditure, income, reserves and cash flow movements without assurance over the opening balances, as illustrated in the example below:

If a body has £100 at the end of the year but the auditor does not know whether the body had £50 or £10 at the start of the year, the auditor will not know whether the body has gained £50 or £90 during the year.

This may also impact on subsequent years. Where the auditor does not have assurance over in-year movements, they will also not have assurance over those figures when they are shown as comparatives in the following year.

Rebuilding assurance

In normal circumstances, in the year after a disclaimed opinion is issued, an auditor would perform work to assure all the opening balances and prior year comparatives in a single year.

The recovery period has been designed to allow auditors to recover from disclaimed opinions in a way that does not cause timeliness issues to recur. The backstop arrangements may create time constraints that impede the auditor from completing all the necessary audit procedures, in a single year, to support their opinion. There may also be several years prior to the current year for which the auditor has issued a disclaimed opinion. In these circumstances, significant challenges exist in both the preparation and auditing of opening balances.

When designing approaches to rebuild assurance over multiple years, auditors will need to decide which balances to prioritise each year to deliver the optimal pathway to returning, as soon as possible, to a position where they are able to complete audits in full and the opinion is not influenced by backstop dates. The testing may be different from normal as the auditors may need different evidence to conclude that they have reasonable assurance over the balances.

To help auditors meet their requirements under the Local Audit and Accountability Act 2014 and the Code of Audit Practice, the National Audit Office (NAO) has published a package of guidance: **Local Audit Reset and Recovery Implementation Guidance** (LARRIGs). LARRIGs are prepared and published with the endorsement of the Financial Reporting Council (FRC) and are intended to support the reset and recovery of local audit in England.

Local public bodies should not be unfairly judged for modified or disclaimed opinions beyond their control.

The measures have been designed to enable any limitation of scope of the audit to be a result of the system-imposed backstop and not any actions of management, as the latter may lead to significant consequences for a local public body. In circumstances where the local public body has significantly delayed the publication of their statement of accounts or withheld audit evidence, the auditor may use their judgement to determine that management's failure to meet the backstop date represents a management-imposed limitation of scope.

Rebuilding assurance

Key to success is effective communication between the auditor and the audited body, including those charged with governance.

All audit engagements are different, and local circumstances will influence the scale of work needed for auditors to make a timely return to removing disclaimed opinions.

Proposals on the audit approach to be adopted and the timeline for returning to unmodified opinions will be presented to those charged with governance. The development of this audit approach is likely to be an iterative process and refined over successive audit cycles.

Recovery from the backlog is a shared endeavour between auditors and local public bodies. Accounts preparers have a vital part to play, providing good quality draft financial statements supported by comprehensive working papers and supporting evidence to auditors. The success of these proposals relies on both auditors and accounts preparers working closely together to agree jointly-owned delivery plans for each year's audit. Audit Committees should ensure that they are planning and able to play their full part in the process .

