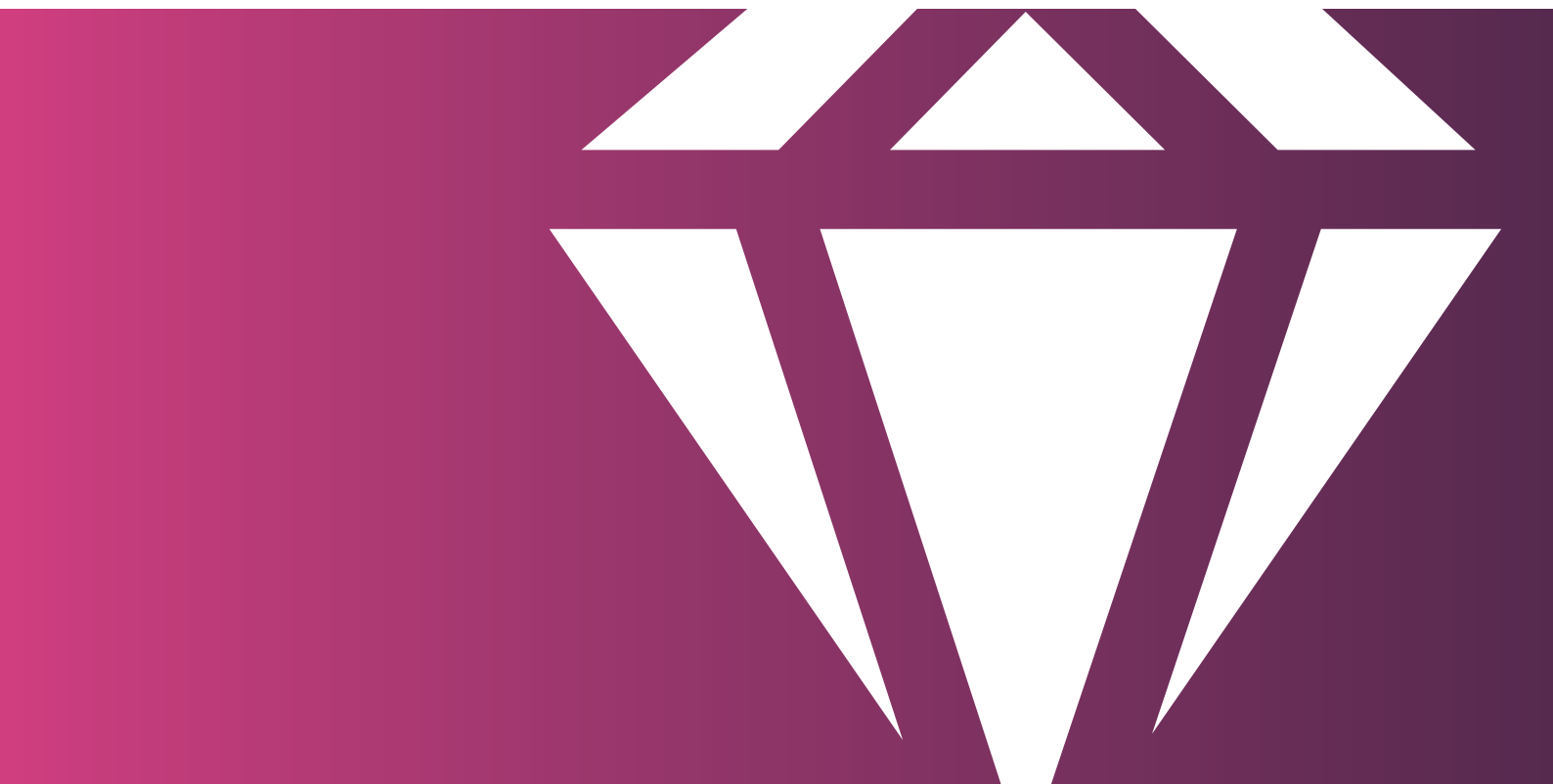


# Quality of public audit in Scotland

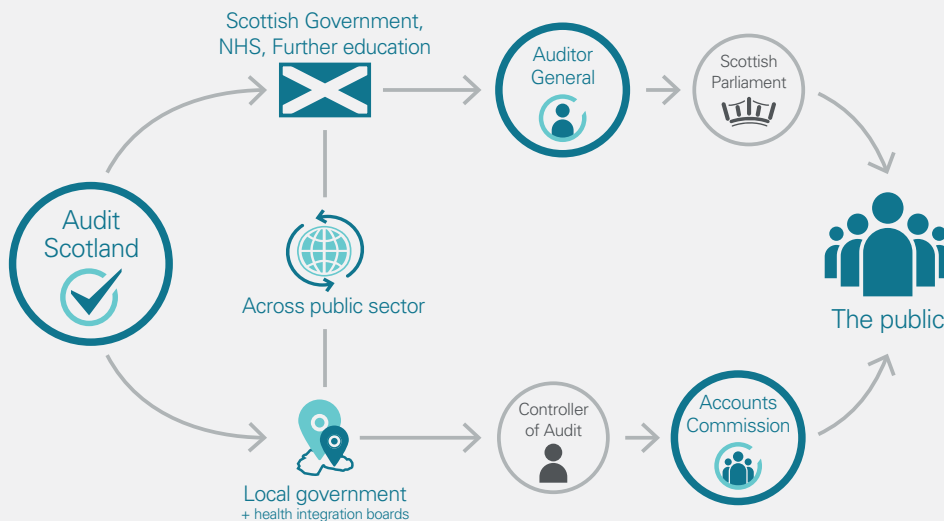
Annual report 2018/19



# Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- **Audit Scotland** is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.
- The **Auditor General** is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The **Accounts Commission** is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.



## About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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# Contents

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Audit Quality and Appointments team	3
Key messages	4
Public audit in Scotland	5
<b>Introduction</b>	<b>6</b>
Auditor General for Scotland and Accounts Commission	6
The Audit Quality Framework	6
Audit Scotland and appointed firms	7
Audited bodies	8
<b>Inputs</b>	<b>9</b>
Values, ethics and attitudes	9
Knowledge, experience and time	9
Audit process and quality control arrangements	12
<b>Outputs</b>	<b>14</b>
Audit quality indicators	14
Quality monitoring	15
Reporting	18
Audited bodies' views on audit work	20
Areas for improvement and future focus	23

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# Audit Quality and Appointments team

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This report has been prepared by the Audit Quality and Appointments (AQA) team which is responsible for applying the [Audit Quality Framework](#) across all financial audits and performance and Best Value audits. This covers the quality of audit work undertaken by Audit Scotland and appointed firms. AQA is independent of audit delivery and provides assurance on audit quality to the Auditor General for Scotland and the Accounts Commission.

Audit Scotland is committed to providing high-quality audits to the public sector in Scotland. This is detailed in [Public Audit in Scotland](#), which sets out the principles and themes of public audit and how it fits with and responds to the public policy environment in Scotland. Audit Scotland exists to support the work of the Auditor General for Scotland and the Accounts Commission.

This report summarises the detailed assessment of audit quality carried out on audit work delivered by Audit Scotland and the appointed firms on behalf of the Auditor General for Scotland and the Accounts Commission in 2018/19. The report provides evidence that auditors have designed and implemented effective audit quality arrangements to assure the quality of their audit work. The report also highlights areas for further improvement.

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# Key messages

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The programme of work carried out under the Audit Quality Framework provides evidence of compliance with auditing standards and the [Code of audit practice](#) (the Code), together with good levels of qualitative performance and some scope for improvements in audit work delivered in the period 1 April 2018 to 31 March 2019.

Independent external reviews of audit quality carried out by The Institute of Chartered Accountants of Scotland (ICAS) show evidence of compliance with expected standards:

- ICAS did not identify any concerns with audit opinions
- 55 per cent of financial audit files reviewed by ICAS over the last two years were graded as limited improvement required, the remaining reviews were graded as improvement required
- ICAS noted considerable improvements in the documentation of performance audits and Best Value assurance reports.

Other performance measures showing good performance include:

- 78 per cent of internal reviews of financial audits in the last two years required only limited improvements
- all audit providers have a strong culture of support for performing high-quality audit
- stakeholder feedback shows audit work has had impact
- non-audit services (NAS) are declining in number and value and requests made complied with the Auditor General for Scotland and Accounts Commission's [NAS policy](#).

AQA monitors progress against areas for improvement. A common area for improvement in the last two years has been the need for better documentation of audit evidence. In 2018/19 further areas for improvement were identified in:

- the use of analytical procedures
- the application of sampling methodology.

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# Public audit in Scotland

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Recent high-profile corporate collapses in the private sector have led to considerable scrutiny of the audit profession. The Brydon review is looking into the quality and effectiveness of the UK audit market. The Kingman review, the Competition and Markets Authority market study of the audit services market and the Business, Energy and Industrial Strategy Committee's report on the Future of Audit have all reported on structural weaknesses in the private sector audit regime. The reviews are placing a strong focus on the need for independence of auditors from the bodies they audit.

The public audit model in Scotland is fundamentally different to the private sector audit regime and is well placed to meet the challenges arising from the reviews of the auditing profession. Public audit in Scotland already operates many of the proposed features to reduce threats to auditor independence including:

- independent appointment of auditors by the Auditor General for Scotland and Accounts Commission
- rotation of auditors every five years
- independent fee-setting arrangements and limits on non-audit services
- a comprehensive Audit Quality Framework.

AQA will continue to develop its activities to provide the Auditor General for Scotland and Accounts Commission with assurance about audit quality. The Audit Quality Framework will be refreshed to take account of the findings from the first two years of its application and to reflect on the developments in the wider audit environment. Further development is planned over the following year to include:

- enhancing stakeholder feedback
- reviewing the structure and transparency of audit quality reporting.

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# Introduction

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The AQA team prepares this report on behalf of Audit Scotland. AQA provides assurance on audit quality to the Auditor General for Scotland and the Accounts Commission and is led by an Associate Director. The team does not conduct audit work and is independent from auditors. AQA also supports Audit Scotland's Ethics Partner and provides advice and guidance to staff, firms, the Auditor General for Scotland and the Secretary to the Accounts Commission on ethical standards issues in accordance with the [Ethical Standard](#).

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Audit Quality and  
Appointments  
team

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## Auditor General for Scotland and Accounts Commission

The Auditor General for Scotland and the Accounts Commission set out the principles and themes of public audit, and how auditors carry it out in [Public Audit in Scotland](#). The Auditor General for Scotland and Accounts Commission have adopted a joint [Code of audit practice](#), a rigorous joint procurement process that is independent of the individual audited bodies, and a joint Audit Quality Framework.

The Auditor General for Scotland is responsible for central government, NHS and further education college audits, while the Accounts Commission is responsible for local government audits, including integration joint boards. Both appoint auditors to conduct the financial audits under the Code, which in local government includes Best Value. The Auditor General for Scotland and Accounts Commission consult widely to set their performance and Best Value [work programme](#), however the statutory responsibilities for the programme rest solely with the Auditor General for Scotland and Accounts Commission.

The Auditor General for Scotland and the Accounts Commission's governance of audit quality is of fundamental importance to their roles. AQA provides biannual assurance reports to both during the year, with details of actions taken in response to findings. The findings of these two reports are summarised in this annual public report in the [Outputs](#) section.

## The Audit Quality Framework

Producing high-quality audit work is critical in delivering Audit Scotland's ambition for world class audit. The [Audit Quality Framework](#) establishes working arrangements that go beyond regulatory requirements and provide assurance over all audit work and providers, including Best Value and performance auditing. The Audit Quality Framework complements Public Audit in



Scotland and the Code. These documents require auditors to comply with the highest professional standards, including International Standards on Auditing (UK) (ISAs (UK)) and the Financial Reporting Council's Ethical Standard. The Audit Quality Framework ensures there is greater consistency in measuring audit quality across all audit work.

AQA applies the Audit Quality Framework across all audit work and providers to assess and improve audit quality. The Audit Quality Framework recognises the high level of public scrutiny of the audit profession and the role of auditors. AQA carries out direct reviews of work delivered by Audit Scotland and the firms and draws evidence from independent reviews carried out by the Institute of Chartered Accountants in Scotland (ICAS), Mark Diffley Consultancy and Research (MDCR) surveys and other independent sources.

ICAS carries out independent assurance reviews covering financial audit, performance audit and Best Value work. The reviews include annual coverage of the work carried out by Audit Scotland auditors and all appointed firms over the five-year appointment. MDCR carries out independent surveys on the perception of audit by recipients of audit to provide robust data about the views of stakeholders. These independent arrangements are a significant part of assessing audit quality and provide the highest level of assurance to all stakeholders.

The Audit Quality Framework has been used to direct the programme of work on which this report is based. The Audit Quality Framework strengthens audit quality arrangements at several levels through:

- independent external assurance across all audit work improving comparability and robustness
- consistency of approach across all audit work and providers
- transparent and contextual reporting of audit quality work.

This report provides an assessment of audit quality in terms of the key roles, the inputs and the outputs as described in the diagram below.



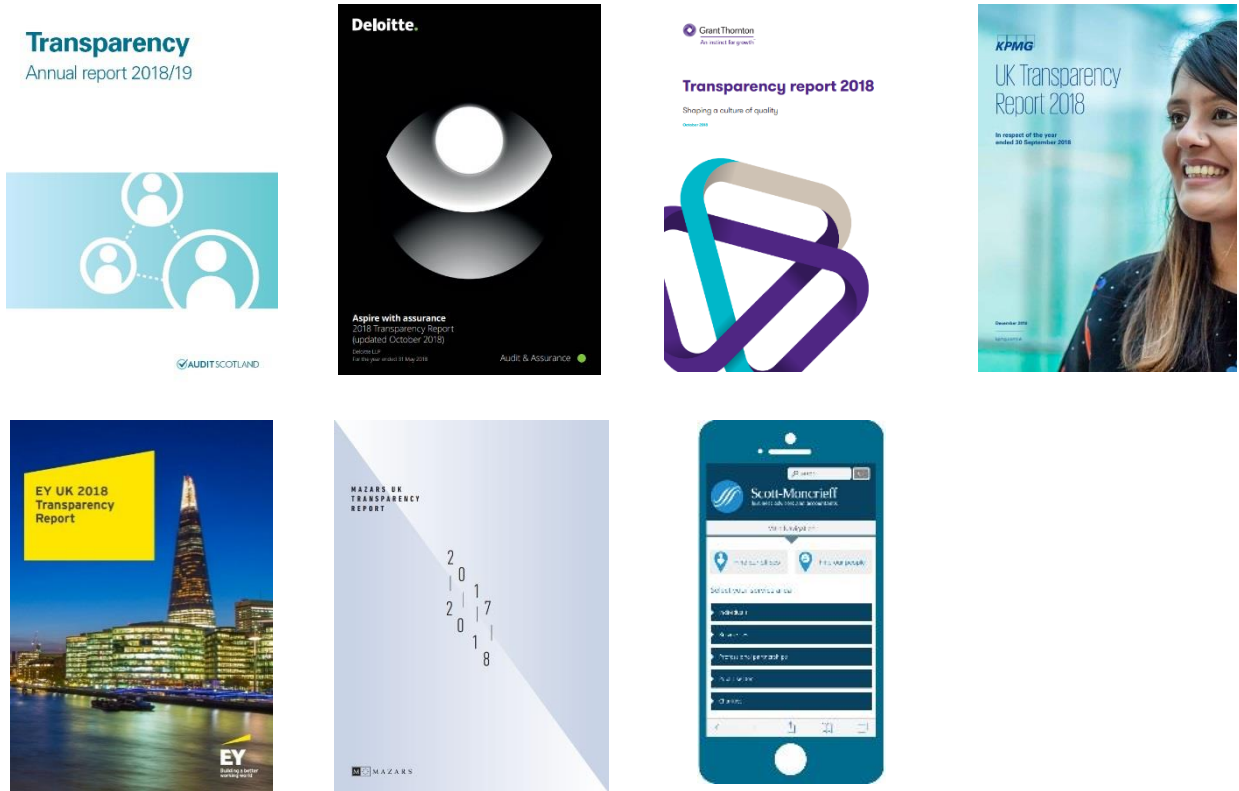
## Audit Scotland and appointed firms

Public audit is carried out by Audit Scotland auditors and appointed firms who are subject to a rigorous and open procurement process. Approximately two thirds of financial and Best Value audit work is carried out by Audit Scotland auditors with the remaining third conducted by appointed firms. Performance audit work is carried out by Audit Scotland auditors.

Each appointed firm has its own arrangements for ensuring audit quality for financial audits. Their arrangements vary but are all consistent with [International Standard on Quality Control 1](#).



Further information about their audit quality arrangements is available in their Transparency reports.



### Audited bodies

Public sector auditors in Scotland audited 222 2017/18 accounts for 215 [public organisations](#) in 2018/19, including the Scottish Government, the NHS in Scotland and local authorities. These organisations spend over £43 billion of public money every year.



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# Inputs

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This section of the report explains how the inputs to an audit, such as knowledgeable and experienced staff, audit methodologies and the arrangements for ensuring compliance with ethical standards put in place by auditors contribute to the delivery of audit quality.

## Values, ethics and attitudes

### Independence

Scottish public sector bodies do not appoint their own auditors. The independent appointment of auditors is a unique feature of public sector audit and is an important safeguard that helps to ensure that the auditor is free from any potential conflict of interest or other pressure which may compromise their judgement. The Auditor General for Scotland and Accounts Commission appoint auditors to carry out the statutory financial audits of Scottish public sector bodies. The appointed auditors include Audit Scotland staff and some of the major UK audit firms. Audit Scotland's performance audit and Best Value staff carry out performance audits and work with financial auditors in auditing Best Value. Auditors are required to apply their professional expertise to conduct their audits and report their findings in public.

### Ethics

All auditors have arrangements to comply with the Financial Reporting Council's Ethical Standard to avoid any actual or perceived conflicts of interest. AQA works with Audit Scotland's Ethics Partner to evaluate potential conflicts of interest when making recommendations for audit appointments.

All auditors make annual declarations of any potential conflicts of interest for their public sector work. Audit Scotland and appointed firms use this information to allocate staff to audits or to put in appropriate controls. ICAS reviews auditors' ethics arrangements under International Standard on Quality Control 1 as part of their review programme.

### Non-audit services

Auditors may undertake some non-audit services, including consultancy type work, for the bodies they audit. The Auditor General for Scotland and Accounts Commission issued a policy statement explaining what non-audit work is permissible and requiring auditors to explain how any proposed work complies with the Financial Reporting Council's Ethical Standard and the Code, together with an explanation of how their independence will be safeguarded. No non-audit services are carried out by auditors without the prior approval of AQA, and AQA only approves work that clearly complies with the Ethical Standard. AQA may consult Audit Scotland's Ethics Partner where appropriate. Auditors carried out permitted non-audit services to a value of £155k representing 0.8 per cent of total fees during the 2017/18 audits (£618k representing three per cent of total fees during 2016/17 audits) without compromising their independence.

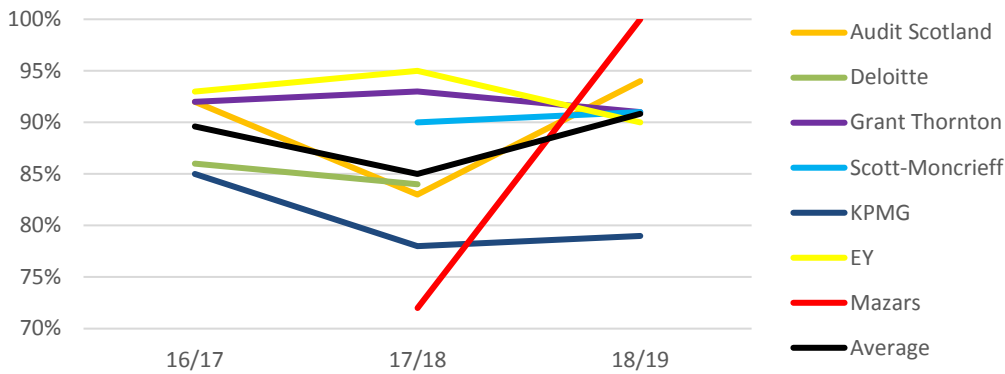
## Knowledge, experience and time

People are the most important assets in an audit. Having the right staff, allocating the right time to audits and providing the right training and knowledge are critical to delivering high-quality audit work. The quality of the staff inputs to audits are demonstrated through staff surveys, qualifications, training and application of technical guidance.

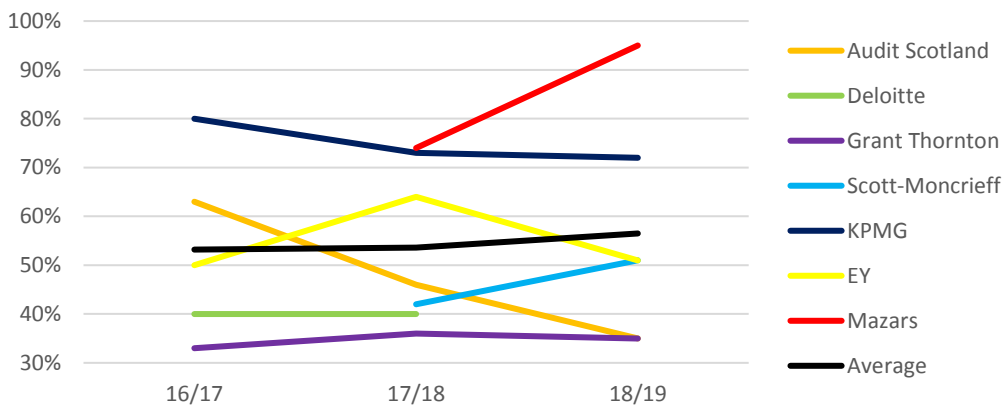
### Staff surveys

Audit Scotland and appointed firms conduct regular surveys to provide an insight into staff views on how well they are supported to provide high-quality audit work. The information presented by the appointed firms is representative of the public sector audit work carried out in Scotland.

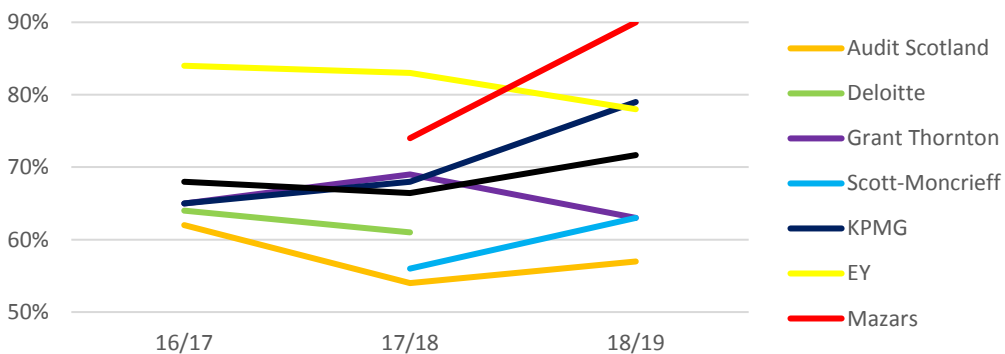
### I am encouraged to carry out a high quality audit



### The time and resources available to me enables the delivery of a high quality audit



### The training and development I receive enables a high quality audit



Note: Scott-Moncrieff and Mazars did not provide details in 16/17, and Deloitte conducts the survey on an 18-month cycle so do not have figures for the current year.

The results show that there is a strong culture of support for performing high-quality audit across all auditors, with the decline seen in 17/18 reversed in 18/19. The average view of the time available to auditors is steady year on year. There is however considerable variation between auditors. Both Audit Scotland and Grant Thornton scores have fallen to 35 per cent. Auditors remain broadly positive about the adequacy of training as the majority show an improved view in 18/19.

This information enables monitoring of trends over time and allows auditors to take account of the findings in developing their human resources strategies.

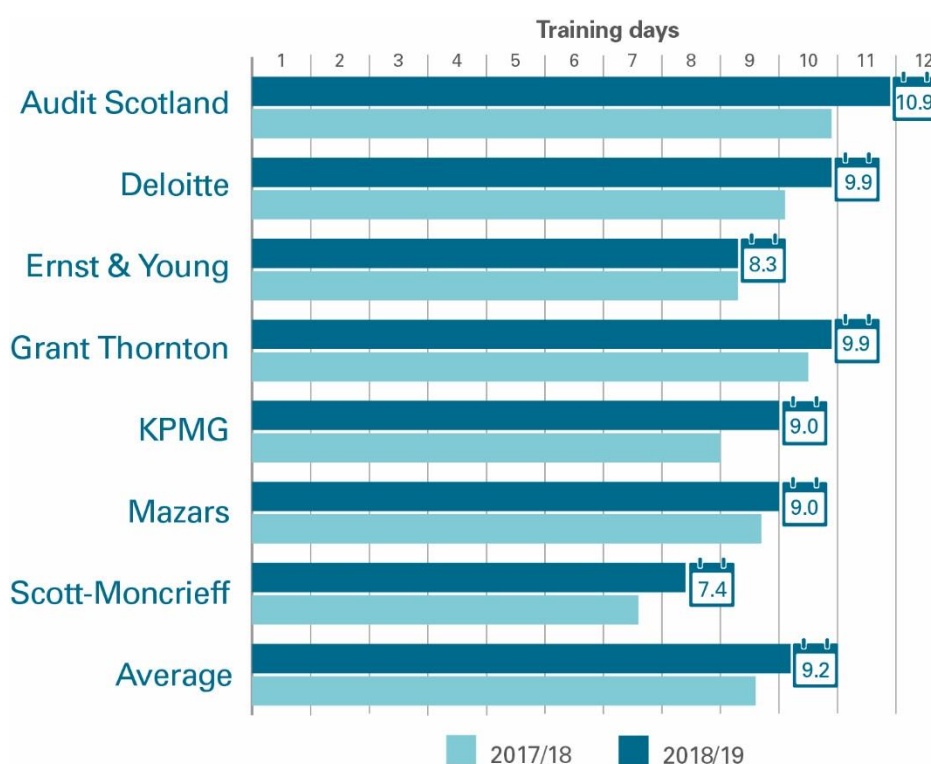
## Qualifications

Audit work is carried out by appropriately trained and qualified individuals. The firms have 100 per cent of their staff either qualified or in training. Ninety-seven per cent of Audit Scotland staff working in financial audit are either CCAB (Consultative Committee of Accountancy Bodies) or Chartered Institute of Management Accountants qualified or in training for a CCAB qualification. A further three per cent have other qualifications in areas such as accounting or IT.

Staff in the Performance Audit and Best Value group (PABV) have a variety of audit and research-related qualifications, all of which go towards supporting the delivery of high-quality audit work. Seventeen per cent (25 per cent in 2017-18) of staff within PABV are either CCAB qualified or in training for a CCAB qualification, which supports Audit Scotland's flexible 'one organisation' working. PABV staff also have several relevant post graduate qualifications in support of their work.

## Training

All auditors recognise the importance of training their staff. The average number of days that staff receive in a year are shown in the table below. This figure excludes trainees.



Note: Scott Moncrieff's total excludes wider Continuous Professional Development undertaken by staff.

The amount of time spent on staff training varies between providers. This variation arises from the different ways in which training is organised and recorded. Nevertheless, the data shows that considerable investment is being made in staff training with an overall average of 9.2 days per member of staff (8.6 days in 17/18).

The professional institutes, of which all qualified auditors are members, have Continuous Professional Development requirements which they monitor. This provides further assurance that auditors are undertaking adequate training to maintain their professional competence.

## Technical guidance

Audit Scotland's Professional Support team provides guidance and advice on technical accounting and auditing issues to all auditors to inform their professional judgement and promote a consistent approach. The Professional Support team also provides bulletins and updates on technical developments and emerging risks to auditors and audited bodies, promotes good practice in financial reporting, and produces guidance on wider scope subjects. Appointed firms supplement this with their own technical guidance and advice to staff.

## Audit process and quality control arrangements

The [Code](#) applies to the audits covered by this report and is the fundamental document which defines the scope of the audit of public sector bodies in Scotland. The Code places specific expectations on auditors, in particular regarding the wider scope of public audit. This is most notable in the requirements to provide conclusions on the audit dimensions (financial sustainability, financial management, value for money, and governance and transparency alongside Best Value). The wider audit reporting requirements in the Scottish public sector differentiates this work from private sector audit and requires greater judgement from the auditor. It also puts more useful information in the public domain about the audit process and about performance of the bodies being audited.

### Organisation-wide audit quality arrangements

Audit Scotland and the appointed firms are responsible for their own organisation-wide arrangements for quality control in accordance with International Standard on Quality Control 1 and professional guidance. These arrangements focus on making continuous improvements to audit work by implementing a cycle of reviews, understanding why errors are made and sharing good practice.

Effective audit arrangements share some critical features. The specific arrangements vary slightly between financial, performance and Best Value auditing, but the main overarching components are explained below.

### Manuals and methodologies

All staff must comply with relevant manuals and methodologies and record all work on the appropriate corporate documentation system. Manuals and methodologies set out how to conduct the audit to ensure high compliance with auditing standards. These are regularly reviewed and updated to ensure they reflect changes in standards and continue to meet business requirements.

Financial audits share certain common features to ensure audit quality. They are designed to comply with International Standards on Auditing (UK) (ISAs (UK)), the International Standard on Quality Control 1 and the Code.

Performance audits, auditing Best Value, statutory reports (S102 or S22), sector overview reports, and reports in the 'How councils work' series share a common set of audit quality arrangements. These audits are designed to comply with Audit Scotland's Audit Management Framework or Auditing Best Value Manual rather than ISAs (UK). The Audit Management Framework is being revised to comply with International Organisation of Supreme Audit Institutions (INTOSAI) standards. The Audit Management Framework covers each key stage of an audit from project selection, audit design, fieldwork and reporting through to post-audit review and impact assessment.

### Review of work

More experienced members of the audit team review all the audit work of less experienced staff. This review process helps ensure that audit work achieves its objectives, judgements are appropriate, and work complies with the audit methodology and auditing standards. This type of review extends to all types of work including financial, performance and Best Value auditing. Reviews provide an opportunity to identify and correct any errors.

The Auditor General for Scotland, the Accounts Commission and the Controller of Audit also play a critical role in assuring the quality of performance audits and Best Value assurance reports. They are involved at the planning and reporting stages of audits to ensure that the audits are of high quality and meet their needs.

### Hot reviews

All auditors carry out a programme of reviews before the audit opinion is signed or the report issued, these are known as 'hot' reviews. Audit providers apply a variety of approaches using different criteria to select which audits are subject to hot review. Overall judgements, conclusions and the wording of the independent auditor's report are reviewed in a proportion of financial audits based on audit size, risk or likelihood of a modified opinion. Auditors' approaches to specific issues are reviewed across the population where a specific matter is considered to be high risk or to ensure that training has been successfully reflected in audit

work. Hot reviews are used to provide assurance that the judgements in the reports are appropriate and are supported by appropriate audit evidence.

### Cold reviews

Cold reviews are conducted after the completion of the audit and provide a higher level of assurance than hot reviews. They differ from hot reviews in that they cannot change the work in the event of any failure to comply with auditing standards. Cold reviews go into greater depth than hot reviews.

Auditors then carry out root cause analysis to better understand what led to failures to comply with auditing standards. This helps to identify what changes will best be able to prevent any recurrence of such failures and contributes to shared learning and ownership of audit quality.

AQA commissioned ICAS to carry out a fully independent programme of cold reviews. The programme includes samples of 2017/18 financial audits carried out by Audit Scotland auditors and firms, and on performance audits and Best Value assurance reports published in 2018. These independently conducted reviews provide the highest-level assurance on audit quality.

Assurance is also drawn from cold reviews carried out by audit providers where senior and appropriately experienced colleagues that have not been involved in the audits carry out a sample of reviews after audits have reported. The samples of financial audits reviewed ensure that all auditors that sign an opinion are reviewed at least once in a three-year cycle and cover all sectors and sizes of audit. The results are reported back to the teams that conducted the audit. The results also help to identify wider training needs and where audit manuals and methodologies can be improved.





The independence of the reviews is further strengthened within Audit Scotland by having reciprocal arrangements with other members of the UK public audit forum and by firms using staff from other UK offices. In the case of the appointed firms, the scoring from quality control reviews forms a part of the performance assessment of the engagement lead.



# Outputs

## Audit quality indicators

This section summarises the results of the audit quality review work carried out in accordance with the Audit Quality Framework. Where appropriate the Financial Reporting Council grading system has been applied.

Score	Standard	Description
1	 <b>Good</b>	No areas for improvement that warrant inclusion in the quality assurance report.
2a	 <b>Limited improvements required</b>	Limited concerns in a small number of areas identified. In such circumstances the auditor would adjust the audit approach in subsequent years' audits to address the issues raised.
2b	 <b>Improvements required</b>	A number of matters are reported but these are assessed as neither individually nor collectively significant. In such circumstances it is expected that the auditor would consider whether any remedial action is required in respect of the audit inspected and to amend procedures for subsequent audits.
3	 <b>Significant improvements required</b>	The reviewer has significant concerns in relation to the sufficiency or quality of evidence, or the appropriateness of key judgements, or the implications of other matters that are considered to be individually or collectively significant.  In such circumstances some remedial action may be requested to address the issues identified and to confirm that the audit opinion remained appropriate.

Source: Financial Reporting Council

This report includes results that are separately identified between audits carried out on behalf of the Auditor General for Scotland (AGS) and on behalf of the Accounts Commission (AC).

The cumulative reporting is important as it increases the sample size over the timeframe of the Audit Quality Framework and provides a better evidence base for conclusions to be made on the overall quality of auditors' work. The changes to the numbers of audits falling within each grading from year to year reflect a wide range of factors, which may include the size, complexity and risk of the individual audits selected for review and the scope of the individual reviews. For these reasons changes in the cold review results from one year to the next are not necessarily indicative of any overall change in audit quality and need to be considered in the context of other information available.



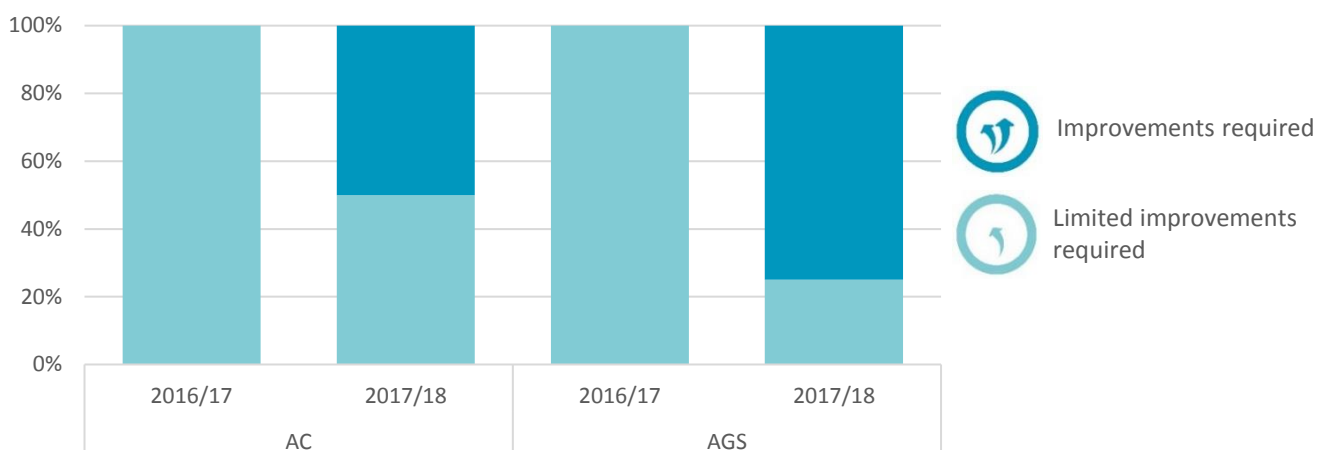
## Quality monitoring

### Cold reviews

#### Independent external reviews

Independent external assurance offers the highest level of assurance to stakeholders. ICAS reviewed five of the seven financial audit providers, and four performance audit and Best Value assurance reports over the last two years.

ICAS inspection results: financial audits

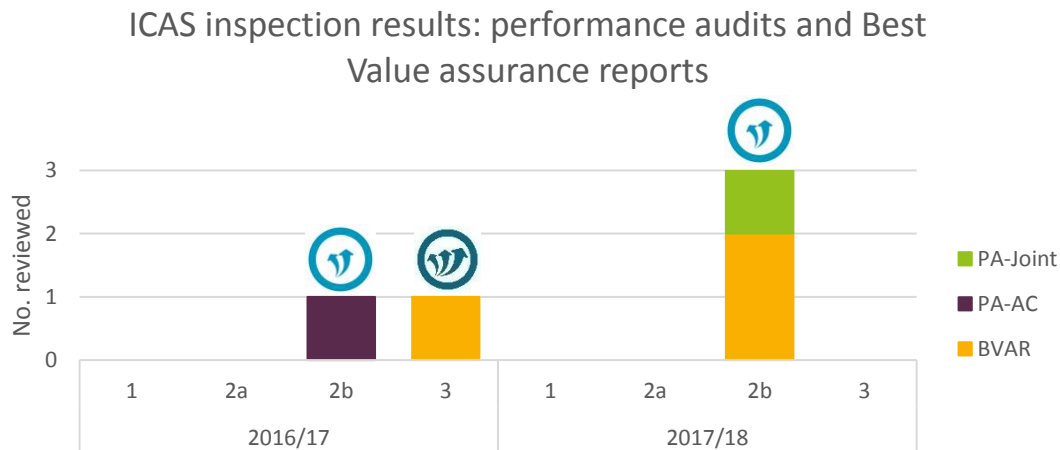


ICAS did not identify any concerns with audit opinions. Fifty-five per cent of the ICAS financial audit reviews over the last two years were graded as limited improvements required. Thirty-eight per cent of the 2017/18 financial audits were graded as limited improvements required compared to 100 per cent of 2016/17 financial audits. The remaining reviews were graded as improvements required.

This provides assurance that overall the audit work carried out on 2017/18 financial audits was of a high standard, supported key judgements and resulted in the correct audit opinions being issued.

ICAS identified specific areas for all auditors assessed to consider improving compliance with ISAs (UK). Two auditors had audits graded as improvements required in 2017/18. The principal reasons for the improvements required (2b) were the need to:

- improve documentation of the approach to selecting audit samples and the size of samples selected
- improve the way analytical procedures are used as substantive procedures
- widen consideration of areas where accounting estimates may arise during audit planning
- ensure that the use of analytical procedures to reduce sample sizes complies with the firm's sampling guidance.



The two Best Value assurance reports and one performance audit were assessed as improvements required (2b), while recognising the considerable improvements made since the two 2016/17 audits were reviewed. ICAS concerns were mainly about ISA (UK) compliance and identified this in particular as an area for future focus in performance and Best Value work.

ICAS provided the following comments on the audits that they reviewed:

**ICAS provided the following comments on the audits that they reviewed:**



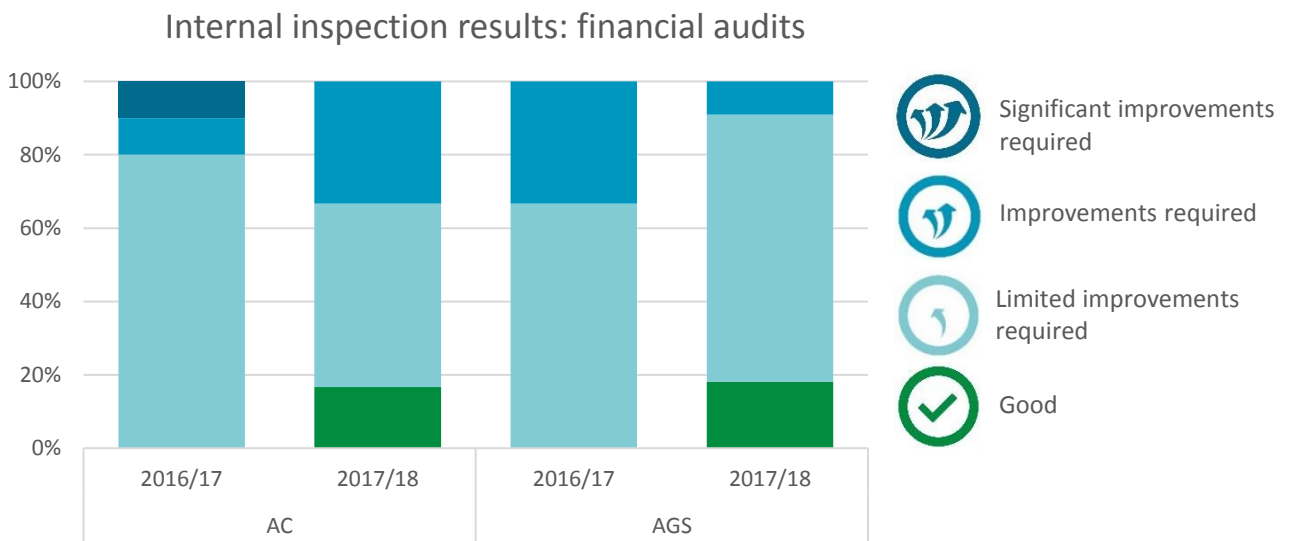
ICAS conducted a review of a large number of financial statement audit engagements. Some of these were assessed as being of an acceptable standard, where the planning sections were comprehensive and included a significant amount of information and background; the completion sections were found to be comprehensive; and financial statement disclosures were generally found to be well-presented. Whilst there were areas identified where audit evidence could have been improved, the majority of matters raised related to the documentation of work performed and considerations made. With regards other financial statement audits reviewed, whilst a number of positive points were noted on each file, there were file specific matters identified and, more pertinently, common underlying causes that would warrant focus going forward, including the documentation of audit sampling; and the performance of substantive analytical review.

On the performance audit reviewed there were no significant issues with regards compliance with the Audit Scotland Audit Management Framework, and the report was published within the prescribed timescale and no issues were identified with regards report publication. That being said, ISA issues were raised in relation to documented evidence of review and recording of work performed.

In the prior year ICAS reviewed a BVAR engagement and it was difficult to determine the nature, timing and extent of work performed in the majority of areas. There was improvement identified in the current year, particularly in relation to the linkage between the evidence gathering stage to scoping and reporting, and triangulation of evidence obtained. Again, however, ISA issues were raised, primarily in relation to documentation of work performed.

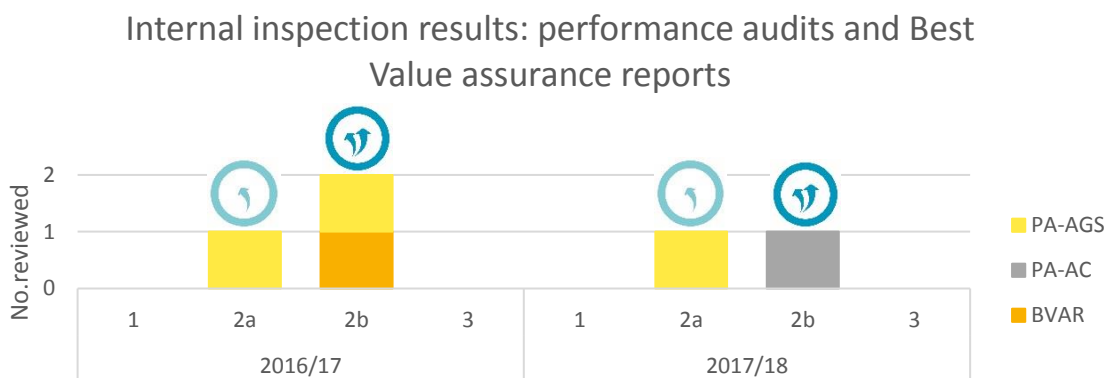
### Internal reviews conducted by Audit Scotland and appointed firms

Auditors reviewed 17 audits representing eight per cent of 2017/18 audits (19 audits representing eight per cent of 2016/17 audits).



Reviewers did not identify any concerns with audit opinions. Seventy-eight per cent of the internal financial audit reviews over the last two years were graded as limited improvements required. Eighty-two per cent of the 2017/18 financial audit were graded as limited improvements required compared to seventy-four per cent of 2016/17 financial audits. The remaining reviews were graded as improvements required.

Auditors carried out two internal cold reviews of performance audits, covering 11 per cent of performance audits published in 2017/18 (three audits representing 15 per cent of reports published in 2016/17). These were also scored using the Financial Reporting Council’s grading to provide comparability and more meaningful assurance.



Auditors are putting arrangements in place to address the findings from cold reviews. AQA will monitor how well the new arrangements improve audit quality.

### Financial Reporting Council

The Financial Reporting Council publishes [Thematic reviews](#) of audit quality. A thematic inspection on Other Information in Annual Reports concluded in December 2018 that the nature, extent and quality of the work performed by audit teams on the Other Information vary considerably. The review highlighted an absence of prescriptive requirements in Auditing Standards in this area. Despite the Financial Reporting Council’s review being based on private sector audit work, its findings are relevant to Scottish public sector audit which could be improved with further training on the importance of audit work on the narrative statements in the annual accounts.

## External and internal reviews and investigations

No appointed firms were subject to external investigations, eg by regulators, in relation to their public sector work. No Audit Scotland work or staff were subject to any external investigations.

AQA received three complaints relating to audit quality in 2018/19 and has not identified any significant shortfalls in audit quality to date. The approach to considering such complaints is still in development and the number of complaints is too small to draw wider conclusions about audit quality. It does however provide a basis for ensuring that matters are appropriately considered within the overall Audit Quality Framework.

## Hot reviews

The results of hot reviews carried out by audit providers gives further evidence of audit quality. These hot reviews are designed to meet the scope of Engagement Quality Control Reviews as set out in International Standard on Quality Control 1. Audit Scotland teams conducted six reviews covering three per cent of 2017/18 financial audits (compared to eight reviews covering six per cent of 2016/17) all of which were satisfactorily concluded. Deloitte and Mazars conducted hot reviews on all their audits. Grant Thornton conducted hot reviews on two of their audits because of their value and KPMG on one because it is a Public Interest Entity. The other appointed firms did not conduct any Engagement Quality Control Review scope reviews. Grant Thornton also reviewed one 2017/18 audit against their audit quality measures (two in 2016/17).

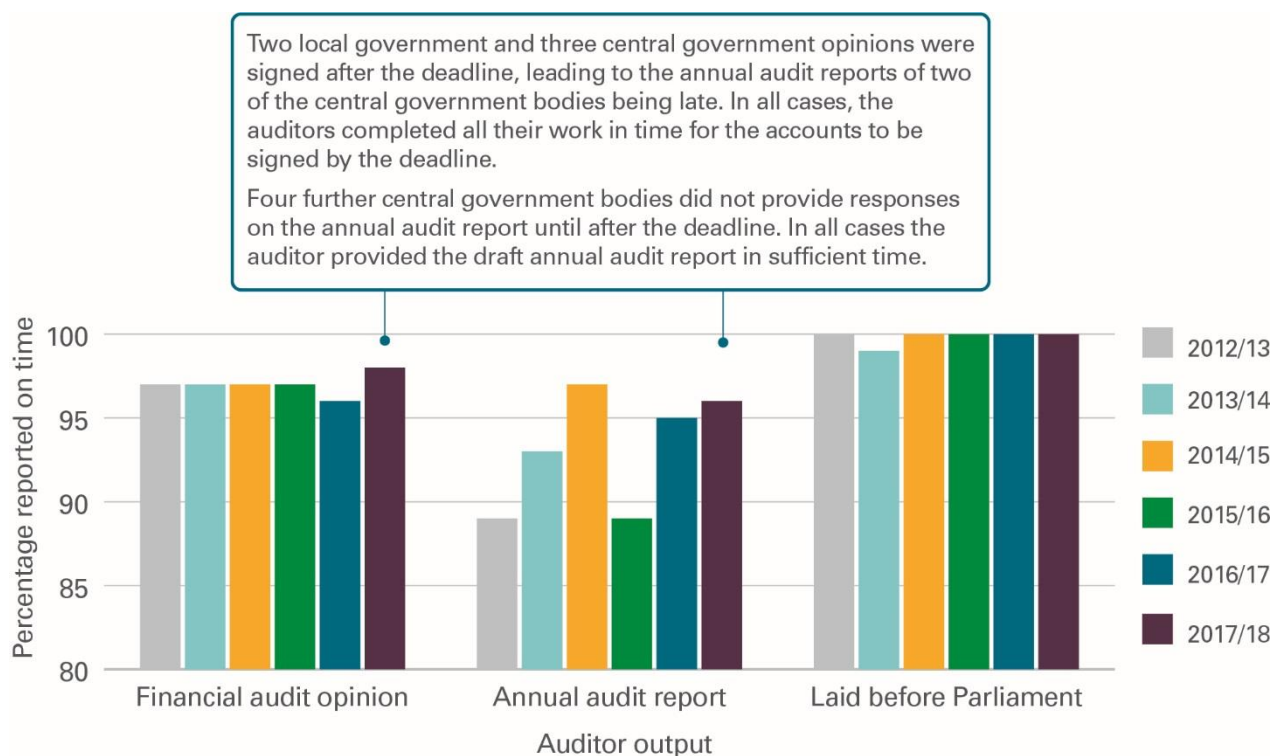
Performance Audit and Best Value staff not involved in the work reviewed all 11 performance audits and seven Best Value audits published in 2018/19. The reviews helped to shape the final reports and confirmed that the judgements were appropriate and supported by evidence.

## Reporting

### Timeliness of financial audit work on 2017/18 accounts

Audit Scotland sets deadlines for auditors to ensure that their financial audits are completed in a timely manner. The deadlines vary by sector. Audit opinions and annual audit report deadlines are 30 June for health, 30 September for local government, 31 October for central government and 31 December for further education. The accounts of all bodies other than local government must be laid in the Scottish Parliament. Legislation requires the accounts to be laid within nine months of the financial year end. This is 31 December for health and central government and 30 April for further education.

Audit Scotland expects auditors to do all they can to meet the deadlines but recognises that in some circumstances, events beyond their control can cause the deadlines to be missed. Auditors' performance in meeting the deadlines for 2017/18 audits with the previous five years for context is set out below.



### Modification of audit opinions

Modified audit opinions are issued where an auditor concludes that the accounts contain material misstatements, where significant expenditure has been incurred in breach of rules, or where reporting requirements have not been met.

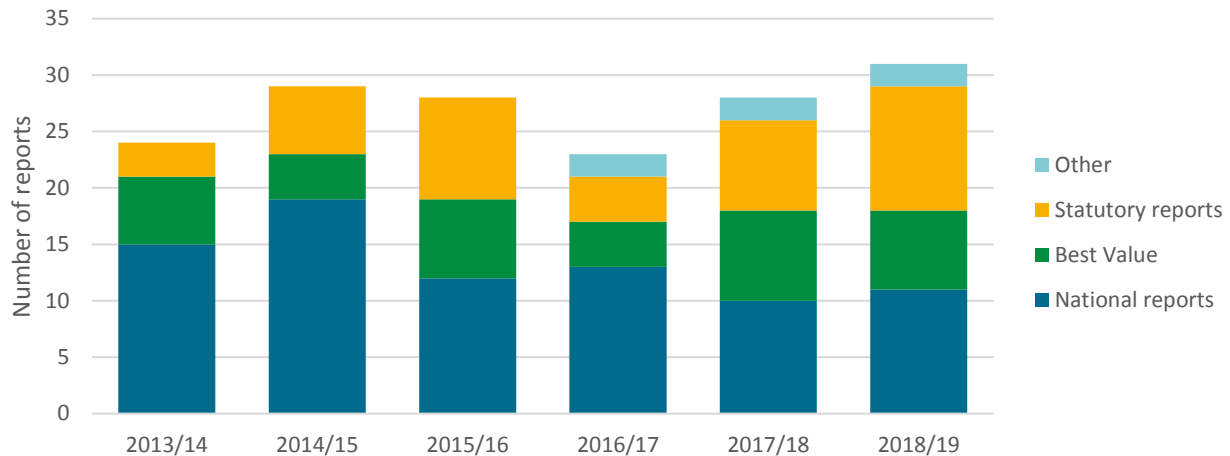
There were no modified audit opinions in 2017/18 (none in 2016/17). There were four instances where the auditor reported by exception (four in 2016/17). These were all where local government significant trading operations failed to achieve the statutory objective to break even over a three-year period.

### Publication of performance audit and other reports

The number of performance audit and other reports fluctuates over time. The Auditor General for Scotland and Accounts Commission have a five-year rolling work programme that covers a range of public sector bodies and services.

The Auditor General for Scotland writes statutory reports under Section 22 of the Public Finance and Accountability (Scotland) Act 2000 for laying in parliament and the Controller of Audit writes statutory reports under Section 102 of the Local Government (Scotland) Act 1973 to the Accounts Commission. The Auditor General for Scotland and the Controller of Audit may prepare reports where they identify matters that require reporting, and the Accounts Commission may require the Controller of Audit to report on specific matters.

Audit Scotland’s performance in delivering national performance audits, Best Value reports, statutory reports and other reports during 2017/18 with the previous five years for context is set out below.



Progress on delivery of the work programme is routinely reported to the Auditor General for Scotland and the Accounts Commission's Performance Audit Committee throughout the year. Any changes to planned publication dates are agreed with the Auditor General for Scotland and/or the Accounts Commission's Performance Audit Committee.

Ninety per cent of performance audits (including overview reports) and Best Value assurance reports (BVAR) were delivered in the planned quarter, compared to 75 per cent last year. Revised arrangements delivered a significant improvement in delivery against target deadlines.

### Annual audit reports and adding value

The Code recognises the increasingly high expectations the public has about the role of audit in the stewardship of public funds. It defines the wider scope of public audit as going beyond the financial statements to include work that contributes to audit judgements and conclusions on the appropriateness, effectiveness and impact of corporate governance and performance management arrangements and financial sustainability. In the local government sector, the audit of Best Value is central to auditor reporting on the audit dimensions.

AQA coordinated a programme of reviews of annual audit reports (AARs) to assess how effectively they were complying with the Code including this new area of audit judgement. The review found that there is now a high level of compliance with the Code requirements by all appointed auditors.

Auditors continue to improve compliance with the Code requirements in reporting on the wider audit dimensions of public audit in Scotland, all auditors are now making the mandatory ethical and independence disclosures in AARs and there is considerable improvement in auditor reporting on how they will add value in AARs.

### Audited bodies' views on audit work

MDCR surveyed 408 individuals in audited bodies about the 2017/18 financial audits they received and the performance audits, overview reports and Best Value assurance reports published in the past year and received 187 responses (46 per cent). Audited bodies were asked to respond to questions using a scale of 1 to 5 where 1 is 'very poor' and 5 is 'very good'. Audited bodies' aggregate views on the key questions on the annual audit are:

Question	Score
<b>Usefulness of the annual audit overall</b>	<b>4.1</b>
Usefulness of the annual audit in providing assurance	4.4
Performance of the audit team overall	4.3
The team's ability to challenge decisions and judgements	4.2
Usefulness of the annual audit report overall	3.9

Question	Score
Appropriate coverage of governance and accountability	4.2
Appropriate coverage of financial management	4.2
Appropriate coverage of financial sustainability	4.0
Appropriate coverage of value for money	3.8
Appropriate coverage of Best Value	3.8

Audited bodies expressed a high level of satisfaction with the usefulness of the annual audit, with a particular recognition of the assurance that audit provides.

Audited bodies' views on how much performance audits, Best Value assurance reports and overview reports help bodies to deliver improvement are also positive but not as strong as the annual audit. The results are analysed here:

	Auditor General CG, NHS, FE	Joint	Accounts Commission LG	Average
Performance audits	3.1	3.6	3.5	3.3
Best Value			3.4	3.4
Overviews	3.5		3.5	3.5

This is the first year of this set of survey questions. These will be monitored over time to assess how perception of audit changes over time. Audited bodies were offered an opportunity to comment on each question, and a representative sample of comments is included below.

On quality of the audit work:

- *What worked was the audit team starting from a position of a good understanding of our business - so their audit focused on relevant issues. The team were also understanding of the pressures on us and so accommodated our timescales well.*
- *The approach is generally about errors and recommending that we don't make them again in the future. There are very few examples of better/best practice provided as evidence or ideas for improvement.*

On the annual audit plans:

- *Generally, the team has an excellent understanding of the organisation and is technically able. However draft reports are presented late in the Committee process which does not give adequate time for considered responses. Information requests are also sometimes at very short notice.*
- *The composition of the team was not consistent, and this was problematic - affecting testing, communication and creating some duplication of work and effort.*

On the annual audit reports:

- *The audit report is well written and presented but it will always be a balance between the level of detail and making it accessible and readable; on balance the auditor does a good job in setting the balance.*



- *Easily interpreted by Board members. Again, distinction between compliance and best practice could be drawn better, particularly in relation to governance statement and performance report.*

On performance audits and Best Value assurance reports:

- *A detailed summary of recommendations / key recommendations at an early part of the reports would be useful. Otherwise reports are good.*
- *A lot of the report provided useful background and context to local government in Scotland - few however are directly relevant to drive improvement in other than the specific organisation they relate to. National reports are largely helpful contextually and rarely provide a focus for improvement.*
- *The reports I read are well written and provide clarity on complex issues.*
- *The use of infographics is useful and helps aid understanding of elected members. It was useful to have input into the consultation on future audit work as it was good to see comments and suggestions reflected in final plans.*

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# Areas for improvement and future focus

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The arrangements under the Audit Quality Framework provide evidence of the quality of 2017/18 financial and Best Value auditing and the 2018/19 performance audits. The evidence base continues to grow and comprises an assessment of compliance with the highest professional standards and the achievement of impact and other qualitative measures.

Auditors have made improvements since the 2017/18 Audit Quality Annual Report:

- raising the standard of audit documentation, especially for performance and best value work
- demonstrating more clearly how audit adds value
- ensuring mandatory ethical and independence disclosures are made in annual audit reports
- increasing focus on capital accounting by both auditors and audited bodies.
- improved the timeliness of publishing performance audit and Best Value reports.

Work carried out under the Audit Quality Framework has highlighted areas where further improvement may be possible to support the Auditor General for Scotland and Accounts Commission's drive towards world class audit. AQA will monitor improvement areas identified this year. The evidence will be used in discussion with all audit providers to focus on areas for improvement including:

- continued focus on raising the standard of audit documentation
- the use of analytical procedures
- the application of sampling methodology
- the importance of audit work on the narrative statements in the annual accounts
- continued implementation of the PABV decision to comply with ISAs (UK) and the International Organisation of Supreme Audit Institutions (INTOSAI) auditing standards for performance audits
- considering action necessary to address staff views on the time and resources available to deliver high quality audit.

Public expectations about audit quality have developed rapidly since the Audit Quality Framework was introduced in 2017. In 2019/20 development is planned to refresh the Audit Quality Framework and key performance indicators. Other developments will include:

- enhancing stakeholder feedback arrangements
- reviewing the structure and transparency of audit quality reporting.

# Quality of public audit in Scotland

## Annual report 2018/19

This report is available in PDF and RTF formats,  
along with a podcast summary at:

[www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk) 

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