

Transparency and quality

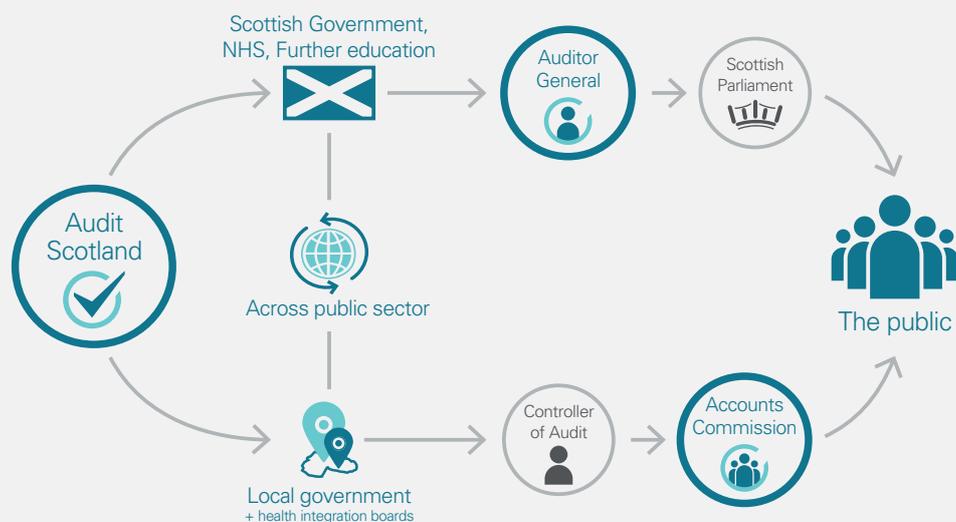
Annual report 2015/16



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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Key messages

1. Audit Scotland's Corporate Plan guiding principles include operating to the highest ethical and professional standards and maximising the value of audit. Our Quality Framework continues to provide an effective principle-led structure for our quality control and quality monitoring activities. We revised the framework last year to reflect international initiatives on the quality of audit.

2. Overall, the arrangements in place and activity for the year provide assurance that Audit Scotland and the appointed firms continue to provide the Auditor General and the Accounts Commission with quality work in accordance with their expectations.

3. In particular, the quality appraisal work carried out by Audit Strategy on the work of the firms and Audit Services Group has confirmed that each auditor:

- understands and complies with the ethical standards in force during the course of the audit and is independent of the audited body
- has the required professional competence to carry out the audit in accordance with relevant standards and the Code of audit practice
- operates in a regulatory environment that actively oversees auditors
- has delivered audit opinions that can be relied upon
- delivered reports on time and that have met the needs of most of their intended readers.

4. We are satisfied that the audit work performed by Audit Services Group, Performance Audit and Best Value and the firms satisfy the International Audit and Assurance Standards Board (IAASB) definition of a quality audit ([paragraph 27](#)).

5. The new Code of audit practice, issued in May 2016, applies from the 2016/17 audits. It raises the expectations on auditors, in particular to provide conclusions on the wider scope areas of public sector audit and a changing approach to Best Value audit. We have secured the appointment of high-quality audit firms at a reduced cost through a competitive tendering exercise.

6. The quality control arrangements in place across Audit Scotland continue to develop and help us attain our vision of being a world-class audit organisation. We are revising all aspects of these arrangements in the context of greater expectations and reduced cost to:

- ensure we can provide appropriate assurance to the Accounts Commission and Auditor General
- improve the quality of public audit.

7. The report demonstrates that arrangements across Audit Scotland's business groups are continuing to develop, with the aim of ensuring that the quality monitoring framework remains effective.



Corporate plan
2016/17 update

📄 May 2016



Code of audit
practice 2016

📄 May 2016

Introduction

Public bodies audited



77



Central government bodies and Scottish Parliament
(including police, fire, Scottish Water)

23



NHS bodies

32



Councils

74



Joint boards and committees
(including 30 health integration boards)

21



Further education colleges

227 Public bodies audited

8. Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively. We do this by carrying out financial, performance and Best Value audits across the public sector in Scotland. In carrying out this work we seek to be transparent in our governance and operations and to produce consistent, high-quality audits.

9. The Auditor General audits or appoints the external auditor of most public bodies in Scotland, except for local authorities and integration joint boards where the Accounts Commission is responsible for securing audits. Public audit in Scotland covers 227 public organisations and includes the Scottish Government, the NHS in Scotland and local councils. These organisations spend over £40 billion of public money every year.

10. Our Quality Framework sets out the high-level principles we apply to our work to ensure its quality. We updated it in 2015 to take account of a number of national and international initiatives and publications. These include the IAASB [A Framework for Audit Quality](#) (February 2014) and the Financial Reporting Council's [Professional Scepticism](#) (March 2012). This Transparency and Quality Report meets the Framework's requirement to report annually in line with best practice.

11. This report combines information on:

- the overall structure and governance of Audit Scotland (transparency)
- the arrangements in place for producing high quality work by Audit Scotland and the appointed firms, in the services provided to the Auditor General and the Accounts Commission (quality).



Transparency

How we work

Our vision and the principles that guide our work

12. Our Corporate Plan sets out our vision to be a world-class audit organisation that improves the use of public money. It sets out that we exist to provide independent assurance to the people of Scotland that public money is spent properly and provides value for money.



Corporate plan
2016/17 update

📄 May 2016

The principles that guide our work

13. Audit is at the heart of the work carried out by Audit Scotland staff. The principles that guide our current work are set out in the 2011 *Code of audit practice*:



Code of audit
practice

📄 May 2011

- Auditors are independent of the organisations that they audit.
- Public audit is wide in scope to reflect the accountabilities attached to the use of public money.
- Audits are based on comprehensive risk assessment.
- Reports are made public.
- Auditors work in partnership with each other.
- Auditors work collaboratively with other scrutiny bodies.
- Auditors work as catalysts to help public bodies improve their performance.
- Audits are carried out to a high standard using skilled and experienced staff.
- Audits are informed by assessment of costs and benefits and achievement of Best Value or value for money.
- Auditors balance confidentiality and information security with public accountability and freedom of information.

14. We published a new Code of audit practice that will apply the financial audits of 2016/17 to 2020/21. This report covers work on the 2014/15 audits, so the existing Code applies to the work described in this report.



Code of audit
practice 2016

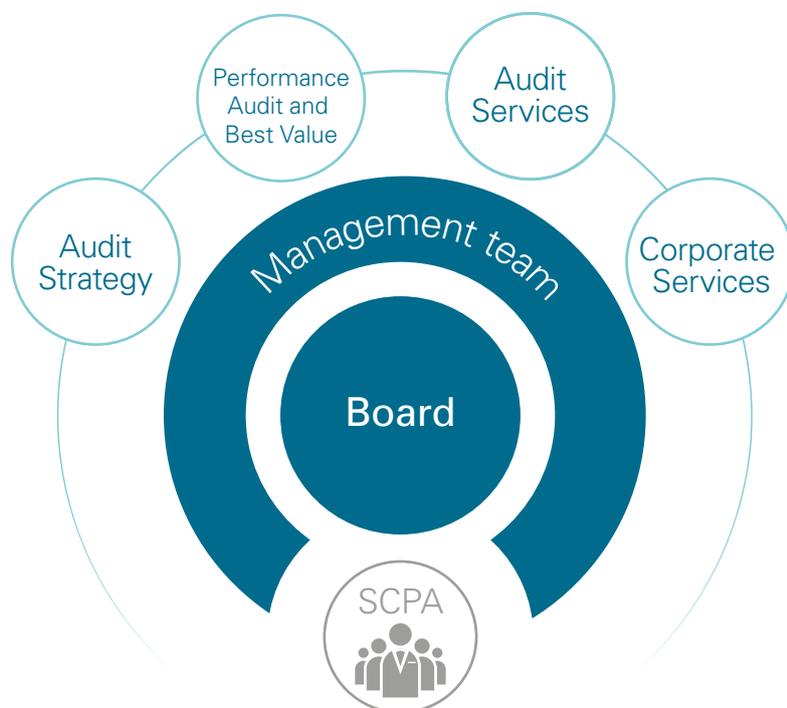
📄 May 2016

Our governance arrangements and operational structure

Governance

15. Governance is about the processes for making and implementing decisions. We expect high standards of governance from the organisations we audit and we set high standards for our own governance. We believe that a world-class organisation requires world-class governance arrangements.

16. The Audit Scotland Board is responsible for all Audit Scotland's functions. It exercises its powers and authorities through a Scheme of Delegation, which it determines and approves. The board consists 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 (SCPA), a commission of the Scottish Parliament.



17. The board has two standing committees:

- **The Audit Committee** oversees the arrangements for internal control, risk and corporate governance, internal and external audit, the annual accounts and the Standing Orders, Financial Regulations and Scheme of Delegation.

- **The Remuneration and Human Resources Committee** oversees the arrangements for salaries and terms and conditions of staff and other HR matters.

18. The board members during 2015/16 were as follows:

- An independent chair, Ian Leitch from October 2015. John Maclean was our independent chair until September 2015. Two independent non-executive members, Heather Logan and Russel Griggs (from October 2015).
- The Auditor General, Caroline Gardner who is also the Accountable Officer for Audit Scotland. She was appointed by the Crown for a single fixed-term of eight years from 1 July 2012.
- The chair of the Accounts Commission, Douglas Sinclair. The Accounts Commission is responsible for securing local authority audits and is independent of local government. Scottish Ministers appoint the chair and Commission members.

19. Our governance arrangements provide effective governance of Audit Scotland while preserving the independence of the Auditor General and the Accounts Commission in their statutory roles. All the audit judgements in the reports we publish for the Auditor General, the Accounts Commission, the Controller of Audit and appointed auditors are independent.

20. A management team oversees our day-to-day operations. The members at 31 March 2016 were as follows:

- Caroline Gardner, Auditor General for Scotland and Accountable Officer.
- Diane McGiffen, Chief Operating Officer, chairs management team meetings and is responsible for our internal operations and business performance.
- Russell Frith, Assistant Auditor General, is responsible for the external strategic and development work of financial audit, auditing and accounting standards, technical support and quality assurance. He acts as Audit Scotland's Ethics Partner.
- Fraser McKinlay, Director of Performance Audit and Best Value and Controller of Audit, manages a team that is responsible for carrying out performance and Best Value audits.
- Fiona Kordiak, Director of Audit Services, is responsible for the in-house audit services we provide to the health service, central and local government. She acts as our Ethical Compliance Partner.

Our operational structure

21. Our operational structure is based around four main business groups:



Audit Services

Audit Services Group (ASG) is responsible for carrying out audits of public bodies falling within the remit of the Auditor General and the Accounts Commission on a five-year appointment cycle.



Performance audit and Best Value

Performance audit and Best Value is responsible for providing a range of audits to the Auditor General and the Accounts Commission. These include a programme of performance audits, Best Value (BV) audits of local authorities, audits of Community Planning Partnership (CPP), preparing statutory reports (S102 or S22), sector overview reports and scrutiny improvement activity (including shared risk assessments).



Audit Strategy

Audit Strategy is responsible for audit procurement, technical guidance and support, reviewing and reporting on audit quality, coordinating the National Fraud Initiative exercise in Scotland and conducting benefits performance audits of local government.



Corporate Services

Corporate Services is responsible for supporting Audit Scotland's principal functions with communications and media, finance, information services, human resources and organisational development, facilities management and business support.

22. The Auditor General and the Accounts Commission appoint the external auditors of public bodies in Scotland for periods of five years. The current appointments end when the 2015/16 audits are completed. Appointments to carry out annual audits are split between ASG staff and seven private firms. The private firms carry out just over a third of these audits by value. You can find the appointments and annual audit reports on our [website](#) .

23. Performance and Best Value audits are generally carried out by our staff with assistance from appointed auditors or external experts, where appropriate. These audits are [published on our website](#) .

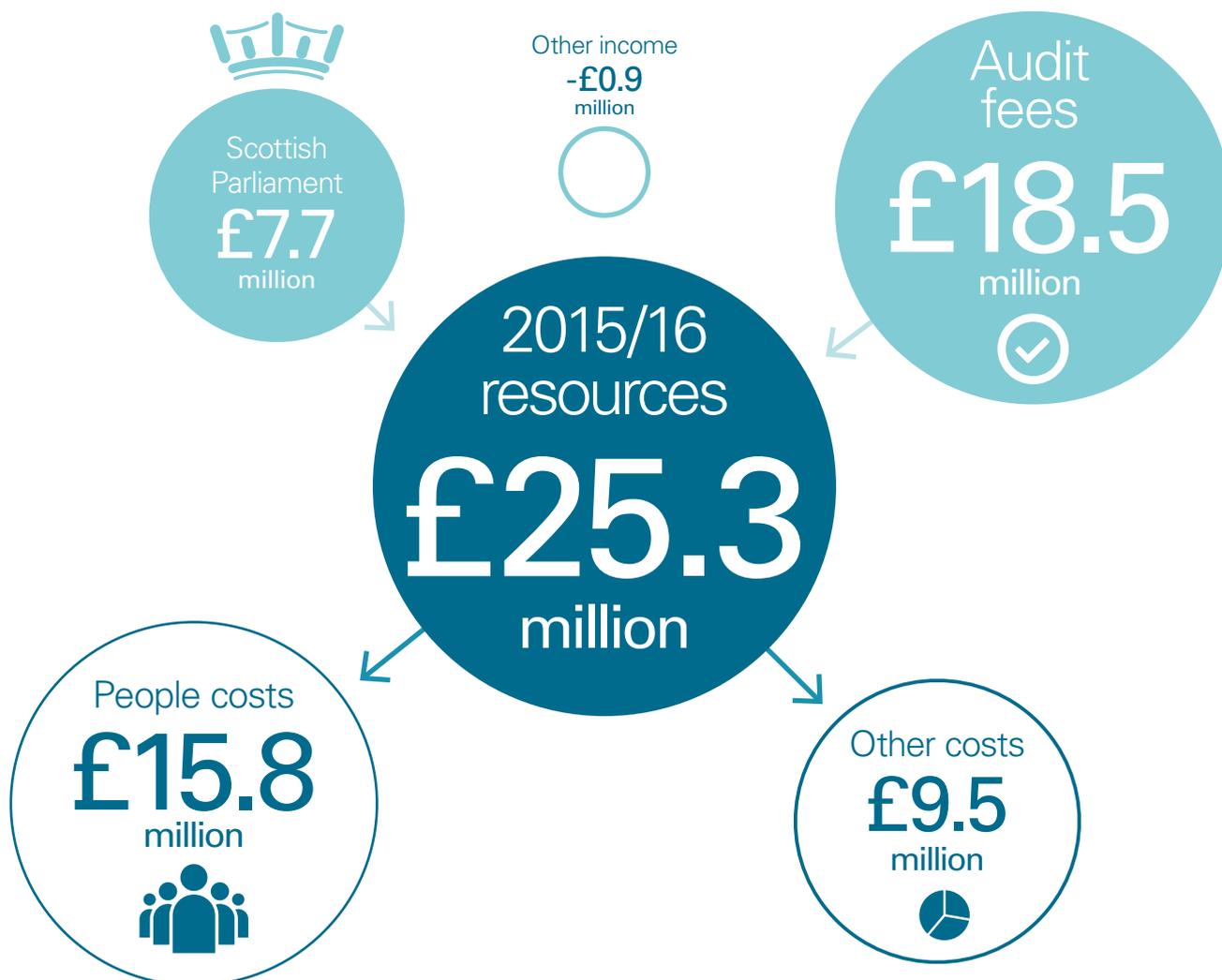
24. We have a workforce of 273 whole-time equivalent staff, over half of whom are in ASG. Staff are mostly based at offices in Edinburgh, Glasgow and Inverness.

Our finances

25. We meet our costs from a combination of audit charges to public bodies and funding from the Scottish Parliament through the annual Budget Act. We set audit fees to recover the costs of local audit work and, where appropriate, a contribution to other audit and support costs. We are reviewing our approach to funding and fee setting to ensure that it meets our business needs and is clear and understandable to audited bodies and stakeholders.

26. Our spending and use of resources are examined by the SCPA. This is a statutory body comprising five MSPs that reports to Parliament and appoints external auditors for Audit Scotland.

Income and expenditure 2015/16 (£ millions)



Quality

The components of a quality audit

27. The [International Audit and Assurance Standards Board \(IAASB\)](#)  sets out five elements of a quality audit. In keeping with our vision to be a world-class audit organisation, our Quality Framework takes account of these five elements. These are listed in the IAASB's [A Framework for Audit Quality](#) . It states that:

A quality audit is likely to have been achieved by an engagement team that:

-  exhibited appropriate values, ethics and attitudes

-  was sufficiently knowledgeable, skilled, and experienced and had sufficient time allocated to perform the audit work

-  applied a rigorous audit process and quality control procedures that complied with law, regulation and applicable standards

-  provided useful and timely reports

-  interacted appropriately with relevant stakeholders.

28. Our Quality Framework sets out how these important components are relevant to Audit Scotland's work. Our quality appraisal activities include sending audit quality surveys to audited bodies for feedback every other year. They include internal or peer reviews of our work. These activities provide assurance on the quality audit criteria. The rest of this report describes how we demonstrate these elements across our business groups through:

- the quality control arrangements we have put in place
- the results of quality assurance activities during the year.

Quality arrangements

29. Our Corporate Plan confirms our commitment to operate to the highest ethical and professional standards and our aim to maximise the value of the audit and support improvement. This commitment is central to our Quality Framework, which sets out the following principles:

- Quality is the responsibility of everyone in Audit Scotland.
- Our approach to quality will drive continuous improvement across Audit Scotland.
- Quality will be assessed in terms of outputs, outcomes and impact, as well as inputs and processes.



30. Getting it right first time is fundamental to Audit Scotland being a high-quality, efficient and effective audit organisation. It requires us to make quality central to all our thinking, our processes and our activities. All our staff have a responsibility to get it right first time, and need to demonstrate a commitment to quality in everything they do.

31. Auditors' independence from the bodies they audit is an essential element of high quality audit. We have a rigorous process to ensure that our auditors comply with the Financial Reporting Council's [Ethical Standards](#)  to avoid any actual or perceived conflicts of interest. We consider potential conflicts of interest when making recommendations for appointment, and also when approving non-audit work as described in [paragraph 53](#).

32. All staff are personally responsible for declaring any potential conflicts by completing annual Fit and Proper forms. As part of this process they must confirm they have read relevant policy documents and are up to date with their professional training. As an organisation we use their responses to put in place any necessary safeguards, such as removing someone from an audit.

33. Quality control refers to quality management during an audit. It may involve peer review and in some cases external input. Quality control has four principal characteristics:

- Regular internal review of work by more senior staff.
- Regular internal challenge sessions.
- Formally assessing how auditing complies with local quality processes.
- Proportionate quality control activities to both maximise the quality and efficiency of work and make sure staff retain a sense of ownership.

34. Quality monitoring ensures that systems of quality control are operating well and that all audit work is reviewed and lessons are learned and used to improve processes. The sections below, on quality arrangements and results of quality control, describe our quality control and quality monitoring activities.

35. All parts of Audit Scotland have distinct responsibilities for the main strands of audit quality.

Audit quality



Board

Setting the tone at the top
Quality framework



Audit Strategy

Oversight of quality arrangements
Surveys of audited bodies
Monitoring of firms' arrangements



Business groups and firms

Quality control arrangements
Quality monitoring of audits



Audit leads

Quality control of individual audits

36. The Audit Strategy Group is independent of auditors. It is responsible for overseeing quality assurance arrangements of all audit work and providing assurance to the Auditor General for Scotland and the Accounts Commission in accordance with the framework approved by the Board.

37. Business groups are responsible for establishing the quality arrangements for their activities, including the processes for getting it right first time, quality control and quality monitoring. Relevant documents are available to staff on our intranet.

38. The Corporate Quality Group, with representatives from each business group, helps to maintain the Quality Framework and to prepare this Transparency and Quality Report. It coordinates and shares best practice in quality monitoring and supports each business group's quality control and monitoring procedures, for example by offering advice or sharing best practice. The appendix to this report details these arrangements.

39. The following sections of the report outline the results of quality control and monitoring activity during 2015/16 and developments in audit quality arrangements taking place in each business group. We are satisfied that the internal quality control systems described in more detail in the appendix are operating effectively.

Sources of quality assurance

40. Information from various sources is combined to provide reasonable assurance on the quality of audit work. The sources include internal arrangements, and both internal and external checks. These are set out below on the basis of the Quality Framework. Assurance arrangements are set out for the two principal business groups [ASG \(page 24\)](#) and [PABV \(page 29\)](#). The [Appendix: Quality arrangements \(page 34\)](#) provides further details.



Getting it right first time

- Audit methodology manuals
- Audit management frameworks (AMFs)
- Audit software and standard documentation
- Training for auditors



Quality control

- Management review of all audit work
- Internal peer reviews of sample audits before the audits are completed



Internal quality monitoring

- Internal inspection of compliance on a sample of completed audits (cold reviews)
- Examinations of high-risk themes
- Lessons learned from internal reviews



External quality monitoring

- External inspection on a sample of completed audits or reports
- Independent external evaluations of new audit approaches and audit outputs (for example SRA, BV2, Police and Fire BV audit work)
- Feedback from audit recipients
- Professional institute regulation

Results of quality assurance activity

41. This section of the report covers the quality appraisal work undertaken by the Audit Strategy Group across appointed auditors. The subsequent sections cover the work of the Audit Services Group and Performance Audit and Best Value Group in a similar way to that for a private sector audit firm.

Audit Strategy work on appointed auditors

42. Audit Strategy's principal quality appraisal work covers all appointed auditors and focuses on the public sector audits to which they are appointed. The same level of scrutiny is applied to Audit Services Group and the firms. This provides the assurance specific to the appointed audits, and also provides assurance on the wider scope of public sector audit carried out in accordance with the Code of audit practice.

43. The work on the appointed firms also relies on the system of statutory regulation and oversight that is in place for the audit profession. This consists primarily of the activities of the Financial Reporting Council, and the professional bodies of accountants that audit firms are registered with. Examples are the [Institute of Chartered Accountants of England and Wales](#) and the [Institute of Chartered Accountants of Scotland \(ICAS\)](#). This provides a good level of assurance about the firm-wide arrangements that our appointed firms have for ISA compliance.

Output monitoring

44. Audit Strategy monitors the delivery of principal outputs by auditors to confirm that the year's work is complete. Auditors' performance in meeting the deadlines for 2014/15 audits is set out below.

	Local government	Health	Central government	Further education
Audit opinion on time	77/77 (100%) 30 Sept 15	23/23 (100%) 30 June 15	71/74 (96%) 31 Oct 15	19/21 (90%) 31 Dec 15
Annual audit report on time	77/77 (100%) 31 Oct 15	23/23 (100%) 31 July 15	71/74 (96%) 30 Nov 15	19/21 (90%) 31 Dec 15
Accounts sent for laying on time	N/A	23/23 (100%) 31 Dec 15	74/74 (100%) 31 Dec 15	21/21 (100%) 30 April 16

45. Under central government, annual audit reports that auditors issued late were caused by delays in clearing the final report. Delays in further education were related to work by the auditor in support of Section 22 reports. These are reports that the Auditor General makes to parliament if concerns or issues have been raised in the audit of a public body she is responsible for.

Review of audit outputs

46. A sample of 71 annual audit reports from 2014/15 (compared to 62 the previous year) were reviewed for compliance with the Code of audit practice and the quality of their reporting. The review covered all sectors and all audit providers.

47. The reviews found that reports complied with the Code on the whole and all auditors had increased the quality of their reporting after the issue of a compliance checklist last year. Examples of good practice and areas for improvement were reported to auditors in March 2015.

Audit service quality surveys

48. Audit Strategy issued audit service quality surveys to 34 local government bodies and 59 central government bodies asking for feedback on the 2014/15 audits. Response rates were 82 per cent and 56 per cent respectively.

49. The key indicators are:

- what audited bodies thought of the quality of service provided by the auditors
- whether the audit had made an impact on the bodies in the four areas defined in Audit Scotland's corporate impact framework
- whether relevant national performance reports had an impact on the body.

50. A summary of their responses is shown on [page 19](#). The feedback was positive in terms of the quality of audit service delivered and the overall impact of audit work. The impact of national performance reports is reported in more detail in [paragraphs 97–99](#).

		Local government % positive responses	Central government % positive responses
Overall quality of service		95	100
Overall audit impact	(Finance directors)	100	97
	(Audit Committee chairs)	100	94
Impact of audit on:			
Financial sustainability		81	60
Transparent reporting of financial and other performance		86	80
Value for money		62	62
Governance and financial management		86	80

Auditors' own quality control results

51. Firms carried out six quality control inspections relating to public sector audits procured for the Auditor General or Accounts Commission. Audit Services Group carried out quality control inspections as detailed in [paragraph 76](#). All reports concluded that the audits inspected complied with ISAs in all material respects and identified areas for improvement.

Thematic work

52. Auditors' opinions of 2014/15 audits were reviewed to follow up the review of the previous year. Auditors' compliance with the model auditor's opinions had improved, but auditors were shown where they could better tailor the wording to reflect the body being audited.

Oversight of acceptance of non-audit work

53. A small number of requests for non-audit work during 2015/16 were approved. Non-audit work can create actual or perceived threats to the independence of the auditor, and the FRC's Ethical Standards set out the principles that auditors must follow to avoid such threats. The requests were assessed against current Ethical Standards to ensure that the work would not compromise the external auditors' independence. The firms' designated Ethics teams reviewed all proposals and confirmed they did not consider them to pose any threats to the auditor's independence.

Respond proportionately to complaints about auditors and audit work

54. We operate a complaints handling process that conforms to the complaint-handling procedures set out by the Scottish Public Services Ombudsman. We systematically analyse and investigate complaints and report to our management team and the board. We received no complaints by audited bodies about the quality of auditors' work this year. One external complaint about an auditor's work was received. This was independently reviewed and found to be of an appropriate quality. The complaint was therefore not upheld. This is an important element of the overall assurance on the quality of auditors' work.

How we considered conflicting audit judgements between auditors

55. One conflicting judgement between auditors this year led to different audit opinions being given. This difference related to local government charities with missing governing documents. One firm modified their conclusion on accounting records. A meeting of auditors from this sector was held to discuss how to treat local government charities with missing governing documents. The aim was to reach a consensus on whether these circumstances warrant a modified opinion.

56. The Technical Services Unit (TSU) issues guidance on technical matters to help auditors in reaching judgements. In addition, Audit Scotland has hosted regular sectorial meetings and technical forums during the year involving auditors from each of the four sectors. At these, emerging or contentious technical issues were discussed. With the forthcoming change of most audit appointments for 2016/17 the TSU will be paying particular attention to the risk of inconsistent judgements being made.

Financial Reporting Council Audit Quality Review Reports

57. The Financial Reporting Council's Audit Quality Review team (AQR) issued one public report in February 2015 and three in May 2015 on firms that perform audits for the Accounts Commission and the Auditor General:

[!\[\]\(0fc5900959ab10acc878f9ca1e00fe37_img.jpg\) PricewaterhouseCoopers](#)

[!\[\]\(fe5d33c08faf9a42a148630afb19375e_img.jpg\) Deloitte](#)

[!\[\]\(2e39534fa484c54b999a1fc9c8a46d5a_img.jpg\) KPMG](#)

[!\[\]\(82ace3c1cdce20e5f8670b9f0a4207cd_img.jpg\) Grant Thornton](#)

58. The reports cover the firm-wide systems, policies and processes for ensuring audit quality, and a sample of their audits of public interest entities. This is to monitor firms' compliance with Auditing Standards, Ethical Standards and Quality Control Standards. The FRC also produced an annual report summarising all of its inspection work, bringing together common findings and examples of good practice.

59. The four firms' public reports show a better combined performance when compared to the sample of firms inspected by the AQR team:

- 70 per cent of the audits sampled were assessed as good with limited improvements required (compared to 60 per cent for all those sampled by the FRC)
- 21 per cent were acceptable overall with improvements required (29 per cent)
- 9 per cent required significant improvement (11 per cent).

60. The results are broadly consistent with the previous year.

61. Audit Strategy reviews the annual transparency reports published by the five largest firms that provide external audit work for the Auditor General and the Accounts Commission. This is to ensure the information in them is consistent with our understanding of quality arrangements within these firms. The FRC's AQR team also reviews the firms' transparency reports during its audit inspections. The transparency reports and the FRC's findings do not identify any areas for concern.

ICAS Audit Monitoring

62. Three appointed firms outwith the AQR inspection scope are registered by ICAS to carry out audit work and are within its audit monitoring responsibilities. They are Scott-Moncrieff, Wylie & Bisset and Henderson Loggie. ICAS's [Annual Audit Monitoring Report for 2014](#)  provides indirect assurance about compliance by these firms with auditing standards.

Developments in audit quality

63. Audit Strategy has developed quality reporting to auditors by increasingly issuing draft findings to confirm factual accuracy, where appropriate, to ensure findings are robust. Firms bidding for the tender for 2016/17 to 2020/21 audits were invited to share ideas for how they would demonstrate the difference that their audit work makes. The quality appraisal framework will be further developed during the coming year to maximise improvements in audit quality.

64. The new Code of audit practice, issued in May 2016, applies to the 2016/17 audits. It raises the expectations on auditors, in particular to provide conclusions on the wider scope areas of public sector audit and a changing approach to Best Value audit. The appointments of high-quality audit firms have been secured at a reduced cost through a competitive tendering exercise.

65. The quality control arrangements in place across Audit Scotland continue to develop and help us attain our vision of being a world-class audit organisation. We are revising all aspects of these arrangements in the context of greater expectations and reduced cost to:

- ensure we can provide appropriate assurance to the Accounts Commission and Auditor General
- improve the quality of public audit.

66. The revision will include considering and revising the:

- extent of external review of auditors' work (in-house teams and private firms)
- approach to monitoring wider scope audit work
- approach to obtaining audited body and other stakeholder feedback on quality of audit work
- reporting of quality monitoring work within Audit Scotland and to the Auditor General and Accounts Commission.

Audit Services Group

Our approach and development of audit quality

67. Becoming World Class. At the heart of our ambition to demonstrate we are a world-class provider of audit services is an emphasis on audit quality. We are committed to continuous improvement and treat external review as an important source of improvement. Last year ASG integrated professional standards development and quality work by creating the Professional Standards and Quality Improvement group (PSQI). The audit approach, quality reviews and training are now interdependent.

68. ASG recognises the need to continue to achieve further audit efficiency and the risk this might pose to audit quality. This places further emphasis on the quality processes and assurance procedures that exist in ASG.

69. A more extensive programme of quality reviews was performed this year than in previous years. Ten audits went through internal reviews and six went through external ICAS review. One audit went through both processes. This has resulted in better understanding than ever before of the challenges and how to overcome them.

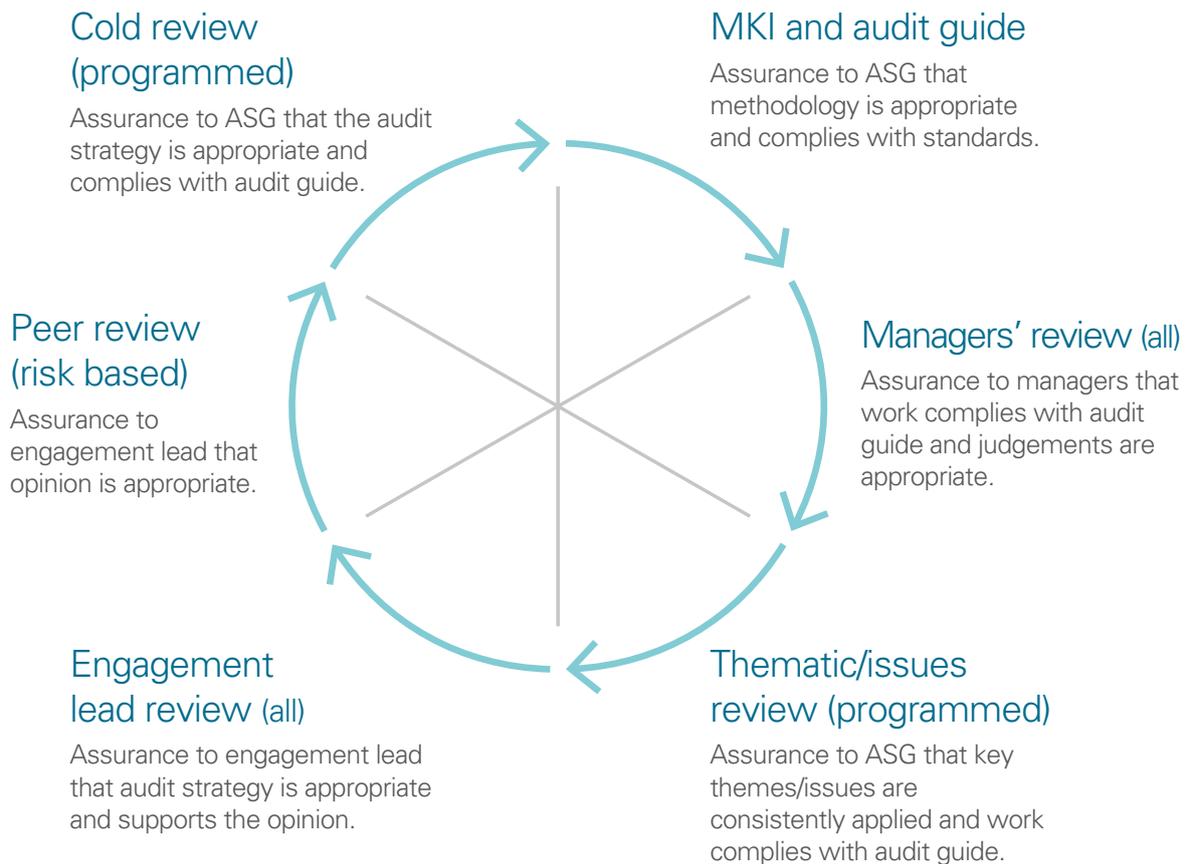
70. ASG's audit approach is closely aligned with [International Standards on Auditing \(ISA\)](#)  and reflects the structure and terminology of this framework: a key aspect of getting it right first time. This was an important objective of the streamlining activity and the work of the PSQI group in Audit Services in recent years. This can be seen in feedback from the ICAS review, which makes fewer recommendations about the audit approach than in previous years.

71. However, the challenge is now to consistently apply the methodology to achieve a high quality in audit work across Audit Services. This concerns behaviours and attitudes and will continue the programme, which started last year, of staff training and development of auditing knowledge. This included additional training events for all staff in smaller groups on specific areas of concern

72. The quality management processes are fully documented in the audit guide in the electronic working papers package, MKI, which is used for all audits. The appendix expands on these arrangements



Audit Services Group



Thematic reviews

73. ASG responded to Audit Strategy's thematic review of auditors' opinions and will address the points highlighted by Audit Strategy about individual audits. The lack of systemic issues identified provided assurance about the methodology.

Engagement lead reviews

74. All audits received engagement lead reviews, which confirmed that the audits had been carried out in accordance with the audit guide and quality arrangements.

Peer reviews

75. Eight peer reviews of 2014/15 audits were completed as part of the planned coverage. These confirmed that identified risks, judgements and audit opinions were appropriate.

Number of peer reviews planned or delivered each audit year

	2012/13	2013/14	2014/15	2015/16
	10	9	8	9

Cold reviews

76. Ten cold reviews of 2014/15 audits were completed, using the revised cold review programme.

Number of cold reviews planned or delivered each year (audit years)

	2011/12	2012/13	2013/14	2014/15	2015/16
ASG reviews	8	4	8	10	10 planned
ICAS reviews	-	6	-	6	-

77. Two of the reviews were performed by the Northern Ireland Audit Office and Wales Audit Office. This includes a reciprocal arrangement where ASG provide quality reviews for those organisations.

78. The reviews confirmed compliance with auditing standards and identified areas for improvement including that we should:

- be clearer at the planning stage of each audit about the proposed audit approach, including being clearer about the extent and focus of how we test financial controls and the importance of this work to our audit of the financial statements
- be clearer about how we intend to use internal audit's work on financial controls in each audit
- better explain our justification for selecting samples and identify what our testing covers
- ensure we record sufficient audit evidence in our electronic working papers package to back-up all audit judgements

- ensure that the file review processes that lead auditors and managers perform is thorough, prompt and challenges shortcomings in evidence, justification and judgements.

79. The ICAS quality monitoring team is currently completing its third twice-yearly assessment, covering the 2014/15 audit year. The scope of their work was to:

- inspect a sample of six completed audits to assess the quality of audit work and compliance with the ISAs and Ethical Standards
- review progress against the findings contained within the report issued in relation to the outcomes from their second assessment of 2012/13 audits.

80. The work of ICAS provided positive assurance on many aspects of ASG's audits including:

- a well-documented knowledge and understanding of audited bodies
- well-performed and recorded assessment of systems and controls
- consideration of [ISA 240](#) (The auditor's responsibilities relating to fraud in an audit of financial statements) risks of revenue recognition and management override
- evidence of planning meeting and team briefings
- good reporting to committee, including planning and annual audit reporting with evidence of two-way communication
- substantive testing of income and expenditure transactions at interim and year end
- well-performed substantive testing of staff costs
- well-evidenced non-current asset testing, including testing of title to properties and valuation and impairment
- good assessment of trade receivables accuracy and recoverability
- consideration of work of an expert on valuer and actuary in compliance with [ISA 500](#) (Audit evidence)
- well-recorded review of financial statements disclosures, governance statement, remuneration report.

81. The ICAS review identified that there is “a reasonable level of compliance with the Auditing Standards, (but)... there were varying standards of audit quality across the files reviewed.”

82. The ICAS review made a number of recommendations that will be put in place ([paragraphs 86–87](#)). Many are about how existing audit procedures are applied and the adequacy of recording. Consistency in applying audit procedures will improve by establishing an even greater focus on staff training this year.

Developments in audit quality

83. The main area of development in the year was designing and introducing an approach to relying on auditors’ work where bodies used shared services. This was developed as a direct result of the introduction of Integrated Joint Board (IJB) audits and addresses one of the findings from current and previous ICAS reviews. In IJBs, the council and health board host all the IJB’s systems including general ledger, payroll and other payments systems (including care provision, general supplies, prescribing and Family Health Services). The approach and related audit programme has much wider application across the audits of public sector bodies.

84. An important development in ASG in 2015/16 was revising the audit training provided to teams. This included designing and introducing an additional two half-day training sessions to all audit staff to supplement the annual one-day training. The one-day event was delivered in January 2016 to almost all ASG staff and around 40 other staff drawn from across Audit Scotland. The additional events were delivered at superteam level. This involved groups of 25-45 staff at two rounds of six separate team meetings in November and April. Topics covered included:

- how to meet [ISA 230](#)  (Audit documentation) requirements within MKI
- introduction and audit approach to the audit of state aid
- our audit approach in our key planning file
- how we record and deal with matters arising from audit work
- the findings from our quality reviews
- final accounts issues
- how we evaluate audit errors.

85. During 2015/16, the Professional Standards and Quality Improvement (PSQI) Group revised the programme used to review audits. PSQI increased the number and coverage of reviews to reflect ICAS recommendations that all certifying auditors (28) should be reviewed over a three-year period and to ensure coverage of all sectors.

86. Following the internal and ICAS reviews ASG is committed to improving the following over-arching issues:

- More timely and evident review of key planning and completion files by the certifying auditor before important stages of the audit.
- Better standards of review by managers or lead senior auditors in files where proper evidence or documentation is lacking.
- Better recording of audit evidence by individuals in compliance with [ISA 230](#) (Audit documentation) and better recording of justifications for selecting samples and sizes.

87. ASG has established procedures to help ensure continuous quality during the transition to the new audit appointments in 2016/17. This includes:

- applying additional audit programmes in compliance with [ISA 510](#) (Initial audit engagements – opening balances)
- considering staff continuity on audits that are being retained by ASG (subject to the Ethical Standards' rotation principles)
- earlier formation of teams and responsibilities for the new audits
- developing wider handover procedures.

Performance Audit and Best Value

88. The Audit Management Framework applies to all types of audit work and is consistent with relevant INTOSAI standards. The Audit Management Framework has a three-stage structure of scoping, evidence gathering and reporting with a range of quality controls within each stage. Feedback on our work continues to be positive, but we continue to look for improvement.

89. The focus in the last year has been on maintaining the Audit Management Framework on an ongoing basis. The development of standards, cold review arrangements and further training will make sure that all staff can seamlessly move around the different types of audits.



Performance audit and Best Value

Lessons learned review and impact analysis (all)

Assurance to PABV that opportunities to improve audit processes, implement more effective methodologies and better understand how our work can make a difference are being identified.

Peer review (risk based)

Independent review and challenge on the appropriateness of selected performance audit topics, audit methodologies and the quality of audit reports.

Assistant director review (engagement lead) (All)

Assurance to engagement lead that the audit scope, approach and proposed reporting format is appropriate and reflects identified audit risks.

PABV Audit Management Framework

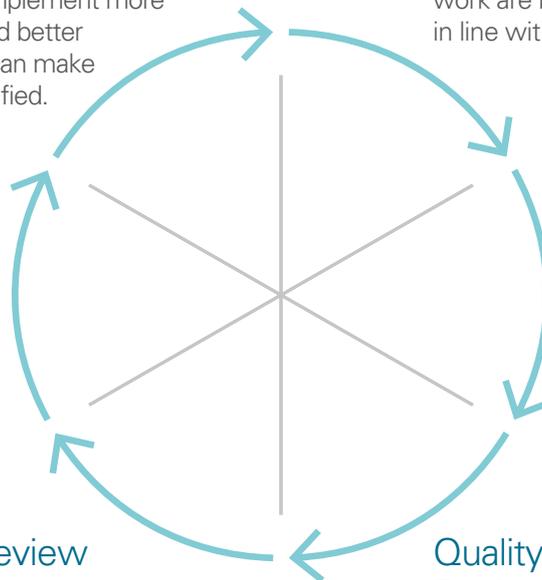
Assurance to PABV that all pieces of audit work are being managed consistently and in line with agreed QA and QC processes.

Senior managers' review (all)

Assurance to director/assistant director that work complies with audit guide and judgements are appropriate.

Quality and Consistency Review (QCRP) (Risk based for BV and CPP work) or audit advisory group (performance audit)

Assurance to PABV that work is proportionate, and risk based; audit judgements are consistent and recommendations will add value.



Senior manager and assistant director review

90. Senior managers and assistant directors reviewed the audit work for all the reports published in 2015/16. The reviews confirmed that the work had been done in accordance with the Audit Management Framework and quality arrangements and met their audit objectives.

Peer review

91. The Audit Management Framework contains requirements for internal and external peer reviews. Groups of staff from outside the immediate audit team comment on draft scoping documents and draft reports. This is a critical element in ensuring quality.

92. Performance Audit and Best Value (PABV) continues to participate in external peer review of performance audit reports with UK partner audit agencies. The report on [The Scottish Fire and Rescue Service](#)  was peer reviewed in 2015/16 by the Welsh and Northern Ireland Audit Offices. The findings were positive, with particular emphasis on the clarity of audit judgements, use of plain English, and the strength of the evidence base to support audit recommendations.

93. PABV provided peer review feedback on the Wales Audit Office audit reports on elective waiting times, managing the impact of welfare reform, and regional education consortia. A similar service was provided to the Northern Ireland Audit Office reports on the cross-border broadband initiative Bytel project, primary care prescribing and the Northern Ireland Events Company.

Lessons learned reviews and impact analysis

94. A few weeks after the completion of the majority of audits conducted by PABV (in 2015/16, three overview reports, eight performance audits, six Best Value audits), audit teams and senior management (including the director) conducted lessons learned reviews to assess how the audits were carried out and the short-term impact of the audits. These reviews include consideration of any divergence from the Audit Management Framework or whether there are any proposals for changes to it. These are then considered by the Quality Group.

Accounts Commission sponsor and Auditor General reviews

95. Where the Accounts Commission are report sponsors and reports are published by the Auditor General, the Accounts Commission obtain assurance directly through the report sponsors and the Auditor General as part of their arrangements to review planned work and final drafts of the reports. The Accounts Commission and Auditor General are integral to the quality processes in performance audits and overview reports. They sign off the scope, emerging messages and the final report. Learning points from these reviews are fed into the lessons learned reviews.

96. Members of the Accounts Commission met with representatives of six audited bodies following the publication of audit reports during 2015/16. The meetings focused on audit findings, the audited bodies' response to issues raised and feedback from the audited bodies on the audit process itself. That feedback has been positive and constructive.

Audit service quality survey results for local and central government

97. The audit service quality surveys that were issued to local government and central government bodies following the 2014/15 audits included questions on the value and impact of performance audit reports. The table below summarises their responses.

Did the report help with... (% agreeing with statement)	better understanding of financial sustainability	more transparent reporting of financial and other performance	our body providing better value for money	improved governance and financial management
Local government overview	100	91	95	100
Borrowing and treasury management	86	90	57	95
Community planning (local government)	80	75	74	95
School education	91	95	90	95
Self-directed support	85	81	81	90
Procurement in councils	95	89	90	95
Managing ICT contracts: follow-up	54	57	69	81
Community planning (central government)	60	60	60	60
Court efficiency	100	50	100	50

98. The service quality surveys also include free text comments from respondents. A sample of representative quotes is set out on [page 32](#).

A sample of representative quotes



"The report gives a very useful set of comparators against other local authorities in Scotland and is a very useful point of reference for how this council is performing"

An overview of local government in Scotland 2015, March 2015



"The overview report is an interesting report, however often the issues identified are well known to councils and are recurring issues"

An overview of local government in Scotland 2015, March 2015



"The report served the purpose of highlighting an area of finance where members required further assistance to understand and scrutinise Treasury Management decisions and information"

Borrowing and treasury management in councils, March 2015



"The report made general comments around how treasury management was operated within councils which didn't always reflect the good practice and professionalism that is in place"

Borrowing and treasury management in councils, March 2015



"The report has contributed to the ongoing educational approach to ensure that pupils get as good an education as possible and attain as much as they can in an appropriate educational setting"

School education, June 2014



"The report informed the council's revised raising attainment strategy"

School education, June 2014



"The report served to enhance members' awareness of the rationale for, and implications of, SDS in councils"

Self-directed support, June 2014



"The report was informative and provided some clarity around the issues of SDS which were particularly timely"

Self-directed support, June 2014



"The overview was helpful in placing the critical importance of improved procurement practices in its wider context"

Procurement in councils, April 2014



"The report allowed procurement to establish where the council had improved and helped confirm the direction for future improvement"

Procurement in councils, April 2014

99. Overall the results of the surveys suggest that satisfaction with performance audit reports is high.

Quality feedback from the Scottish Parliament's Public Audit Committee

100. The feedback received from the Public Audit Committee on the quality of Audit Scotland work has been consistently positive, as is shown by the following recent quotes from committee members:



"I want to thank, on the committee's behalf, Audit Scotland and the Auditor General for their hard work and professionalism over the past five years. Their reports and the evidence and the support that they have provided to us have, as I am sure that all members will agree, been invaluable. I am sure that our successors will be as grateful as we are for their good work"

Paul Martin, Public Audit Committee.



"The role of Audit Scotland has been phenomenally important in every committee that I have sat on throughout my 13 years in the Parliament – mainly on health committees, although I was on the Finance Committee at the beginning. Without Audit Scotland's reports, we could not provide the sort of scrutiny that we have been able to provide"

Dr Richard Simpson, Public Audit Committee.

Developments in audit quality

101. The PABV quality group separated from the impact group this year to reinforce the focus on maintaining the Audit Management Framework on an ongoing basis and better align the measurement of impact with the corporate focus on making a difference. During the year the quality group also:

- developed new arrangements for cold reviews of audit compliance with the Audit Management Framework
- considered how to integrate equalities more effectively within the Audit Management Framework
- began work to develop a set of standards applicable to all PABV-led audit work.

102. The focus during 2016/17 will remain primarily on maintaining the Audit Management Framework. This will be supported by:

- delivering training to all staff on using the Audit Management Framework, and the documentation of evidence and judgements
- completing the set of standards applicable to all PABV-led audit work
- finalising the cold review arrangements and begin using it as a core part of quality control arrangements.

Appendix: Quality arrangements

Quality arrangements for Audit Strategy

Audit Strategy carries out a quality appraisal function for all financial audits conducted under appointment by the Auditor General and the Accounts Commission by the firms and ASG. This work is described in detail in the Quality Appraisal Framework, which was approved in May 2012.

The principal objectives of the quality appraisal work are to:

- provide assurance to the Auditor General and the Accounts Commission on the quality of audit work undertaken
- promote improvements and good practices in auditing.

Audit Strategy carries out a number of activities in its monitoring role, for example:

- Review firms' and ASG's quality arrangements, including transparency reporting by firms.
- Review external assurance, in particular reports issued by the Financial Reporting Council on professional firms and monitor reports produced by The Institute of Chartered Accountants in Scotland.
- Review and assess the reports issued by auditors, giving feedback to auditors on examples of good practice and areas for improvement.
- Issue audit quality surveys to audited bodies in each sector every two years to ask them for their views and report these findings to auditors and our management team.
- Monitor that auditors completed all their audit work on time.
- Oversee acceptance by firms of non-audit work.
- Respond proportionately to complaints about auditors.
- Consider the impact of conflicting audit judgements by auditors.
- Independently review audits.

The results of these activities are reported in the 'Results of Quality Assurance Activity' section in the main body of this report.

The IAASB [A Framework for Audit Quality](#)  highlights the importance of access to high-quality technical support. Auditing requires knowledge of a considerable number of technical areas, including financial reporting, auditing standards, and legislation. The Technical Services Unit is a small team of technical specialists who keep financial auditors up to date with developments. The team also provides guidance and assistance on complex areas to inform auditors' judgements and support the exercise of professional scepticism.

None of the measures in place provides absolute assurance for any of the elements of the quality appraisal framework. However, we can never get absolute assurance and it is not the framework's aim to do this.

Appointed firms

All the appointed audit firms completed a detailed questionnaire setting out how their quality arrangements complied with [International Standard of Quality Control 1](#) (ISQC1) at the start of the five-year audit cycle in 2011/12. The firms and ASG also submitted details of how they would monitor the quality of the audits that they would carry out under their appointment by the Auditor General and the Accounts Commission.

All firms are required to obtain permission from Audit Strategy before they do any non-audit work for the audited bodies to which they have been appointed. They must also declare that they consider such work permissible under Ethical Standards. Non-audit work is only permitted where the work is consistent with Ethical Standards in the context of public sector audit. This review enhances the independence and ethical conduct of the audits.

During 2015/16 the firms under appointment from the Auditor General and the Accounts Commission completed the following 2014/15 audits:

Firm	Central government	Local government	Health	Further education	Total
KPMG LLP	9	11	-	4	24
PWC LLP	10	8	4	-	22
Scott-Moncrieff	-	2	7	5	14
Grant Thornton UK LLP	6	3	-	3	12
Deloitte LLP	1	5	3	-	9
Henderson Loggie	-	-	-	3	3
Wylie & Bisset LLP	-	-	-	4	4
Total	26	29	14	19	88

Quality arrangements for Audit Services (ASG)

ASG's framework covers financial audit, ethical and quality standards as required by the FRC. The foundation of ASG's quality framework is the ASG audit guide. This sets out the methodology used across all ASG audits and includes:

- how to apply professional audit, quality and ethical standards
- the Code of audit practice
- guidance notes on specific issues such as audit testing.

The Professional Standards and Quality Improvement group (PSQI) consists of staff members from across ASG and reports directly to ASG's management team. It oversees the development of the audit guide and the integration of any new standards into ASG's audit approach. The audit guide is kept under review and was most recently updated in June 2014.

Auditors are required to complete audit engagements using an electronic working paper package called MK Insight (MKI). This allows them to document their work to provide evidence that they are complying with relevant auditing standards. The package also builds in appropriate levels of supervision and management.

ASG carries out peer reviews in line with ISQC1 requirements to perform engagement quality control reviews for all audits meeting certain criteria. The criteria for selection include the level of fee income (size), assessed risk and where any modification to the audit opinion is expected.

The ASG Director, or assistant directors within ASG, carry out peer reviews before an audit report and certificate is issued. These reviews focus on identified audit risks, audit responses, and whether the evidence and judgements are adequate. The certifying auditor resolves any significant issues before issuing the auditor's report. Peer reviewers are not involved with the audit in the current or recent financial years, in line with ASG's rotation policy.

ASG operates a rotation policy that complies with the FRC's Ethical Standards. The policy is designed to reinforce auditor independence by rotating key senior staff every five years. This protects against threats to independence such as over-familiarity with management at an audited body. ASG staff must complete an annual fit and proper declaration that covers time they have spent on particular audits and confirms they have complied with Audit Scotland's Code of Conduct.

ASG's programme of reviews ensures that all the auditors who take the lead on financial audits are reviewed every three years by a subgroup of experienced PSQI staff. These are supplemented by periodic external reviews.

The managers and teams responsible for individual audits reviewed are provided with reports on the findings of the review. They respond to the findings in the report and this often results in improvement actions for each team.

As part of the review process, PSQI works with other UK audit agencies to give an independent view of ASG's work. The Northern Ireland Audit Office and the Wales Audit Office carry out a small proportion of ASG's reviews. Audit Scotland's staff provide reciprocal reviews.

These reciprocal reviews provide an opportunity to identify differences in approach among the UK audit agencies and bring back examples of good practice or challenge existing practices.

PSQI considers the findings from the reviews and identifies where changes to audit methodology, audit programmes and reporting are needed. These are then implemented by revising the audit guide, MKI audit programmes and reporting templates, and through specific training events and the Annual Audit Update.

All ASG staff must attend practitioner update sessions each year, along with further half-day sessions for smaller groups of staff. These update sessions provide training on changes to the audit guide, developments in auditing and professional standards and issues identified by quality reviews.

ASG management team and PSQI consider and respond to any reviews or reporting of audit approach or quality that Audit Strategy issues.

Quality arrangements for Performance Audit and Best Value (PABV)

Arrangements for managing the quality of performance audits draw on a comprehensive audit management framework (AMF). This covers each key stage of a performance audit from project selection, audit design, fieldwork and reporting through to post-audit review and impact assessment. The AMF is supported by the in-house performance audit manual and performance audit standards that comply with [INTOSAI standards](#). Staff also have access to a comprehensive library of good practice guidance to help them in their work.

The Quality Assurance Framework covers the following:

- Performance audits
- Best Value (BV) audit work
- The Shared Risk Assessment process
- Community Planning Partnership (CPP) audits
- Statutory reports (S102 or S22)
- Local government overview reports
- Reports in the '*How councils work*' series
- Statutory performance reporting
- Dealing with correspondence from the public, including MPs and MSPs.

A range of processes, procedures and guidance, including Best Value toolkits is also available to guide and direct staff when they are doing BV work. The [BV toolkits](#) are available on our website. This is to make our audit process clear and understandable and help audited bodies improve their performance.

All PABV's audit work includes internal and external peer review and challenge, and extensively uses independent external evaluation when major new audit developments are introduced, for example audits of Integration Joint Boards (IJBs). All audit teams carry out a review to identify any lessons learned following audit work to identify potential improvements to the audit process for future work. These are supplemented with reviews of project reviews. At these, common issues in post-project reviews are identified. These common issues are discussed alongside any potential improvements and solutions that can be introduced across the systems.

The Auditor General and the Accounts Commission are the main stakeholders for PABV reports. Both are involved at the planning and reporting stages of the work to provide input to help ensure that the audits are high quality and will meet their needs.

The Public Audit Committee (PAC) of the Scottish Parliament is a key stakeholder for:

- all the work that is done on behalf of the Auditor General
- the joint work that is done on behalf of the Auditor General and the Accounts Commission.
- PABV consults the PAC on performance audit work programmes. Staff in PABV work hard to ensure that audit reports provide the committee with the evidence that it needs to properly scrutinise the spending and performance of public bodies that fall within its remit.

Transparency and quality

Annual report 2015/16

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

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Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN

T: 0131 625 1500 E: info@audit-scotland.gov.uk 

www.audit-scotland.gov.uk 

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