



## Supplementary Guidance Note (SGN) 02

### Audit reporting issues

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#### About Supplementary Guidance Notes

Supplementary Guidance Notes (SGNs) are prepared and published by the National Audit Office (NAO) on behalf of the Comptroller and Auditor General (C&AG) who has power to issue guidance to auditors under Schedule 6 paragraph 9 of the Local Audit and Accountability Act 2014 (the Act). SGNs are prepared and published when the C&AG wishes to address a particular issue. SGNs are part of the full suite of Auditor Guidance Notes (AGNs) which as such constitute guidance to which local auditors must have regard under Section 20(6) of the Act. The guidance in SGNs supports auditors in meeting their requirements under the Act and the [Code of Audit Practice](#) published by the NAO on behalf of the C&AG.

The NAO issues Weekly Auditor Communications (WACs), and less frequently Special Auditor Communications (SACs) to local auditors to bring to their attention relevant information to support them in carrying out audit work. Whilst these are for information, they may draw attention to guidance that has been issued by the NAO on behalf of the C&AG in AGNs to which, as stated above, auditors must have regard. The NAO may also use SACs to clarify expectations in relation to interpretation of specific issues.

The firms that are local auditors under the Act may use these communications to update their own internal communications and reference tools.

SGNs are numbered sequentially and published on the NAO's website. Any new or revised SGNs are brought to the attention of local auditors through the WACs.

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The SGNs are designed to assist local auditors in forming their own understanding of the requirements of the Code. Auditors are required to have regard to SGNs, which means that they must take into account the guidance issued by the NAO, and, if they decide not to follow it, they must give clear (in the sense of objective, proper, and legitimate) reasons within audit documentation as to why they have not followed the guidance. SGNs are in no way intended as a substitute for the exercise of the independent professional skill and judgement of a local auditor in deciding how to apply the NAO's guidance or when providing explanations as to why guidance has not been followed.

Local auditors should not assume that SGNs are comprehensive or that they will provide a definitive answer in every case.



This Supplementary Guidance Note is relevant to all local auditors of local public bodies covered by the Local Audit and Accountability Act 2014 and the [Code of Audit Practice](#) (the Code) including auditors of NHS foundation trusts but except for auditors of smaller authorities. Guidance on auditors' work on value for money arrangements is published in AGN 03, considerations when exercising additional powers is published in AGN 04 and reporting is published in AGN 07.

## Introduction and context

This SGN has been issued to provide additional guidance to support external auditors when considering certain reporting issues currently relevant to their work under the Code. The additional guidance in Section A is issued in the context of the significant delays in completing local government audits. It aims to assist auditors in reporting more rapidly and more effectively given the delays. It does not however relieve auditors of their statutory obligations to reach a view of organisations' arrangements to secure value for money each year. In time the C&AG will look to rescind this guidance once more timely annual reporting of VFM commentaries is re-established.

While this SGN draws on some text from AGN 03 and AGN 07 to highlight a particular issue, the SGN still needs to be read in conjunction with AGN 03 and AGN 07. The SGN is not intended to apply indefinitely. It will be reviewed and updated and withdrawn when no longer required.

The SGN covers the following reporting issues:

- Section A: VFM arrangements commentaries covering more than one year
- Section B: Placing reliance on significant weaknesses in VFM arrangements identified by another external auditor
- Section C: VFM reporting considerations at demised NHS bodies

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## Section A: VFM arrangements commentaries covering more than one year

1. This section applies to audits where auditors have or will have completed their work on VFM arrangements for 2021-22 but have not yet issued a commentary for 2020-21. As VFM arrangements work is not completed under ISAs, the reporting framework is set out in the Code and AGNs 03 and 07.
2. The original expectation under the approach to VFM arrangements work set out in the 2020 Code was that auditors would follow an annual cycle of work, with more timely reporting on VFM arrangements, including issuing their commentary on VFM arrangements for local government by 30 September each year at the latest. Unfortunately, due to the on-going difficulties affecting the local audit market, and which [we reported on in March 2021](#), there remains a significant number of local government audits where even as auditors approach their 2021-22 audits, reporting on 2020-21 is not yet complete. The C&AG is issuing this supplementary guidance to enable auditors to issue a commentary on arrangements that covers more than one year in their 2021-22 Auditor's Annual Report. This provides auditors with an opportunity to report more efficiently and ensure that audited bodies get their commentary as quickly as possible.
3. This supplementary guidance is, however, being issued on a temporary basis only, with the expectation that auditors will return to issuing separate commentaries for each audit year as soon as possible. This guidance will be rescinded as soon as possible.
4. Paragraph 4.5 of the Code states that *"the auditor's annual report should bring together all of the auditor's work over the year. A core element of the auditor's annual report will be the commentary"*. However, the Code does not explicitly require a separate commentary for each individual financial year and, for example, AGN 03 permits auditors to issue a joint commentary as part of a combined Auditor's Annual Report where the auditor considers it to be appropriate, for example, a police and crime commissioner and chief constable.
5. Therefore, consistent with the Code and current practice in some circumstances under AGN 03, auditors may now issue a commentary covering more than one financial year where it is more efficient and effective in their judgement to do so. Such a commentary must cover the three specified reporting criteria and must state clearly, for each audit year covered by the commentary, whether or not significant weaknesses in VFM arrangements were identified. Auditors may, however, exercise their own judgement in determining the level of detail they consider to be appropriate to report, especially in relation to arrangements in place in 2020-21.
6. Given the requirement under 3.14 of the Code for the auditor to issue a recommendation in relation to a significant weakness in a body's arrangements, the



auditor should still raise a recommendation regarding any significant weaknesses identified under the 2020 Code, even if the auditor is satisfied that the weakness has since been addressed. The auditor can reflect, however, the status of the recommendation in their commentary on arrangements.

7. Nothing in this SGN removes the requirement as set out in Section 20 (1) of the Act for the auditor to be satisfied as to whether the body has proper arrangements in place to secure value for money in the use of its resources for each financial year. Auditors must therefore ensure they continue to report by exception significant weaknesses relating to each specific financial year in accordance with AGNs 03 and 07.

8. Auditors are also reminded that where they have identified significant weaknesses in arrangements in either 2020-21 or 2021-22, they should still be reporting them promptly to those charged with governance in accordance with paragraph 1.19 of the Code and paragraph 52 of AGN 03.

## Section B: Placing reliance on significant weaknesses in VFM arrangements identified by another external auditor

9. 2022-23 will see significant restructuring in the NHS commissioning sector with integrated care boards replacing clinical commissioning groups under the Health and Care Act 2022. Additionally, further NHS and local government reorganisation is possible, and the current PSAA procurement exercise may lead to changes in firms' audit portfolios. It is therefore likely that there will be a number of situations where a new auditor, or the auditor of a new body has to consider significant weaknesses in VFM arrangements that were reported by another external auditor. Paragraph 1.10 of the Code requires auditor's work to be "*risk-based and proportionate*", and paragraph 28 of AGN 03 already includes a principle that permits auditors to place reliance on the findings of inspectorates and other regulators.

10. Therefore, consistent with the principles of paragraph 28 of AGN 03, where another external auditor has raised a significant weakness in arrangements, the newly appointed auditor is not required to re-perform their work and should include the extant significant weakness as part of their VFM arrangements risk assessment. The newly appointed auditor will need to consider the body's response to the previously reported weakness in order to inform their commentary and judgements around exception reporting.

11. Where auditors are drawing on significant weaknesses identified by another external auditor, they should clearly identify that they are doing so in their commentary. The auditor should then go on to explain the application of their own judgement in respect of the current year. Paragraph 78 of AGN 03 only requires the auditor to report by exception where they consider that previously reported significant weaknesses have not been addressed. While paragraph 78 does not require auditors to repeat recommendations already made, it is ultimately for the newly appointed auditor/auditor of the successor body to determine whether they wish to report their own significant weaknesses and make associated recommendations.

12. While included in the SGN at present, the principles set out in above in this section will be incorporated into AGN 03 and or AGN 07 as appropriate when they are next updated.

## Section C: VFM reporting considerations at demised NHS bodies

13. AGN 03 paragraphs 84-91 includes the following guidance in relation to demising bodies:

*84. "It is possible that some audited bodies may demise part-way through or at the end of a financial year (for example, due to a reorganisation in the NHS).*

*85. For bodies that demise part way through a financial year, auditors are not required to perform the full programme of work set out in this AGN. The auditor is not required to undertake a full risk assessment specifically aimed at planning a programme of VFM arrangements work to support a full commentary on arrangements against the reporting criteria. However, should any significant weaknesses come to the auditor's attention they should still be reported by exception. Auditors will, therefore, need to assess if there are any risks of significant weakness arising from:*

- the auditor's wider work on the audit of the financial statements. Under the Code, and as set out in paragraph 7 in this AGN, there is an expectation of an 'integrated audit'. Therefore, for example, this could include identifying VFM arrangements risks that may be present in minutes covered by the minute review undertaken for audit work on the financial statements;*
- the auditor's understanding of the body and interactions with management and those charged with governance;*
- the status of significant weaknesses or, where previously reported, improvement recommendations; and*
- any other information brought to your attention, for example through correspondence with the public or reports in the media*

*86. If information from any of the areas listed above suggests there is a risk of a significant weakness in arrangements, the auditor may need to undertake further work to determine whether there is a significant weakness.*

*87. Paragraph 4.5 of the Code states "a core element of the auditor's annual report will be the commentary in accordance with the specified reporting criteria set out in Chapter Three (and as supplemented in statutory guidance issued by the NAO)." For bodies that demise part way through a financial year, the auditor's*

*commentary can be limited to setting out the approach as outlined above and confirming whether any significant weaknesses have come to the auditor's attention, including making any associated recommendations. Auditors may also choose to include improvement recommendations where they consider this to be appropriate.*

*88. Further guidance relating to the consideration of reporting at CCGs that demised on 30 June 2022 is contained within section C of SGN 02 Audit reporting issues 2021-22.*

*89. For bodies that demise at the end of a financial year, the Code requires auditors to include a commentary on arrangements in their Auditor's Annual Report in accordance with paragraph 26. The commentary should focus on whether or not any significant weaknesses were identified at the demised body but may also highlight any other findings that the auditor considers appropriate. Auditors therefore still need to undertake the work under this AGN to satisfy themselves as to whether or not any significant weaknesses existed. These should still be reported by exception and included in the Auditor's Annual Report which will be addressed to the successor body.*

*90. Where several bodies are demising and being merged into a single successor body, either part-way through or at the end of a financial year, each auditor may issue a combined Auditor's Annual Report covering all of the demised bodies that they audit.*

*91. Where the auditor identifies significant weaknesses at a demised body, the auditor should include them in their Auditor's Annual Report and note that it will be for the incoming auditor to consider whether the successor body has adequately considered the weaknesses reported and acted appropriately."*

14. Auditors will be aware that the Annex to AGN 03 currently allows for auditors to complete their VFM work and report their commentaries and Auditor's Annual Report to a later timetable than that required by the Code. As a result of these special provisions, and due to the demise of all CCGs as at 30 June 2022, auditors may find themselves in the position of having not yet issued their commentary on CCG VFM arrangements for 2021-22. Where this is the case, and consistent with the principles of paragraph 91 of AGN 03, auditors may elect to proceed as follows:

- a) If the auditor is reporting in the commentary significant weaknesses that were not previously drawn to the demised CCG's attention in relation to 2021-22, in drafting their commentary on 2021-22 arrangements, auditors may reflect the fact that the CCG has now demised and report the recommendation(s) to the successor integrated care board (ICB). The ICB can then consider whether the



recommendation(s) remains relevant and take action accordingly. This approach will also discharge the auditor's duty to bring significant weaknesses to the attention of audited bodies promptly, in this case, by notifying the ICB at the earliest reporting opportunity.

- b) The auditor may have previously reported significant weaknesses and made recommendations to the CCG in 2021-22, but not yet completed their commentary on arrangements by the time the CCG demised on 30<sup>th</sup> June. Where this is the case, the auditor should reflect the fact in their reporting to the successor body that they have previously reported the issues to the CCG (where the audit report was issued up to 30<sup>th</sup> June). It will be for the successor body to consider whether any recommendations remain relevant and take action accordingly.

15. Auditors should note however that nothing in this SGN changes the auditor's duties in respect of being satisfied about arrangements to secure VFM at a demising body. Therefore, for the CCG part-year 2022-23 (three-month period 1 April to 30 June 2022), auditors should continue to report significant weaknesses by exception and include them in their CCG 2022-23 Auditor's Annual Report as required by AGN 03 and AGN 07.

16. Auditors are also reminded that, should they identify any new significant weaknesses relating only to the CCG part-year period, they should report these weaknesses to the relevant ICB as successor body at the earliest opportunity. Auditors should not wait to include them in their 2022-23 audit report or their Auditor's Annual Report and certificate.



## Other support and raising technical issues or queries on this SGN

17. Auditors in firms should raise queries within the firm, in the first instance, so that the relevant technical support service can consider whether to refer queries to the NAO's Local Audit Code and Guidance (LACG) team by e-mailing [LACG.queries@nao.org.uk](mailto:LACG.queries@nao.org.uk).

18. Information supporting auditors is available on the LACG extranet. This includes details of third-party reports and information. Copies of referenced third party information and service auditor reports will also be available on the LACG extranet following issue. Updates will be communicated through the Weekly Auditor Communication (WAC). If there is a need for further statutory guidance during the year, the NAO may issue an addendum to this SGN.

19. The NAO also engages with the firms through its Local Auditors' Advisory Group (LAAG) and supporting technical networks to consider any emerging regime-wide technical issues on a timely basis. Auditors should follow their in-house arrangements for bringing significant emerging issues to the attention of their supplier's representative on LAAG or the relevant technical network.