

**AAT RESPONSE TO THE FINANCIAL REPORTING COUNCIL'S
CONSULTATION DOCUMENT ON "FRC REGULATIONS AND STATUTORY
GUIDELINES UNDER THE LOCAL AUDIT AND ACCOUNTABILITY ACT 2014"**

1 EXECUTIVE SUMMARY AND OVERVIEW

- 1.1 The Association of Accounting Technicians (AAT) welcomes the opportunity to respond to this Financial Reporting Council (FRC) consultation on the key issue of "FRC Regulations and Statutory Guidance under the Local Audit and Accountability Act 2014" (condoc).
- 1.2 From a public perception and confidence viewpoint, it is AAT's view that there should be a presumption that there is one set of standards applicable to all audits and a consistent quality of auditing across the entire spectrum of audits. AAT therefore welcomes these proposals to align the requirements for local public bodies' audits with other types of audits as an essential underlying concept of these Regulations and Guidelines.
- 1.3 The proposed Regulations concerning transparency requirements and in respect of the Register of Local Public Auditors are considered acceptable and desirable.
- 1.4 AAT has concluded that the proposed Regulations and Statutory Guidelines will be totally acceptable and workable by those audit firms already committed to providing audit services to local public bodies. However AAT can foresee difficulties in enabling other firms to enter this market.
- 1.5 AAT is fully supportive of the concept generally that the approval of Engagement Leads needs to be rigorous but not to be restrictive in enabling firms access to the local public bodies audit market.
- 1.6 If the approval of Engagement Leads is conditional upon minimum periods of practical experience of local public bodies' audits specifically, the consequence is that access to the local public audit market is restricted to those currently involved in such work, which is represented by the largest audit firms.
- 1.7 Smaller firms wishing to be involved would need to entice suitably experienced staff from one of those larger firms to be nominated as Engagement Lead and would need to secure sufficient local public audit appointments as to be financially viable. Inevitably this would require a commitment to establish a full time team dedicated to local public body audits with a level of total fee income to be generated which is unlikely to be readily achievable and so would discourage smaller firms from even attempting to enter the market. AAT has expanded on these concerns in section 3.3 (below).
- 1.8 There is also a matter of fee levels which need to be considered in enabling smaller firms to enter the market, particularly if they are to be expected to provide services to smaller local public bodies. At the present time, the level of scale fees used by the Audit Commission would not be a viable basis for smaller firms to adopt. For example, most Parish Council audits, while carried out by a larger national audit firm, each generate audit fees of only a few hundred pounds which would be totally inadequate to enable, say, a local smaller firm, to recover the costs of carrying out an audit in accordance with Auditing Standards.
- 1.9 Consequently AAT concludes that the requirements for the approval of Engagement Leads needs to recognise that local public audits may only be a minor part of their overall audit responsibilities and experience and also need to recognise the nature, size and complexity of the audit engagements for which they are responsible.

- 1.10 AAT has further concluded as set out in 2.3.8. (below) that there are further benefits to be achieved by the requirements for the scrutiny of accounts for smaller public bodies to mirror those for charities in terms of widening access to the local public audit market.

2 RESPONSE TO QUESTIONS FOR RESPONDENTS

2.1 Transparency Reports

Question 1

Do you agree that the requirement to publish transparency reports should be restricted to auditors of “major local audits” (paragraph 4.4.1)?

- 2.1.1 Although there is a strong argument that public confidence needs to be established in all auditors of public bodies, AAT agrees that the requirement to publish transparency reports should be restricted to auditors of ‘major local audits’ as the burdens and costs of such for firms auditing smaller public bodies would be disproportionate to the benefits achieved.

Question 2

Do you agree that a firm that audits both major local bodies and private sector public interest entities should be able to publish a single transparency report (4.4.2)?

- 2.1.2 It is our view that public bodies’ audits should be considered as requiring the same approach and audit techniques applied to audits in general, but as a specific industry sector, requiring expertise of specialist technical and statutory requirements (similar, for example, to the needs for charity audits or housing association audits). Therefore AAT considers it sensible for audit firms of both major public bodies and private sector public interest entities to publish a single transparency report both to avoid a duplication of effort and to ensure that such firms are consistent in their internal quality procedures as regards audits in all sectors.

Question 3

Do you agree that (i) the information requirements and (ii) the requirements for publication should follow as closely as possible the existing requirements for auditors of private sector public interest entities (paragraph 4.4.3)?

- 2.1.3 For the reasons set out in the response to question 2 (above) AAT believes that the information requirements and the requirement for publication should be fully aligned with requirements for auditors of private sector public interest entities, even if this necessitates modifying the existing requirements for private sector audits.

Question 4

Are there additional information requirements relating to local public audit that we should include as statutory requirements for transparency reports?

- 2.1.4 AAT does not consider that the inclusion of major public audits in the requirements for transparency reports should require any additional information for the reasons set out in our response to question 2 (above).

Question 5

Do you have specific comments on the draft regulations at Annex A?

- 2.1.5 AAT has no specific comments to make in respect of the draft regulations as set out at Annex A (condoc) relating to transparency reports.

2.2 Register of Local Public Auditors

Question 6

Do you agree that the requirements for the Register of Local Public Auditors should match as closely as possible the existing FRC requirements for the Register of Statutory Auditors (paragraphs 4.8 and 4.9)?

- 2.2.1 AAT's view is that the information required to be shown in the Register of Local Public Auditors and the Register of Statutory Auditors should be identical in nature, to avoid any implications of inferiority of one compared to the other.

Question 7

Do you have specific comments on the draft regulations at Annex B?

- 2.2.2 AAT has no specific comments on the draft regulations as set out at Annex B (condoc) in respect of Recognised Supervisory Bodies (RSB).

2.3 Engagement Leads

Question 8

Do you agree with the overall approach at paragraph 4.17 below that the RSB's requirements for approving Engagement Leads need to be rigorous but avoid being too complicated or overly restrictive on allowing access to the local public audit market?

Question 9

Do you support the detailed proposals, set out at paragraphs 4.18 to 4.28 below, for the experience and practical training requirements individuals should have to meet for approval?

Question 10

Do you support the proposal at paragraph 4.29 below, that there should be a specific requirements on an RSB to place a specific obligation on a firm undertaking local public audit work to satisfy itself that the Audit Engagement lead has practical auditing experience of the regulatory and reporting requirements relevant to that audit engagement?

Question 11

Do you have additional or alternative requirements that you consider should apply to those wishing to take on the responsibility as an Engagement Lead within a firm registered for local public audit?

- 2.3.1 The following comments, which follow relate to questions 8, 9, 10 and 11, reflect AAT's concerns over the proposed requirements for approving Engagement Leads.
- 2.3.2 AAT acknowledges and agrees with the objectives as set out in question 8 but believes that the approval requirements should be no more rigorous than those required of a Responsible Individual for audits in general. To be otherwise could lead to a presumption that a lower standard is acceptable for statutory audits other than for local public bodies.
- 2.3.3 AAT's view is that there are two separate aspects to be considered when assessing the competency of Engagement Leads. Firstly, Engagement Leads need to be competent in the conduct of audits generally which is reflected particularly by experience. The second aspect is for Engagement Leads to have the appropriate technical knowledge relevant to the type of local public body being subject to audit, which is dependent upon formal learning as part of the individual's Continuing Professional Development (CPD) requirements.
- 2.3.4 Paragraph 4.21 (conduc) refers to the need for Engagement Leads to have practical experience of the supervision of audits of local public bodies of at least two years out of the previous five years. Under paragraph 4.26 (conduc) it is proposed that an Engagement Lead may be approved on the basis of a maximum of three years supervised practical training in audit and accounting, of which six months must be in local public audit and a minimum of one year in local public audit, other public sector work or company audit work. AAT considers that both of these criteria for approving Engagement Leads result in the need for Engagement Leads to have substantial previous and ongoing experience of local public audits. This level of ongoing experience of an Engagement Lead would necessitate a substantial workload for the audit firm concerned, with a number of staff dedicated to local public audits under the supervision of the Engagement Lead, if such work is to be an economically viable proposition for the audit firm. Consequently this may preclude smaller audit firms who do not have a local public bodies' audits workload sufficient to justify the employment of a dedicated Engagement Lead and audit team from being in this market. The consequence would be that only larger audit firms would be in a position to have full time dedicated Engagement Leads thereby depriving smaller local public bodies from having access to appropriately sized audit firms.
- 2.3.5 AAT recommends that the technical knowledge of Engagement Leads should be focused on setting learning requirements based on CPD requirements set by each RSB, supported by appropriate levels of all audit experience generally, to be able to illustrate competences as is required for the approach to all audits,

such as independence, attitude of mind and appropriate audit techniques. In this respect, it would be vital for approved Engagement Leads to be able to illustrate appropriate technical knowledge of “Value for Money” reporting, although not necessarily having previous experience of such. Experience of profit maximisation in commercial scenarios should be transferrable to value for money concepts for local public audits when supplemented by technical knowledge.

- 2.3.6 Sections 4.29, 4.30 and 4.31 (conduc) suggest the possibility of RSB’s approving Engagement Leads by reference to the nature of the local public bodies engagements undertaken but is dismissed on the grounds of costs, complexity and differentiating from the requirements of company audits. While AAT agrees that detailed regulations to this effect are not desirable, AAT fully supports the concept that RSB’s should require Engagement Leads only to be responsible for engagements for which they are competent, particularly with a view to enabling smaller firms to be involved in local public bodies audits, even if on a small scale. Ultimately there should be reliance on the disciplinary powers of RSB’s to discipline any approved Engagement Leads who carry out work which is outside of their competence.
- 2.3.7 As a consequence, Engagement Leads should be suitably experienced to carry out audits generally across the spectrum of industry sectors, and have the technical knowledge specific to the local public bodies concerned, in the same manner that a Responsible Individual is required to be experienced in audits generally and technically knowledgeable in the specific industry specialisations of the entities concerned.
- 2.3.8 In addition AAT suggests that consideration should be given to the following:
 - (i) Seeking to improve access to the local public body audit market and to give smaller public bodies the opportunity to obtain such services at an economic cost, proportionate to the level of their activities, which is to ease the audit requirements for smaller public bodies.
 - (ii) While it is in the public interest to ensure that all public bodies are fully accountable there can be a close comparison as to meeting public interest needs with those of charities where those with annual income between £250,000 and £500,000 are subject to an Independent Examination by an examiner with a recognised qualification rather than the burden of the full audit regime. For those with annual income between £25,000 and £250,000 the Independent Examiner need not have one of the recognised qualifications but be “suitable” and below £25,000 need have no Independent Examination.
 - (iii) It would therefore appear logical for the requirements to scrutinise local public body accounts to mirror those for charities and thereby widen access to the market for accounts examiners for public bodies with annual income up to £500,000.

3 REGULATORY IMPACT ASSESSMENT

- 3.1 There is a presumption that audit firms bidding for local public bodies audit engagements will not be constrained by scale fees, but will operate in an open market as regards fees. Undoubtedly, this will result in increased fees for smaller public bodies compared with the current nominal levels of scale fees. The latter would not be considered viable for regulated audit firms, especially larger audit firms.

- 3.2 As set out in section 2.3.4 (above), AAT is concerned that requirements for Engagement Leads to have practical experience of local public bodies audits will restrict the number of firms able to take on such audits, and in the absence of smaller firms able to offer audits will give rise to unnecessary additional costs for smaller local public bodies, as well as a limited choice of approved audit firms eligible for appointment.
- 3.3 Annex C (condoc) highlights the fact that the FRC is obliged to provide statutory guidance to the RSB's for the approval of Engagement Leads for local public bodies' audits without a parallel requirement for company audit work. AAT considers it desirable that there should be parallel requirements so that approvals of an Engagement Lead and Responsible Individual are interchangeable. Any individual approved as a Responsible Individual for company audit work should automatically be approved as an Engagement Lead subject only to illustrating appropriate technical knowledge to be able to supervise the engagements falling under his responsibility (and vice versa). AAT recognises that this would necessitate modifying the existing requirements for private sector audits.

4 CONCLUSIONS

- 4.1 AAT considers that the proposed Regulations and Guidelines provide an opportunity to unify the requirements for regulating all auditors, both for statutory audits and local public bodies audits, so that there is a consistency of standards applied. Local public bodies can be recognised as a particular specialised audit area, just as charities or housing associations are recognised as such, with the specialised aspects of the audit requiring technical knowledge, rather than practical experience. Practical experience of the basic approach to and conduct of audits are requirements common to all audits.
- 4.2 As referred to in section 3.3 (above), AAT considers that approval of individuals either as an Engagement Lead or as a Responsible Individual should be automatically interchangeable, subject only to any limitations of technical competence in relation to the audits for which the individual is responsible.
- 4.3 There is also a need to compare the audit requirements for local public bodies with those for charities as set out in 2.3.8 (above), in that both need to be accountable in the public interest but the burdens should be proportionate to the levels of their activities. It is illogical for different audit requirements to apply to smaller local public bodies and smaller charities.
- 4.4 There is an opportunity to expand the number of audit firms involved in local public bodies' audits and especially to encourage smaller local public bodies to look to smaller local audit firms with local knowledge to provide audit services, particularly those firms that are already Registered Auditors. However, it must be recognised that it is unlikely that smaller local audit firms would consider it a viable proposal to establish a dedicated specialist local public bodies audit team if the proposals set out in this Consultation Document were to be adopted for the reasons set out in section 2.3.4 (above).
- 4.5 It is unlikely that many smaller firms would seek to enter the local public bodies audit market if they are not already Registered Auditors due to the commitments and risks attaching to the need for compliance with Audit Regulations, being the same considerations which preclude smaller firms from being involved in other audit work generally.

5 ABOUT THE AAT

- 5.1 The Association of Accounting Technicians (AAT) is pleased to have the opportunity to comment on the Consultation Document on proposals for “FRC Regulations and Statutory Guidelines under the Local Audit and Accountability Act 2014”.
- 5.2 AAT has over 49,800 Members and 80,000 Students worldwide¹.
- 5.3 AAT has over 4,100 Members in Practice who provide accounts and tax services, including assisting companies to meet their statutory filing obligations to over 300,000 sole traders, partnerships and limited companies, covering a full range of businesses, particularly small and medium-sized enterprises and owner-managed entities.

Further engagement

If you have any questions arising from our submission or would like to discuss any of the points in more detail then please contact AAT at:

email: consultation@aat.org.uk and aat@palmerco.co.uk
telephone: 020 7397 3088

Aleem Islan
Association of Accounting Technicians
140 Aldersgate Street
London
EC1A 4HY

¹ Figure correct at 30 Sept 2014